

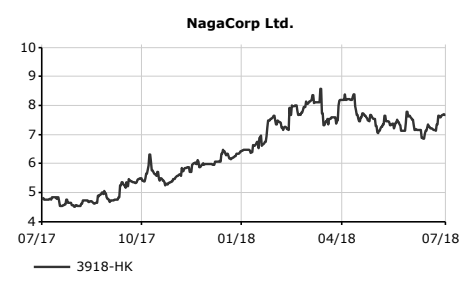
25 July 2018

Asia Research

Rating: Buy

Price Target: HK\$10.00

Price	HK\$8.35
52wk Range	HK\$4.48 - HK\$8.63
Shares Outstanding (MM)	4,341.0
Market Capitalization (MM)	HK\$36,247.4
Enterprise Value (MM)	HK\$35,830.6
30D Avg Volume (000s)	2,960.7
Short Interest/Float	0.0%
Dividend Yield	4.0%
YTD % Chg	26.8%
YTD % Chg Relative to Index	21.3%
Total Implied Return to PT	23.7%
Pricing Date	July 25, 2018



NagaCorp Ltd.

Global Gaming Operators

3918-HK | HKSE | HK\$8.35

Company Update

Still making it look easy; Naga2 ramping faster than Macau IRs; reiterate Buy

2Q18/1H18 recap. All segments showed significant growth, demonstrating none of the (temporary) cannibalization typically seen upon the opening of a new property, which in turn speaks to the enviable demand trends in Phnom Penh. Ultimately, the addition of high quality supply has spurred demand and NagaCorp is generating Macau flagship-like gaming volumes and levels of EBITDA typically only seen at 1st-tier operators. Implied 2Q18 gaming metrics included:

VIP volume +177% (UG at +87%); Mass volume +51% (UG at +45%); Slot volume +21% (UG at +32%)

For the entire 1H18, revenue increased 83% to \$733mm despite the lack of slot license fees during the current period (vs. \$60mm in the prior year period). EBITDA grew 29% (or 92% ex-last year's slot fees) to \$233mm. This compared favorably to our estimate of \$204mm, which included an expected 5% GGR tax that has not yet materialized. Backing out the tax expectations, our EBITDA forecast would have been \$233mm, suggesting an in line quarter – although Naga did it in a much more convincing way without the benefit of pure-margin slot license fees during the current period as our model had assumed.

Naga2 has been a game-changer. In 2017, the company generated \$260mm in EBITDA from operations (ex-slot license fees), which primarily represented operations from the original NagaWorld as Naga2 opened in November. That the company reported \$233mm in EBITDA during 1H18 and that win/day for tables and slots has steadily increased throughout the period indicates the reception to the property has been impressive. This is echoed by our junket contacts who instantly turned bullish on bringing customers to Naga as soon as Naga2 opened. We look for Naga2 to continue to ramp over the coming months and expect the company to move forward with Naga3 in some fashion over the next few years.

Cambodian gaming bill and tax rate. While we had anticipated the regulatory/tax bill to be passed in early 2018, it now appears that it will likely be pushed back to early 2019. As such, we are removing this component from our model this year, but are maintaining it for 2019 and beyond (at 5.5%). As such, our 2019 EBITDA estimate appears to only grow at 4%, but on a like-for-like basis is closer to 23%.

Reiterate Buy rating. Naga continues to make it look easy, and we are reiterating our Buy rating as the growth story remains one of the most enviable in global gaming. Numerous and visible drivers (Naga2 ramping, Naga FBO airport hangar opening soon, new junket partners, Naga1 refurbish, significant FDI into Cambodia, strength in visitation to Cambodia, penetration of new-to-Naga markets like Thailand, etc.) should result in double-digit EBITDA growth (ex-tax situation) over the next few years. On a longer-term basis, and with 18 years of exclusivity remaining on the company's license, we look for even more supply to be developed. We reiterate our Buy rating and are raising our PT to HK\$10 (+\$1).

Analysts

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Year to Dec	Net Revenue	Adjusted EBITDA	EPS
2018E	1,446	452	0.08
Prior	1,408	373	0.07
2019E	1,613	469	0.08
Prior	1,622	431	--

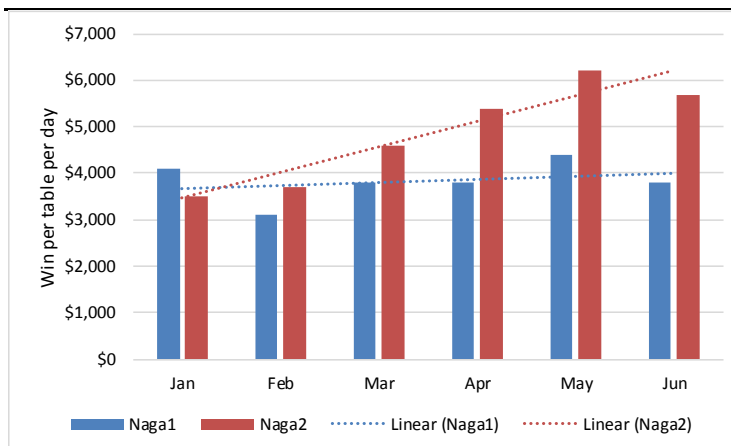
*Please see analyst certification and required disclosures starting on page 4 of this report.

No cannibalization at the original NagaWorld

A hallmark of the recent Macau IR openings is that the legacy/sister properties tend to experience a temporary period of cannibalization as not only gaming positions, but customers too, are lent to the new property. However, we have seen no evidence of this dynamic as it relates to the relationship between NagaWorld (aka Naga1) and Naga2. In fact, not only did Naga1 not need to “lend” any gaming positions to Naga2 (as the government imposes no related gaming position caps), Naga1 continues to operate the same number of EGMs (slots) and tables as it did before the opening of Naga2 and has maintained win/day in line with pre-Naga2 levels.

Concurrently, Naga2 has grown its win/table to levels well above Naga1 while also adding more tables to its inventory to satisfy demand.

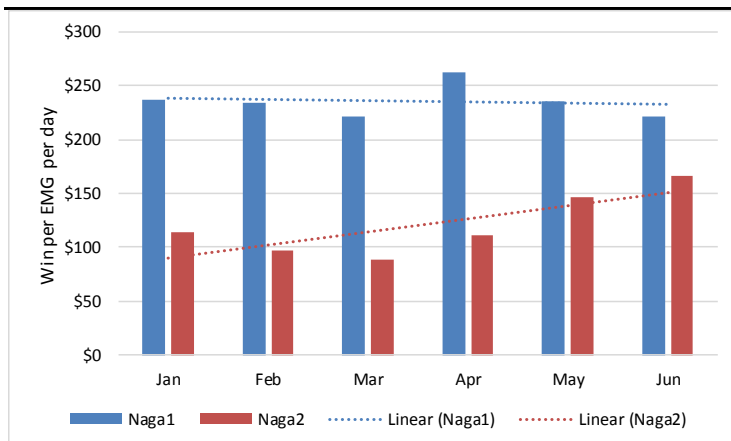
Figure 1: Naga1 and Naga2 win/table, January to June 2018



Source: company data

Similarly, Naga1 has maintained EGM win/day in line with pre-Naga2 levels. However, and while Naga2 is ramping its EGM win/day nicely, it currently remains below Naga1 levels. We expect Naga2 to catchup with Naga1 at some point during 2H18. In our view, the fact that EGM win/day at Naga2 has not yet caught up with Naga1 is the reason the company did not move forward with any slot license fee deals during 1H18. Given our belief that Naga2 EGM win/day will catch up with Naga1 during the current 2H18, we would look for the company to monetize another batch of slots for Naga2 at some point early next year. As such, we have pushed back our expectations for slot license fees to 2019.

Figure 2: Naga1 and Naga2 win/slot, January to June 2018



Source: company data

Naga3 in the works

Given a confluence of factors, including the initial (and instant) success of Naga2, the fact that the company is still under-supplied in terms of sleeping rooms (only 2,000 rooms between Naga1 and Naga2), that there is still 18 years of exclusivity remaining on their license, that visitation to Cambodia continues to grow, that FDI (particularly from China) continues to pour into Cambodia, and that the company is generating significant FCF, we look for an announcement on Naga3 within the next 12-18 months. Management continues to work on the scope of the project and we would expect it to be located within close proximity to Naga1 and Naga2. Given typical IR construction cycles, we would expect the project to be operational within six years, thus giving it plenty of runway prior to the lapsing of the company's monopoly in 2035.

Earnings model

Figure 2: NagaCorp earnings model

NagaCorp	2013	2014	2015	2016	2017	2018E	2019E	2020E
Year ends December 31								
Revenue								
Casino Operations	223.0	296.8	343.8	355.3	775.0	1,280.8	1,357.8	1,485.1
Income from Gaming Machines	101.9	84.6	136.8	145.5	150.9	125.3	210.8	223.4
F&B, Hotel and Other	20.0	22.9	23.1	30.7	30.4	40.1	44.9	50.3
Total revenue	\$344.9	\$404.3	\$503.7	\$531.5	\$956.4	\$1,446.3	\$1,613.5	\$1,758.8
Administrative expense	(47.0)	(51.5)	(47.2)	(52.6)	(67.2)	(72.2)	(75.1)	(77.3)
Other operating expenses	(57.9)	(82.5)	(97.2)	(111.8)	(150.2)	(182.7)	(193.6)	(203.3)
Gaming taxes @ 5.5% on GGR	0.0	0.0	0.0	0.0	0.0	0.0	(86.1)	(94.1)
Total EBITDA	\$171.8	\$176.0	\$228.5	\$256.1	\$319.7	\$452.3	\$468.9	\$514.5
Interest income (expense)	0.0	0.0	0.0	0.0	0.0	(17.6)	(28.1)	(28.1)
Profit before taxation	145.4	142.0	189.0	208.2	263.3	347.0	354.8	400.3
Taxation	(5.1)	(5.9)	(16.4)	(24.1)	(8.1)	(9.0)	(10.1)	(11.4)
Profit attributable to equity holders	140.3	136.1	172.6	184.2	255.2	338.1	344.7	389.0
EPS	\$0.063	\$0.060	\$0.076	\$0.070	\$0.059	\$0.078	\$0.079	\$0.090
Shares outstanding	2235.1	2281.9	2270.0	2616.9	4341.0	4341.0	4341.0	4341.0

Source: Union Gaming

Valuation

We value NagaCorp using an EV/EBITDA approach on forward earnings. Our 12 month price target is HK\$10 (from \$9) and is based on a 10.5x multiple of our 2019 EBITDA estimate. This multiple is slightly higher than the range we have historically assigned to Naga, but is still broadly in line with the regional peer set. We note that our forward earnings forecasts assume that a 5.5% GGR tax is levied upon Naga and is reflected in our earnings estimates and PT. The lack of implementation of a gaming tax, or a differential in the magnitude of the gaming tax could have a material impact on our forward earnings estimates.

Risks

Risks to shares of NagaCorp include: political risk (loss of exclusive license, adjustment to the company's advantageous low monthly fixed obligation tax), development risk including potential delays to the Vladivostok project, incremental regional competition, and volatility associated with a growing VIP business.

Important Disclosure

Analyst Certification

The analyst, Grant Govertsen, primarily responsible for the preparation of this research report attests to the following: (1) that the views and opinions rendered in this research report reflect his or her personal views about the subject companies or issuers; and (2) that no part of the research analyst's compensation was, is, or will be directly related to the specific recommendations or views in this research report.

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Current Ratings Definition

Union Gaming Securities LLC and Union Gaming Securities Asia Limited use a traditional ratings construct (Buy, Hold, and Sell) that is underscored by percentage upside/downside from current trading levels along with dividend yields for total return. We exclude special dividends and contemplate regular dividends only in our total return forecasts. These are absolute ratings, not relative or forced ratings. We define a Buy rating as a company whose shares exhibit total return (appreciation and dividends) potential of at least 15% within the next 12 months, and conversely a Sell rating as a company whose shares exhibit downside potential of at least 15% within the next 12 months. A Hold rating is reserved for companies whose shares exhibit total return potential between those parameters.

Buy – the total forecasted return is expected to be greater than 15% within the next 12 months

Hold – the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 15%

Sell – whose shares exhibit downside potential of at least 15% within the next 12 months

Suspended – the company rating, target price and earnings estimates have been temporarily suspended.

Valuation and Risks

Valuation

Valuation Methodology for Price Target: Enterprise Value-to-EBITDA, Sum-of-the-Parts Analysis, Price-to-Earnings Ratio, Discounted Cash Flow Analysis, Price-to-AFFO, Net Asset Value.

Risks

Investment Risks: Union Gaming Securities' equity research team covers the casino, gambling, gaming, lottery and related sectors. The companies operating within these sectors generally have a global presence or significant exposure to China and Las Vegas, among other markets. In addition, the markets that companies in these sectors operate are highly regulated by local and federal governments. Risks across or specific to one or more of these sectors include regulatory or legislative impacts related to licensing, tourism or the competitive landscape. Licenses to operate gaming facilities or supply gaming equipment or lottery services are often governed by regulatory authorities. Additional Risks for investing in these sectors include volatility in consumer discretionary spending and consumer confidence, currency, interest rates, unemployment rates, access to capital, the cost of capital, commodity costs, geopolitical uncertainty, and unfavorable government regulations. Companies operating within our covered sectors rely in part on tourism, and business trends could be impacted by changes or influences to tourism in a given market or markets, including visa policy, transit policies and security, transportation infrastructure, weather and natural disasters.

Ratings Distribution (as of 07/25/2018)

Coverage Universe

Ratings	Count	Pct.
BUY	21	78%
HOLD	6	22%
SELL	0	0%

Investment Banking Services / Past 12 Months

Rating	Count	Pct.
BUY	9	43%
HOLD	1	17%
SELL	0	0%

NagaCorp Ltd. Rating History as of 07/24/2018

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General Disclosures

Additional information is available upon request.

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