

May 20, 2018 10:38 PM GMT

## NagaCorp

# FCF Declines Immediately with Bond Offering; Positive EBITDA Impact to Be Visible Later

Stock Rating  
Equal-weight

Industry View  
Attractive

Price Target  
HK\$8.10

New bond offering should help NagaCorp in the long run, but in the near term higher interest expense drives our FCFE and PT lower. Retain EW.

## WHAT'S CHANGED?

NagaCorp (3918.HK)	From:	To:
Price Target	HK\$8.50	<b>HK\$8.10</b>

**Investment conclusion:** We remain positive on the growth prospects of the Cambodia gaming industry as China BRI investment drives the local economy and booming Chinese outbound tourism. NagaCorp, with its monopoly gaming license in Phnom Penh, is the key beneficiary, but valuation at 1SD higher than long-term average is keeping us at EW.

In May 2018, NagaCorp raised US\$290m through bond offering, which is significant for the company in many ways. The new route to access capital (hitherto not available to NagaCorp) will support future growth regionally and locally. However, high interest rate of 9.375% could mean annual interest expense of US\$28m (9% of 2017 EBITDA and 11% of net profit). Use of proceeds (US\$150m for Naga1 renovation over the next 24 months and another US\$150m for VIP business) may not drive our 2018/19 EBITDA estimates (currently 39% and 22%, respectively, due to Naga 2 ramp) in the near term. The current gearing is 1x gross debt/EBITDA.

While the stock is trading at a discount to Macau comparables and has higher growth prospects and longer license period, it has already re-rated in the last year from 9x to 13x forward P/E. If the company does not receive US\$60m of additional income in 2018 from slot machine agreement (as in previous years), the P/E multiple could be 18.6x on our 2018 estimate. We would turn positive if we were to see incremental cash that could drive further growth, and if we had more clarity on taxation and setting up of casino regulatory authority.

**What's changed:** We reduced our VIP estimates due to delay in start of Macau Junket Meg-Star to 3Q (previously 2Q), but raised mass revenue forecast due to strong Chinese visitation growth (82% YoY in 1Q18). We cut our FCFE estimates by 4% and 6% due to additional interest expenses of US\$15mn and US\$28mn in 2018/19. We remain EW and cut our PT to HK\$8.10 (from HK\$8.50), based on 8% FCFE yield on 2019 estimates (unchanged).

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## NagaCorp ( 3918.HK, 3918 HK )

ASEAN Gaming / Hong Kong

Stock Rating	Equal-weight
Industry View	Attractive
Price target	HK\$8.10
Shr price, close (May 18, 2018)	HK\$7.66
52-Week Range	HK\$8.63-3.29
Sh out, dil, curr (mn)	4,341
Mkt cap, curr (mn)	US\$4,236
Avg daily trading value (mn)	HK\$33

Fiscal Year Ending	12/17	12/18e	12/19e	12/20e
ModelWare EPS (US\$)	0.059	0.051	0.078	0.086
Prior ModelWare EPS (US\$)	-	0.068	0.084	0.094
Revenue, net (US\$ mn)	956	1,373	1,737	1,910
EBITDA (US\$ mn)	320	325	462	505
ModelWare net inc (US\$ mn)	255	223	337	373
P/E	13.2	19.0	12.6	11.4
P/BV	3.3	2.9	2.6	2.4
RNOA (%)	21.1	15.1	20.9	21.7
ROE (%)	20.4	16.1	23.0	22.9
EV/EBITDA	14.0	13.1	9.0	7.9
Div yld (%)	4.6	3.2	4.8	5.3

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework

e = Morgan Stanley Research estimates

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## Financial Summary

## Exhibit 1: NagaCorp: Financial Summary

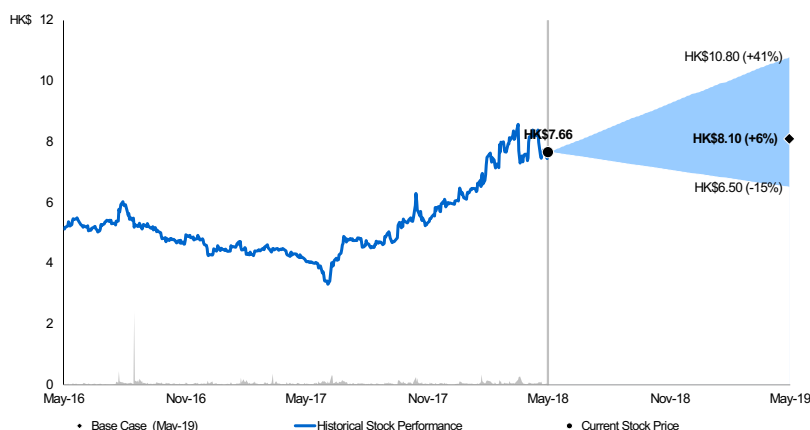
For the years ending December 31

Income Statement					Cash Flow Statement				
US\$ million	2017	2018E	2019E	2020E	US\$ million	2017	2018E	2019E	2020E
<b>Revenue</b>	<b>956</b>	<b>1,373</b>	<b>1,737</b>	<b>1,910</b>	<b>Profit before Tax</b>	<b>263</b>	<b>240</b>	<b>367</b>	<b>404</b>
VIP Revenue	625	976	1,205	1,329	Depreciation & Amortization	56	84	95	102
Mass Revenue	150	220	259	281	Other non-cash adjustments	(7)	(3)	(3)	(3)
EGM Revenue	151	117	200	224	Changes In Working Capital	10	(0)	(11)	(4)
Non-Gaming Revenue	30	62	73	77	<b>Operating cash flows</b>	<b>322</b>	<b>322</b>	<b>449</b>	<b>499</b>
Cost of sales	(483)	(757)	(934)	(1,029)	Capex	(355)	(220)	(170)	(70)
<b>Gross profit</b>	<b>473</b>	<b>617</b>	<b>804</b>	<b>881</b>	Others	0	-	-	-
VIP	154	239	295	326	<b>Investing cash flows</b>	<b>(355)</b>	<b>(220)</b>	<b>(170)</b>	<b>(70)</b>
Mass	145	213	252	273	Dividends Paid	(126)	(142)	(176)	(217)
EGM	149	114	197	220	Issuance of shares	-	-	-	-
Non-Gaming	25	50	60	62	Others	-	-	-	-
Administrative expenses	(67)	(99)	(113)	(125)	<b>Financing cash flows</b>	<b>(126)</b>	<b>134</b>	<b>(200)</b>	<b>(241)</b>
Other operating expenses	(86)	(127)	(145)	(160)	<b>Change in Cash</b>	<b>(158)</b>	<b>236</b>	<b>78</b>	<b>188</b>
<b>EBITDA</b>	<b>320</b>	<b>325</b>	<b>462</b>	<b>505</b>	<b>Ending cash</b>	<b>53</b>	<b>289</b>	<b>367</b>	<b>555</b>
Depreciation	(53)	(81)	(91)	(98)					
Amortization of license	(4)	(4)	(4)	(4)					
<b>EBIT</b>	<b>263</b>	<b>240</b>	<b>367</b>	<b>404</b>	<b>Ratios</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
<b>Profit before tax</b>	<b>263</b>	<b>227</b>	<b>342</b>	<b>380</b>	Current ratio	2.0	3.5	3.6	4.5
Income Tax	(8)	(3)	(3)	(3)	Gross Profit Margin%	49%	45%	46%	46%
<b>Profit after tax</b>	<b>255</b>	<b>224</b>	<b>340</b>	<b>378</b>	- VIP	25%	25%	25%	25%
<b>EPS (HK cents)</b>	<b>61.6</b>	<b>40.0</b>	<b>60.7</b>	<b>67.4</b>	- Mass	97%	97%	97%	97%
<b>DPS (HK cents)</b>	<b>27.4</b>	<b>24.0</b>	<b>36.4</b>	<b>40.5</b>	- EGM	99%	98%	98%	98%
					- Non-gaming	81%	81%	81%	81%
					EBITDA Margin%	33%	24%	27%	26%
					Net Margin%	27%	16%	20%	20%
					Dividend Payout Ratio (total)	60%	60%	60%	60%
					EBITDA to operating CF	99%	101%	103%	101%
					GGR Growth	85%	42%	27%	10%
					VIP Growth	177%	56%	24%	10%
					Mass Growth	15%	47%	18%	8%
					EGM Growth	4%	-23%	71%	12%
					EBITDA Growth	25%	2%	42%	9%
					Net Profit Growth	39%	-12%	52%	11%
					<b>Operating Data</b>				
					VIP Tables (avg)	229	256	263	263
					Mass Tables (avg)	112	141	146	146
					EGM Machines (avg)	1,949	2,500	3,000	3,500
					VIP win/table/Day (US\$)	7,498	10,461	12,553	13,808
					Mass win/table/Day (US\$)	3,679	4,267	4,864	5,254
					EGM win/unit/Day (US\$)	201	201	201	201
					Visitors to Cambodia (m)	5.6	5.9	6.2	6.5

Source: Company data, Morgan Stanley Research. E=Morgan Stanley Research estimates

**Risk Reward**

## Upside driven by capacity expansion in Cambodia

**Price Target** **HK\$8.10**

Base case, target yield of 8% based on 2019e FCFE.

**Bull** **HK\$10.80**

**6.0% recurring FCFE yield 2019e**

Stronger visitation growth; quicker than expected ramp of Naga2.

**Base** **HK\$8.10**

**8.0% recurring FCFE yield 2019e**

Continued Naga2 ramp in 2018/19. VIP revenue growth of 56% in 2018 and 24% in 2019; mass revenue growth of 47% in 2018 and 18% in 2019.

**Bear** **HK\$6.50**

**10.0% recurring FCFE yield 2019e**

Downturn in overall economy, more competition from Vietnam, reduced visitation, and slower than expected Naga2 ramp.

**Why Equal-weight?**

- Capacity expansion in Naga 2.
- China's Belt and Road Initiative (BRI) and Cambodia's China Ready strategy to attract Chinese visitors, driving strong VIP and mass earnings.
- Valuation is fair but not compelling, trading at 9% FCFE yield, 9x EV/EBITDA, and 12x P/E on our 2019 estimates.

**Key Value Drivers**

- Visitors growth, especially from China
- VIP roll, driven by new junket additions (Suncity on 1 March 2018 and Meg-Star in 3Q18)
- Naga2 boost with at least 300 tables, 903 rooms, 2,500 slots and additional non-gaming areas

**Potential Catalysts**

- Stronger than expected earnings growth in 2018
- Meg-Star opening in 3Q18
- Removal of overhang with respect to tax rate in Cambodia in 2H18

**Risks to Achieving Price Target**

- **Downside:**
  - Political uncertainty or tax rate changes
  - Potential share dilution for future developments and expansion
  - Regional competition (e.g., Vietnam, Philippines, Korea, Macau, Singapore)
- **Upside:**
  - Faster ramp of Naga2
  - Dividend increase

## What's changed

**VIP revenue** - We revised down our 2018e VIP revenue by 3% due to the delay of Macau junket Meg-Star, which will now kick in from 3Q18 vs. 2Q18 previously. We also lower our VIP table assumptions by 3% and 6% in 2018 and 2019. However, we expect VIP to grow faster in 2019 as higher cage capital allows bigger players at Naga. Company could also extend more credit to notable junkets like Suncity. Our 2019 VIP revenue estimate rises 2% vs. last publish.

**Mass revenue** - We have raised our mass revenue forecasts by 4% and 2% in 2018 and 2019, supported by continued strong Chinese visitation to Cambodia. Chinese visitors grew by 82% YoY in 1Q18, and we believe that our estimate of 13% p.a. growth through 2020 in our [initiation report](#) is achievable. We also revised our mass table assumptions down by 15% and 26% in 2018 and 2019, partially reflecting the renovation of Naga1. However, we expect higher mass table yield driven by strong demand.

**EBITDA and FCFE** - We have increased our EBITDA estimates by 1-2% in 2018/19 accordingly while we have tweaked free cash flow down by 4% and 6% due to additional interest expenses of US\$15mn and US\$28mn in 2018 and 2019 from the new bond issuance. Some of these are compensated for by interest income generated from extra cash which may not be used immediately.

**MSe vs. Consensus** - Our revenue forecast is in line with consensus in 2018 and 6% ahead of the market for 2019. Our EBITDA (before gaming tax adjustment) forecasts remain ahead of consensus by 6-9% in 2018 and 2019. While consensus has incorporated 5% gaming tax (as we have), it has added that below the EBITDA line, and thus our EBITDA estimates are not directly comparable. Our net profit estimates are below consensus by 1-6%, since we have incorporated interest expense from the new bond offering, while consensus has not.

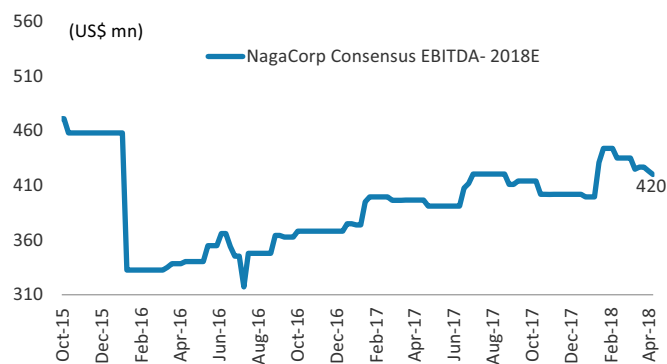
**Exhibit 2:** Earnings estimate revisions and comparisons with consensus

US\$ mn	MS			YoY growth			Consensus		Variance	
	2017	2018E	2019E	2017	2018E	2019E	2018E	2019E	2018E	2019E
Revenue	956	1,433	1,737	80%	50%	21%	1,431	1,640	0%	6%
EBITDA	320	377	462	25%	18%	23%	420	501	-10%	-8%
EBITDA before gaming tax adj.	320	445	546	25%	39%	22%	420	501	6%	9%
Net Income	255	277	340	39%	8%	23%	295	350	-6%	-3%
EPS (US cents)	7.9	6.4	7.8	1%	-20%	23%	6.8	7.9	-6%	-1%

US\$ mn	New			YoY growth			Old		Variance	
	2017	2018E	2019E	2017	2018E	2019E	2018E	2019E	2018E	2019E
Revenue	956	1433	1737	80%	50%	21%	1,458	1,704	-2%	2%
EBITDA	320	377	462	25%	18%	23%	374	455	1%	2%
Net Income	255	277	340	39%	8%	23%	295	367	-6%	-7%
EPS (US cents)	7.94	6.37	7.83	1%	-20%	23%	6.79	8.45	-6%	-7%

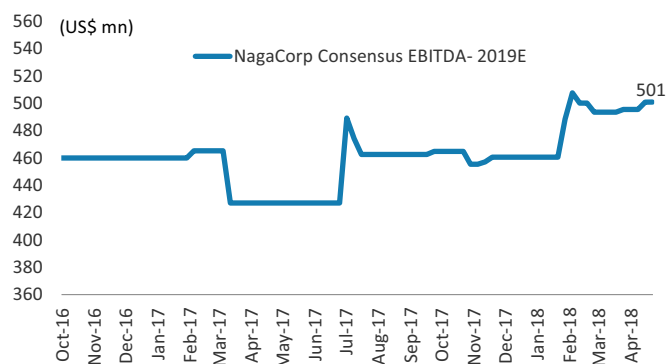
Source: Thomson Reuters, Morgan Stanley Research (E) estimates

**Exhibit 3:** Consensus 2018e EBITDA revision history



Source: Thomson Reuters

**Exhibit 4:** Consensus 2019e EBITDA revision history



Source: Thomson Reuters

**Exhibit 5:** Operating estimate changes

US\$ mn	New			Old		New vs. Old	
	2017	2018E	2019E	2018E	2019E	2018E	2019E
<b>VIP revenue</b>	625	976	1,205	1,008	1,176	-3%	2%
<b>Mass revenue</b>	150	220	259	212	255	4%	2%
<b>EGM revenue</b>	143	184	220	184	220	0%	0%
<b>GGR</b>	<b>918</b>	<b>1,379</b>	<b>1,685</b>	<b>1,403</b>	<b>1,651</b>	-2%	2%
<b>Tables (average)</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2018E</b>	<b>2019E</b>	<b>2018E</b>	<b>2019E</b>
VIP tables	229	256	263	264	280	-3%	-6%
Mass tables	112	141	146	166	196	-15%	-26%
EGM machines	1,949	2,500	3,000	2,500	3,000	0%	0%
<b>Productivity (US\$)</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2018E</b>	<b>2019E</b>	<b>2018E</b>	<b>2019E</b>
VIP w/t/d	7,498	10,461	12,553	10,461	11,507	0%	9%
Mass w/t/d	3,679	4,267	4,864	3,495	3,564	22%	36%
EGM w/u/d	201	201	201	201	201	0%	0%

Source: Morgan Stanley Research estimates (E)

# Valuation

We remain EW and cut our PT to HK\$8.10 (from HK\$8.50), based on 8% FCFE yield on 2019 estimates, above the Macau peers' average of 6.0%. Our 8% target FCFE yield is below the long-term average of 13% since 2011 in view of NagaCorp's monopoly position in Phnom Penh in the fast-growing market of Cambodia, as well as its stable dividend and tax profile.

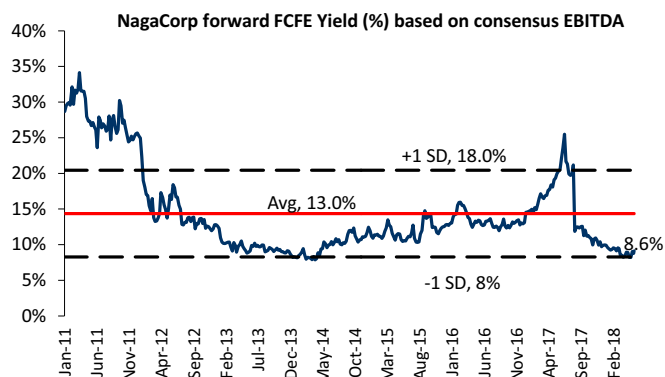
Our price target implies 10x 2019e EV/EBITDA, similar to those for other regional casinos under our coverage (Bloomberg at 10x).

**Exhibit 6: FCFE Valuation and multiples**

FCFE Valuation				
FCFE Valuation (US\$ mn)	2017	2018E	2019E	2020E
Company EBITDA	320	377	462	505
Less: Income tax*	(8)	(3)	(3)	(3)
Less: Maintenance Capex	(50)	(70)	(70)	(70)
Less: Interest Expense		(15)	(28)	(28)
<b>FCFE</b>	<b>262</b>	<b>289</b>	<b>362</b>	<b>405</b>
Target FCFE Yield			8.0%	
Equity Value	3,270	3,614	4,520	5,058
Number of shares			4,341	
<b>Price Target (HK\$)</b>			<b>8.10</b>	
Upside/downside			9%	
Current multiples				
	2017	2018E	2019E	2020E
EV/EBITDA	12.9	11.0	8.8	7.7
P/E	16.4	15.1	12.3	11.1
Recurring FCFE Yield	6.3%	6.9%	8.7%	9.7%
Div Yield%	3.7%	4.0%	4.9%	5.4%

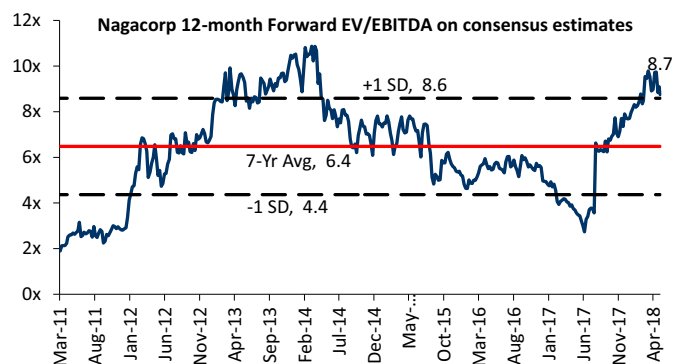
Source: Thomson Reuters data (as of 17 May 2018), Morgan Stanley Research (E) estimates.

**Exhibit 7: NagaCorp forward FCFE yield (%) based on consensus EBITDA**



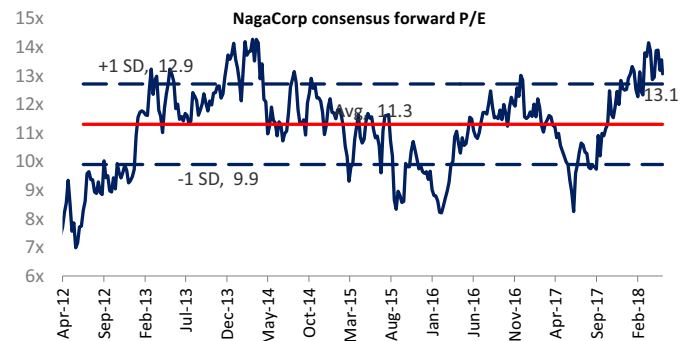
Source: Thomson Reuters data (as of 17 May 2018), Morgan Stanley Research (E) estimates.

**Exhibit 8: NagaCorp 12M forward EV/EBITDA on consensus estimates**



Source: Thomson Reuters data (as of 17 May 2018), Morgan Stanley Research (E) estimates.

**Exhibit 9: NagaCorp 12M forward P/E on consensus estimates**



Source: Thomson Reuters data (as of 17 May 2018), Morgan Stanley Research (E) estimates.

Exhibit 10: Valuation comps – Macau vs. NagaCorp

17-May-18	Current		6M Avg Vol. (US\$ m)	EV/EBITDA		P/E		Recurring FCFF Yield		Recurring FCFE Yield		Div Yield		Net Debt / EBITDA		2017 Perf.	2018 YTD Perf.
	Price LOC\$	Mkt Cap (US\$ m)		2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E		
<b>MACAU</b>																	
Sands China	46.85	48,215	81	17.4	16.4	21.3	20.0	5.0%	5.4%	5.1%	5.5%	4.6%	4.9%	1.2	1.2	20%	16%
Galaxy	67.05	36,882	106	14.8	13.0	20.6	18.0	6.5%	7.4%	5.9%	6.7%	1.5%	1.7%	(1.9)	(1.7)	87%	7%
Wynn Macau	29.20	19,331	43	14.9	13.4	20.6	17.9	6.4%	7.0%	6.5%	7.2%	4.9%	5.6%	1.6	1.3	101%	18%
MGM China	22.55	10,916	27	17.1	10.7	33.8	17.2	5.2%	8.7%	5.1%	8.3%	2.5%	4.9%	1.6	0.2	47%	-5%
SJM	9.05	6,523	18	12.4	13.5	20.9	20.9	7.2%	6.7%	6.4%	6.7%	2.8%	2.8%	(0.6)	1.8	15%	29%
<b>Simple average</b>				<b>15.3</b>	<b>13.4</b>	<b>23.5</b>	<b>18.8</b>	<b>6.1%</b>	<b>7.0%</b>	<b>5.8%</b>	<b>6.9%</b>	<b>3.2%</b>	<b>4.0%</b>	<b>0.4</b>	<b>0.5</b>	<b>54%</b>	<b>13%</b>
<b>ASEAN Gaming</b>																	
Genting Singapore	1.32	11,897	28	10.3	9.9	20.7	19.8	7.5%	7.8%	5.7%	5.9%	2.7%	2.7%	(2.5)	(2.7)	45%	1%
Bloomberry	12.98	2,734	3	11.3	9.4	19.7	20.5	7.8%	9.5%	7.1%	7.6%	0.5%	0.5%	2.2	1.3	77%	19%
NagaCorp	7.45	4,120	5	10.8	8.6	14.4	11.9	7.3%	9.3%	7.1%	8.8%	5.4%	6.8%	(0.1)	(0.3)	138%	23%
<b>Simple average</b>				<b>10.8</b>	<b>9.3</b>	<b>18.3</b>	<b>17.4</b>	<b>7.5%</b>	<b>8.9%</b>	<b>6.7%</b>	<b>7.4%</b>	<b>2.9%</b>	<b>1.6%</b>	<b>(0.2)</b>	<b>(0.5)</b>	<b>87%</b>	<b>14%</b>
<b>Global average</b>				<b>12.1</b>	<b>10.7</b>	<b>22.3</b>	<b>18.3</b>	<b>6.3%</b>	<b>7.2%</b>	<b>6.1%</b>	<b>7.1%</b>	<b>3.0%</b>	<b>3.1%</b>	<b>0.9</b>	<b>0.7</b>	<b>48%</b>	<b>5%</b>

Source: Thomson Reuters data (as of 17 May 2018), Morgan Stanley Research (E) estimates

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(as of April 30, 2018)

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STOCK RATING CATEGORY	COVERAGE UNIVERSE		INVESTMENT BANKING CLIENTS (IBC)			OTHER MATERIAL INVESTMENT SERVICES CLIENTS (MISC)	
	COUNT	% OF TOTAL	COUNT	% OF TOTAL IBC	% OF RATING CATEGORY	COUNT	% OF TOTAL OTHER MSC
<b>Overweight/Buy</b>	<b>1168</b>	<b>38%</b>	<b>305</b>	<b>40%</b>	<b>26%</b>	<b>550</b>	<b>39%</b>
<b>Equal-weight/Hold</b>	<b>1337</b>	<b>43%</b>	<b>371</b>	<b>49%</b>	<b>28%</b>	<b>641</b>	<b>46%</b>
<b>Not-Rated/Hold</b>	<b>53</b>	<b>2%</b>	<b>5</b>	<b>1%</b>	<b>9%</b>	<b>7</b>	<b>0%</b>
<b>Underweight/Sell</b>	<b>539</b>	<b>17%</b>	<b>83</b>	<b>11%</b>	<b>15%</b>	<b>207</b>	<b>15%</b>
<b>TOTAL</b>	<b>3,097</b>		<b>764</b>			<b>1405</b>	

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months. Due to rounding off of decimals, the percentages provided in the "% of total" column may not add up to exactly 100 percent.

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**Overweight (O).** The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

**Equal-weight (E).** The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

**Not-Rated (NR).** Currently the analyst does not have adequate conviction about the stock's total return relative to the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

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Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

### Analyst Industry Views

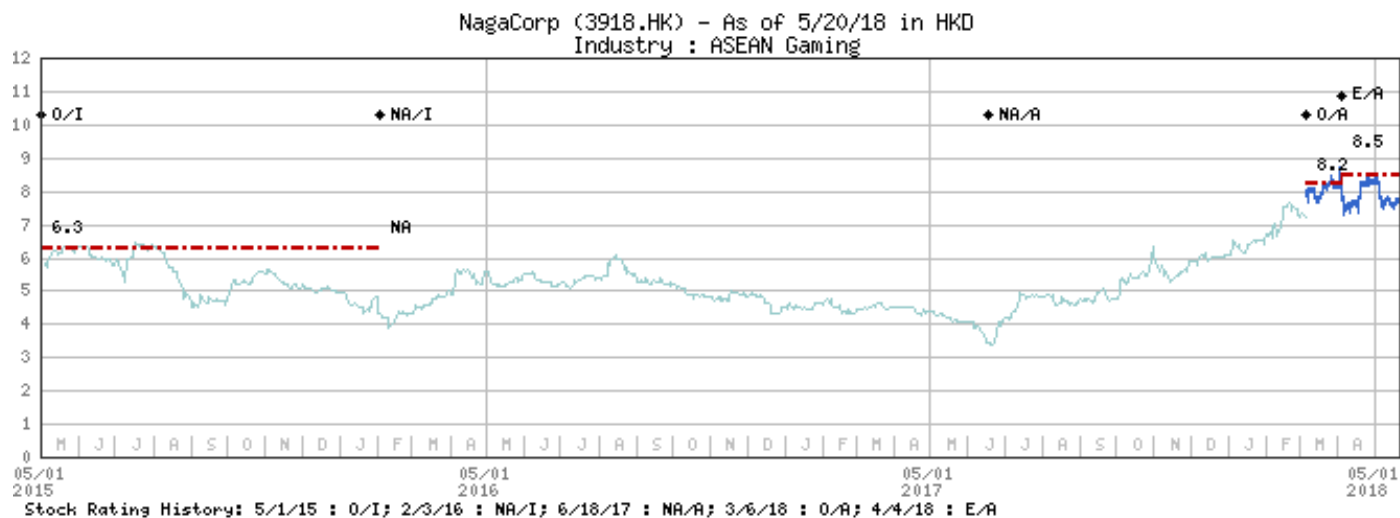
**Attractive (A):** The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.

**In-Line (I):** The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.

**Cautious (C):** The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.

Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

### Stock Price, Price Target and Rating History (See Rating Definitions)



Source: Morgan Stanley Research      Date Format : MM/DD/YY      Price Target ---      No Price Target Assigned (NA)  
 Stock Price (Not Covered by Current Analyst) — Stock Price (Covered by Current Analyst) —  
 Stock and Industry Ratings (abbreviations below) appear as ♦ Stock Rating/Industry View  
 Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)  
 Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

Effective January 13, 2014, the stocks covered by Morgan Stanley Asia Pacific will be rated relative to the analyst's industry (or industry team's) coverage.

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## INDUSTRY COVERAGE: ASEAN Gaming

COMPANY (TICKER)	RATING (AS OF)	PRICE* (05/18/2018)
<b>Praveen K Choudhary</b>		
Bloomberry Resorts Corporation (BLOOMP.S)	O (03/26/2018)	PP12.78
Genting Singapore PLC (GENS.SI)	O (04/12/2018)	S\$1.31
NagaCorp (3918.HK)	E (04/04/2018)	HK\$7.66

Stock Ratings are subject to change. Please see latest research for each company.

\* Historical prices are not split adjusted.