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AFTER WORK
By Moira Herbst

Can Bunnies Get Playboy Hopping Again?

Playboy has a new upscale club in Sin City—and high hopes that licensing casinos and expanding its video downloads will boost its financial fortunes

The Bunnies are ready. So are the croupiers and blackjack dealers. And there's even a "Hugh Hefner Sky Villa" complete with a replica of Hef's signature rotating bed. On Oct. 6, Playboy Enterprises (**PLA**), in partnership with the Palms Casino Resort and nightspot chain N9NE Group, will unveil its new Playboy Club casino in Las Vegas, alongside a smaller Playboy-themed penthouse club and Italian restaurant. The venture is designed to bring the Playboy Mansion ambiance beyond L.A. No invitation is needed, though the cover charge is $40.

The club experience "creates a sense you're going to the coolest party," says Christie Hefner, Playboy's chairman and chief executive. "It's the closest some people will [get to] the Playboy Mansion." (See BusinessWeek.com, 10/19/05, **"A Day's Work at the Playboy Mansion"**.)

Indeed, Christie is struggling to put the company her father founded in 1953 back on solid financial footing. Playboy has been only sporadically profitable in recent years. Advertising revenues for its flagship magazine were down 16% in the second quarter, compared to the same period a year earlier, and are expected to drop 17% in the third quarter. In the last year, the Chicago company's stock has tumbled 30%, to less than $10 a share. Now, Christie and Hef are betting that the Las Vegas club and similar licensing ventures can return the company to profitability and growth.

REVIVING THE CHAIN. The new club is a reinvention of the members-only ones Hugh Hefner started opening in 1960. That chain, which required special key access for gentlemanly lounging among the scantily clad Bunnies, closed its last club in 1991.

The Playboy Club is the main venue at the Palms, and guests also will have access to Moon Nightclub, a VIP penthouse spot with a retractable roof. The licensed venues are housed on the top three floors of the 347-room Fantasy Tower in the $915 million resort, which is operated by casino mogul George Maloof Jr. The project was developed by the N9NE Group, which owns bars and restaurants in Chicago, Dallas, and Las Vegas.

The difference between the Palms club and the clubs of yesteryear, Playboy says, is that the new venture will combine lounging and immersion in all things Playboy with gambling. Previously, Nevada law prohibited clubs from charging a cover to access gambling tables.

Christie Hefner says she expects the club to reinvigorate the brand while boosting the bottom line: "We're bringing in a completely different business model since we're able to include gaming with food and beverage," she says. "It's no surprise that the most successful clubs have done just that."

The company expects revenues of $4 million per year from the Palms, says a Playboy spokesperson. An undisclosed amount is guaranteed by the partnership, with the remainder to be generated through royalties. That should help Playboy's share price, says Lucas Binder, an analyst at UBS (**UBS**), who also says the deal could lift the stock 10 cents per share. Shares closed at $9.90 on Oct. 5, well below a 52-week high of $15.88 reached last November.

RETAIL LICENSING. The Palms isn't Playboy's first foray into Vegas. Playboy opened its first U.S. retail store five months ago at the nearby Caesars shopping gallery. The 2,000-square-foot store, owned and operated under a license with the Waikiki Trader Group, offers Playboy apparel, accessories, and lingerie. Alex Vaickus, Playboy's president of licensing, believes the company hasn't maxed out on licensing opportunities in lifestyle and entertainment products. A Playboy fragrance could be next.

The company also hopes *The Girls Next Door*, a series featuring Hef and three blond girlfriends launched last fall on E! Entertainment network (**DIS** , **CMCSA** , **LCAPA**), will give the brand more exposure to a younger, hipper demographic.

After two losing quarters this year, Playboy Enterprises needs to add some life to its party, and licensing may be a good place to look. Licensing offers higher margins than either entertainment or publishing. Last year, the licensing division earned the company $16 million, though that strong performance wasn't enough to offset trouble in other divisions. One of these divisions was publishing, which swung to a $6.5 million loss last year from a $6.2 million profit in 2004. Playboy lost $700,000 last year, after posting net income of $9.6 million in 2004.

This year, things aren't looking much better. The company lost $3.3 million in the second quarter, with the big disappointment being the entertainment group's decline in income to $4.9 million, vs. $9.8 million for the same period last year. The drop was largely due to the loss of exclusivity on DirecTV (**DTV**), plus increased competition on cable for the Playboy and Spice channels, and an industry shift to more video-on-demand services.

"GOOD, CLEAN FUN." That's why Playboy is hoping its brand recognition will spur success in other areas. The strategy is to ensure that the original Bunny ears symbol, which conjures Hef-style high living, means something for the aspirational young-bachelor set. "The brand still resonates very highly and has multiple meanings," says Robert Passikoff, president and chief executive officer of Brand Keys, a customer-loyalty research firm in New York. According to Passikoff, Playboy is " all-American, good, clean fun—including sex."

Playboy's Vaickus says the company has always taken pride in "being on the leading edge of culture, but we are a mainstream brand as well." Today's consumers see brands more as lifestyles than products, according to Vaickus, which is why the multifaceted Palms project will resonate. "The consumer is very much involved in interactivity," he says. "They won't settle for just one medium."

BRAND EQUITY. According to Christie, London and Macao are priority locations to license more entertainment venues, with other cities in Europe and Asia possibilities down the line. Another expanding area is digital content: digital video downloads from the Playboy library are the company's fastest-growing entertainment product, she says.

Although UBS' Binder expects Playboy to lose 5 cents per share for the third quarter, mainly due to the Spice and Playboy channels, he thinks "the Palms—and the money it will bring in— will get investors focused on Playboy again. "That $4 million in annual revenue will start hitting the income statement—it's what they've been waiting for."

Still, $4 million more in licensing revenues won't fill the growing income gaps in the publishing sector, and the company may face an even greater challenge if the entertainment group continues to stumble. Entertainment is Playboy's heaviest income segment, and if the company can't make a successful transition from its regular cable offerings to video-on-demand, it could continue to face hard times.

Will Bunny ears still hold their allure amid mounting magazine losses? Passikoff, for one, thinks Hef's somewhat ancient empire isn't ready to fall just yet—even with changing consumer demands. "The magazine isn't there to make money," Passikoff says. "Even if there were no magazine the brand would stay alive—it has an equity of its own."

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