

NagaCorp Ltd (3918 HK, BUY, TP: HK\$14.00)

BUY

HOLD

SELL

Target Price: HK\$14.00 Current Price: HK\$10.76

52-Week High HK\$11.66
52-Week Low HK\$6.85
EV (MM) HK\$45,912
Market Cap (MM) HK\$46,709
Shares Outstanding (MM) 4,341
Average Daily Trading Volume (MM) 3.9

Priced as of close on 23 July 2019.

Source: FactSet

Price Performance



Source: FactSet

China Renaissance vs Consensus (% diff)

	2019E	2020E
Rev (MM) (\$)	1,846 (+1%)	2,080 (+1%)
EPS (\$)	0.11 (+9.35%)	0.12 (+8.49%)

Note: Consensus estimates displayed, sourced from Bloomberg. Positive % diff = CR est. above consensus; negative = CR est. below consensus.

1H19 clear beat on continued ramp-up

- **1H19 EBITDA of US\$328mn (+41% YoY, +17% HoH) a clear beat on stronger GGR; net profit up 36% YoY/ 16% HoH to US\$245mn.**
- **Interim DPS of US\$0.0339 was in-line with 60% payout ratio in the past, implying a 2.4% dividend yield as of the latest closing.**
- **Lift FY19E/20E EBITDA forecast by 11%/10% on strong results. TP of HK\$14 implies 11x/10x FY19E/20E EV/EBITDA.**

Solid results on both VIP and mass side.

1H19 revenue grew 22% YoY to US\$892mn, on a 45% YoY jump in mass GGR, and 18% YoY hike in VIP GGR despite a normalized win rate of 2.8%. Gross profit increased 32% YoY, thanks to the margin expansion through a larger exposure to the higher-margin mass business. Opex remained under tight control, resulting in a 41% YoY EBITDA growth. Despite drags from interest expenses and additional tax obligations, 1H19 net profit still recorded an upbeat growth of 36% YoY with margin expansion of 2ppts YoY to 27%.

More promising operating environment.

1) Management does not expect any slowdown in VIP gaming in the near future since Naga does not have exposure to online gaming. 2) 92% of the Naga3 space will be allocated for non-gaming purposes to promote Phnom Penh's leisure tourism and attract visitors from China; 3) the Vladivostok project is on schedule to complete in 2019, and management is optimistic on the business amid a tightening tie between China and Russia through building high speed rail between Haerbin and Far East Russia.

BUY with TP of HK\$14 at 11x FY19E EV/EBITDA, in-line with Macau peers.

NagaCorp is currently trading at 9x FY19E EV/EBITDA and 12x P/E. NagaCorp is set to outshine Macau peers in 2019, in our view. We expect NagaCorp to record 26%/33% YoY growth in FY19E revenue and EBITDA. We expect the Macau GGR to remain largely flat YoY in 2019, which should further narrow the valuation discount between NagaCorp and Macau peers. **Risks** include: potential for political unrest and a cooling economy in Cambodia; change in gaming regulations that may jeopardize NagaCorp's monopoly status or challenge its current low tax position; and a sudden drop in demand from key target markets such as China and Southeast Asia.

Summary Financial Data

Fiscal year-end: Dec	2018A	2019E	2020E	2021E
Revenue (MM) (\$)	1,474	1,861	2,100	2,381
EBITDA (MM) (\$)	512	682	755	865
EPS (\$)	0.09	0.12	0.13	0.16
EV/EBITDA	12x	9x	8x	6x
P/E	16x	12x	11x	9x
FCF yield	4%	5%	11%	13%
Dividend yield	3.8%	5.0%	5.4%	6.7%

Source: China Renaissance Securities (Hong Kong) Limited

Research Team

Angela Han Lee, Vice President
+852 2287 1694
AngelaHanLee@chinarenaissance.com

Nate Deng
+852 2287 1624
NateDeng@chinarenaissance.com

Chris Gao
+852 2287 1242
ChrisGao@chinarenaissance.com

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Exhibit 1: Operational data

US\$m	1H18	2H18	1H19	YoY	HoH	Comment
Casino operations - gaming tables	654	651	796	22%	22%	Better than expected on both VIP and mass
Casino operations - electronic gaming	60	69	76	27%	10%	In line
Non-gaming	19	21	19	0%	-8%	
Total revenue	733	741	892	22%	20%	
Cost of sales	(423)	(377)	(483)	14%	28%	
Gross profit	309	364	408	32%	12%	
<i>Gross margin</i>	42%	49%	46%			
Staff costs	(46)	(47)	(59)	29%	27%	
Operating lease charges	(6)	(6)	(6)	2%	2%	
Depreciation and amortisation	(45)	(48)	(50)	12%	4%	
Other operating expenses	(25)	(32)	(15)	-39%	-53%	Stringent admin opex control
Operating profit	188	231	278	48%	20%	Better than expected
<i>Operating margin</i>	26%	31%	31%			
EBITDA	233	279	328	41%	17%	Better than expected
<i>EBITDA margin</i>	32%	38%	37%			
Non-operating items	(3)	(16)	(17)	396%	8%	In line with increase in interest expenses
Income tax expense	(4)	(4)	(15)	244%	244%	Additional obligation
Non-controlling interest	-	-	-			
Net profit	180	210	245	36%	16%	Better than expected
<i>Net margin</i>	25%	28%	27%			
Gaming related data for NagaWorld						
VIP gaming						
Rolling chip volume	16,840	18,819	23,180	38%	23%	Stronger than expected
<i>VIP win rate</i>	3.3%	2.7%	2.8%			Normalized win rate as expected
VIP GGR	553	517	650	18%	26%	
VIP gross profit	138	148	173	25%	17%	
Mass tables gaming						
Mass table buy-ins	574	664	756	32%	14%	Stronger than expected
<i>Mass table win rate</i>	17.6%	20.3%	19.3%			
Mass table GGR	101	135	146	45%	9%	
Electronic gaming machines						
EGM bills-in	1,043	1,172	1,341	29%	14%	
<i>EGM win rate</i>	8.1%	9.4%	8.7%			
EGM GGR (include entrance fee)	60	69	76	27%	10%	Relatively stagnant

Source: Company data, CRSHK

Exhibit 2: Earnings revision

US\$m	New FY19E	Old FY19E	% chg	New FY20E	Old FY20E	% chg	Comment
Overall							
Total revenue	1,861	1,767	5%	2,100	1,980	6%	Continued ramp-up of Naga2
EBITDA	682	612	11%	755	689	10%	Margin expansion
EBITDA margin	37%	35%	2ppts	36%	35%	1ppt	
Net profit	513	466	10%	560	529	6%	
EPS (US\$)	0.12	0.11	10%	0.13	0.12	6%	
DPS (US\$)	0.07	0.06	10%	0.08	0.07	6%	
NagaWorld							
Total revenue	1,861	1,767	5%	2,071	1,950	6%	
EBITDA	679	608	12%	751	686	10%	
EBITDA margin	36%	34%	2ppts	36%	35%	1ppt	
VIP GGR	1,340	1,273	5%	1,466	1,378	6%	Strong rolling offset by normalized win rate
Mass GGR	480	452	6%	562	528	6%	Stronger than expected
Vladivostok project							
Total revenue	-	-	-	30	30	0%	We model opening in 2H20E
EBITDA	-	-	-	(0)	(0)	0%	
EBITDA margin	-	-	-	-1%	-1%	0ppt	
VIP GGR	-	-	-	16	16	0%	
Mass GGR	-	-	-	11	11	0%	

Source: Company data, CRSHK estimates

Valuation

Currently trading at 9x FY19E EV/EBITDA

The company is currently trading at 9x FY19E EV/EBITDA, 12x P/E and 5% dividend yield. Historically, Naga has been trading at a significant discount to its Macau gaming peers (around 7x EV/EBITDA for Naga vs. 13x for Macau peers) due to the following: 1) Cambodia is relatively under-developed, with political and social uncertainties that may compromise its tourism industry, and therefore, Naga's business; and 2) NagaCorp is of a smaller size and has a relatively unstable customer base as compared to international gaming operators in Macau, suggesting that it could suffer more in a downside market.

Naga's valuation discount to Macau gaming players has been narrowing recently and we believe the trend will continue – Naga deserves a valuation that is in-line with Macau peers given: 1) a more promising industry outlook; 2) its improving business quality; and 3) solid foundation for future expansion.

Exhibit 3: 1-year forward EV/EBITDA



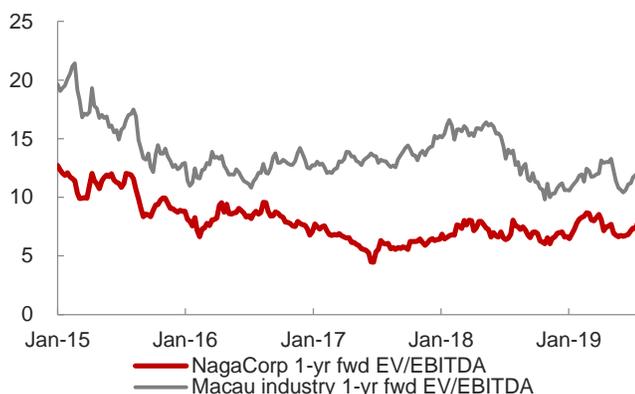
Source: Bloomberg, company data, CRSHK estimates

Exhibit 4: 1-year forward P/E



Source: Bloomberg, company data, CRSHK estimates

Exhibit 5: NagaCorp vs. Macau gaming industry 1-year forward EV/EBITDA



Source: Bloomberg, company data, CRSHK estimates

Exhibit 6: NagaCorp vs. Macau gaming industry 1-year forward P/E



Source: Bloomberg, company data, CRSHK estimates

Exhibit 7: Comparable companies

Company name	Ticker	Rating	Target Px	Current Px 7/24/2019	Market Cap (US\$ mn)	Avg T/O (US\$ mn)	EV/EBITDA (x)		
							FY18	FY19E	FY20E
Macau gaming									
Galaxy	27 HK	BUY	HK\$62.00	HK\$56.20	31,213	79.1	12x	11x	11x
SJM	880 HK	HOLD	HK\$7.00	HK\$9.35	6,790	15.7	15x	15x	12x
Wynn Macau	1128 HK	HOLD	HK\$20.00	HK\$19.02	12,673	27.1	11x	12x	11x
Sands China	1928 HK	HOLD	HK\$40.00	HK\$40.55	42,040	69.1	15x	14x	14x
MGM China	2282 HK	HOLD	HK\$16.00	HK\$13.82	6,733	9.7	15x	13x	11x
Melco Resorts	MLCO US	BUY	US\$26.00	US\$24.84	11,601	49.4	11x	10x	10x
Simple average							13x	13x	12x
Market cap average							14x	13x	12x
Conglomerate									
Melco International	200 HK	BUY	HK\$20.90	HK\$20.60	3,998	7.6	9x	7x	7x
SEA gaming									
NagaCorp	3918 HK	BUY	HK\$14.00	HK\$11.14	6,200	4.5	12x	9x	8x
Genting Singapore	GENS SP	NC	n.a.	SGD0.94	8,263	25.8	7x	8x	8x
Simple average							10x	8x	8x
Market cap average							9x	8x	8x
Las Vegas gaming									
Las Vegas Sands	LVS US	NC	n.a.	US\$65.22	50,402	249.6	11x	11x	11x
MGM Resorts	MGM US	NC	n.a.	US\$29.20	15,686	164.1	12x	10x	9x
Wynn Resorts	WYNN US	NC	n.a.	US\$138.27	14,886	248.2	11x	11x	9x
Simple average							11x	11x	10x
Market cap average							11x	11x	10x

Company name	Ticker	P/E (x)			FCF yield			Dividend yield		
		FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Macau gaming										
Galaxy	27 HK	18x	17x	15x	6%	6%	7%	2%	2%	2%
SJM	880 HK	19x	24x	21x	-5%	0%	4%	3%	2%	3%
Wynn Macau	1128 HK	16x	16x	15x	7%	8%	8%	6%	7%	6%
Sands China	1928 HK	22x	19x	18x	5%	5%	5%	5%	5%	5%
MGM China	2282 HK	49x	17x	14x	1%	3%	3%	1%	2%	3%
Melco Resorts	MLCO US	34x	20x	18x	7%	7%	7%	2%	2%	2%
Simple average		26x	19x	17x	4%	5%	6%	3%	3%	3%
Market cap average		23x	18x	17x	5%	5%	6%	4%	4%	4%
Conglomerate										
Melco International	200 HK	57x	22x	17x	5%	7%	7%	0%	1%	1%
SEA gaming										
NagaCorp	3918 HK	16x	12x	11x	4%	5%	11%	4%	5%	5%
Genting Singapore	GENS SP	14x	16x	16x	10%	6%	7%	3%	3%	3%
Simple average		15x	14x	13x	7%	5%	9%	3%	4%	4%
Market cap average		15x	14x	14x	7%	5%	9%	3%	4%	4%
Las Vegas gaming										
Las Vegas Sands	LVS US	19x	20x	18x	7%	4%	5%	5%	5%	5%
MGM Resorts	MGM US	25x	29x	18x	1%	4%	5%	2%	2%	2%
Wynn Resorts	WYNN US	21x	23x	18x	4%	6%	7%	2%	3%	3%
Simple average		22x	24x	18x	4%	4%	6%	3%	3%	3%
Market cap average		21x	22x	18x	5%	4%	6%	4%	4%	4%

Note: US\$:HK\$ = 7.8

Source: Bloomberg for NC companies, CRSHK estimates

Exhibit 8: NagaCorp - Financial summary
Balance Sheet

US\$ mn	FY18	FY19E	FY20E	FY21E
Current assets	512	524	825	913
Cash and cash equivalents	317	298	579	644
Account and other receivables	117	148	167	189
Inventories	2	2	2	3
Other current assets	76	76	76	76
Non-current assets	1,455	1,702	1,654	1,611
Property and equipment	1,276	1,553	1,509	1,469
Intangible assets	59	56	52	48
Interest in leasehold land	27	(0)	(0)	(1)
Other non-current assets	94	94	94	94
Total assets	1,967	2,226	2,479	2,523
Current liabilities	92	112	124	139
ST borrowings	-	-	-	-
Account payables	80	99	112	126
Other current liabilities	12	12	12	12
Non-current liabilities	335	335	335	46
LT borrowings	291	291	291	2
Other non-current liabilities	44	44	44	44
Total liabilities	427	447	460	185
Share capital	54	54	54	54
Treasury shares	-	-	-	-
Reserves	1,486	1,725	1,965	2,284
Minority interest	-	-	-	-
Shareholders' equity	1,540	1,779	2,020	2,338
Total equity and liabilities	1,967	2,226	2,479	2,523

Statement of cash flows

US\$ mn	FY18	FY19E	FY20E	FY21E
Operating cashflow	477	636	712	815
Net income	391	513	560	689
Depreciation and amortization	93	103	127	124
Change in working capital	(18)	(11)	(7)	(8)
Other operating cashflow	11	31	31	10
Investing cashflow	(317)	(347)	(76)	(76)
CAPEX	(244)	(376)	(80)	(80)
Interest received	3	3	4	4
Investment in bonds	-	-	-	-
Other investing cashflow	(76)	26	-	-
Financing cashflow	104	(308)	(354)	(673)
Net proceeds from borrowings	275	(35)	(35)	(303)
Share issue (repurchase)	-	-	-	-
Dividend paid	(171)	(273)	(320)	(371)
Other financing cashflow	-	-	-	-
Foreign exchange rate adj.	-	-	-	-
Net change in cash	264	(19)	281	65

Source: Company data, CRSHK estimates

Income statement

US\$ mn	FY18	FY19E	FY20E	FY21E
Total revenue	1,474	1,861	2,100	2,381
Cost of sales	(801)	(997)	(1,124)	(1,270)
Employee benefit expenses	(92)	(120)	(132)	(147)
Operating lease charges	(12)	(12)	(12)	(13)
Gaming tax	-	(22)	(48)	(55)
Depreciation and amortisation	(93)	(109)	(132)	(129)
Other operating expenses	(57)	(31)	(32)	(35)
Adjusted EBITDA	512	682	755	865
Operating profit	419	570	619	732
Interest expense	(19)	(35)	(35)	(14)
Interest income	3	3	4	4
Other non-operating items	(3)	-	-	-
Pre-tax profit	399	539	588	722
Income tax expense	(9)	(26)	(27)	(33)
After-tax profit	391	513	560	689
Non-controlling interests	-	-	-	-
Net profit to shareholders	391	513	560	689
Basic EPS (US\$)	0.09	0.12	0.13	0.16
Diluted EPS (US\$)	0.09	0.12	0.13	0.16
DPS (US\$)	0.05	0.07	0.08	0.10

Ratios

	FY18	FY19E	FY20E	FY21E
YoY				
Total revenue	54%	26%	13%	13%
Adjusted EBITDA	60%	33%	11%	15%
Operating profit	59%	36%	9%	18%
Net profit	53%	31%	9%	23%
Profitability				
EBITDA margin	35%	37%	36%	36%
OP margin	28%	31%	29%	31%
NP margin	26%	28%	27%	29%
ROE	25%	29%	28%	29%
ROIC	25%	28%	31%	37%
Liquidity				
Debt/equity	19%	16%	14%	0%
Net debt/equity	-7%	-5%	-18%	-31%
Current ratio	5.6x	4.7x	6.6x	6.6x
Quick ratio	4.7x	4.0x	6.0x	6.0x
Operating efficiency				
Asset turnover	0.7x	0.8x	0.8x	0.9x
Valuation ratios				
EV/EBITDA	12x	9x	8x	6x
P/E	16x	12x	11x	9x
FCF yield	4%	5%	11%	13%
Dividend yield	4%	5%	5%	7%

Risks

Macro. Potential for political unrest and a cooling economy in Cambodia; any change in gaming regulations that may jeopardize NagaCorp's monopoly status or challenge its current low tax position; and a sudden drop in demand from key target markets such as China and Southeast Asia, which could result in lower-than-expected EBITDA growth

Economic 1) A cool down in Southeast Asian economies, which are NagaCorp's key target markets, due to weaker global consumption demand. 2) A substantial drop in foreign direct investment, which could result in a slowdown in overall economic activity in Cambodia.

Political Cambodian Prime Minister Hun Sen's win in the 2018 election was not recognized by western countries, and was also controversial within the country. Political disruption could adversely impact Cambodia's tourism industry, discouraging inbound visitation.

Policy Gaming policies might experience more frequent changes than in other nations, since Phnom Penh does not have a long history of regulating the gaming market. Risks include: 1) a potential increase in gaming tax payments since the current rate is far lower than in other regions; and 2) the issuance of another gaming license in Phnom Penh, ending NagaWorld's monopolistic position in the city.

Regional gaming competition. The increasing number of gaming venues in the region could adversely affect the company's performance.

Market cannibalization Expanding NagaWorld through Phase 3 development may lead to significant growth in the number of gaming tables and hotels, which may outpace demand, leading to a slowdown in revenue growth.

Rising wages Labor costs in Cambodia are relatively low. A hike in the minimum wage would impact NagaCorp's staff costs.

Financing needs The company has a high dividend payout ratio of 60%, which could come under pressure if the company needs to raise finance to support its expansion.

Appendix A

Analyst Certification

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Below is the distribution of research recommendations as of July 24, 2019

Rating	Count	Percent	IB Count	IB%
Buy	59	64.13%	59	100.00%
Hold	27	29.35%	27	100.00%
Sell	6	6.52%	6	100.00%

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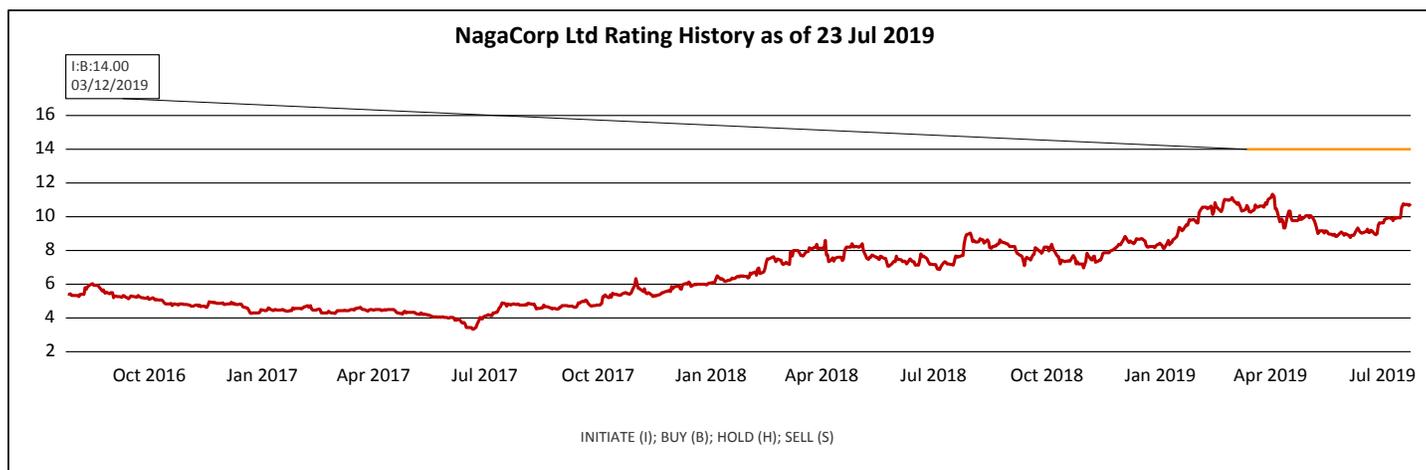
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Overweight – Expect sector to outperform the relevant market.

Neutral – Expect sector to perform in line with the relevant market.

Underweight – Expect sector to underperform the relevant market.



Valuation Methodology

3918 HK:

Our target price for NagaCorp is HK\$14.00, based on 11x FY19E EV/EBITDA, implying 15x FY19E P/E.

Risks include: Potential for political unrest and a cooling economy in Cambodia; any change in gaming regulations that may jeopardize NagaCorp’s monopoly status or challenge its current low tax position; and a sudden drop in demand from key target markets such as China and Southeast Asia, which could result in lower-than-expected EBITDA growth

Economic risks. 1) A cool down in Southeast Asian economies, which are NagaCorp’s key target markets, due to weaker global consumption demand. 2) A substantial drop in foreign direct investment, which could result in a slowdown in overall economic activity in Cambodia.

Political risks. Cambodian Prime Minister Hun Sen’s win in the 2018 election was not recognized by western countries, and was also controversial within the country. Political disruption could adversely impact Cambodia’s tourism industry, discouraging inbound visitation.

Policy risks. Gaming policies might experience more frequent changes than in other nations, since Phnom Penh does not have a long history of regulating the gaming market. Risks include: 1) a potential increase in gaming tax payments since the current rate is far lower than in other regions; and 2) the issuance of another gaming license in Phnom Penh, ending NagaWorld's monopolistic position in the city.

Regional gaming competition. The increasing number of gaming venues in the region could adversely affect the company's performance.

Market cannibalization. Expanding NagaWorld through Phase 3 development may lead to significant growth in the number of gaming tables and hotels, which may outpace demand, leading to a slowdown in revenue growth.

Rising wages. Labor costs in Cambodia are relatively low. A hike in the minimum wage would impact NagaCorp's staff costs.

Financing needs. The company has a high dividend payout ratio of 60%, which could come under pressure if the company needs to raise finance to support its expansion.

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