

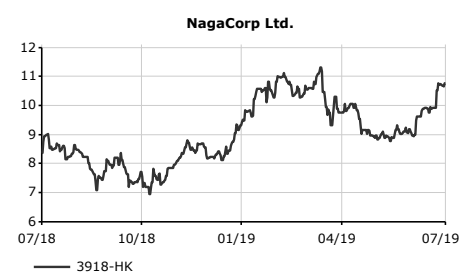
24 July 2019

Asia Research

Rating: Buy

Price Target: HK\$12.00

Price	HK\$11.14
52wk Range	HK\$6.85 - HK\$11.66
Shares Outstanding (MM)	4,341.0
Market Capitalization (MM)	HK\$48,358.8
Enterprise Value (MM)	HK\$48,536.7
30D Avg Volume (000s)	4,044.0
Short Interest/Float	0.0%
Dividend Yield	4.5%
YTD % Chg	27.8%
YTD % Chg Relative to Index	7.9%
Total Implied Return to PT	12.3%
Pricing Date	July 24, 2019



NagaCorp Ltd.

Global Gaming Operators

3918-HK | HKSE | HK\$11.14

Company Update

1H19 results showcase Naga2's ramp; Naga beats expectations again

FY1H19 recap. NagaCorp reported 1H19 results with continued strength across all gaming segments, including in VIP, which continues to decline in most other jurisdictions. GGR grew 22%, to US\$872mm (UG at \$802mm), with EBITDA of \$328mm (+41%). Volume trends remain very robust for all gaming segments, driven by a host of factors detailed below. While the government was yet again unable to get the gaming regulatory bill (including formalizing a GGR tax) across the finish line, the government did assess a \$10.4mm additional tax obligation on non-gaming, which is broadly in line with previous assessments in 2015 and 2016.

Volume metrics and sequential growth. During 1H19, VIP volume grew 38% (UG at +16%), mass table volume +32% (UG at +21%) and slot volume +29% (UG +17%). We were particularly surprised by the strength in VIP considering the regional outlook. However, Naga results continue to demonstrate that there is plenty of underlying demand for VIP given the right parameters that Naga delivers with its Naga2 product. Naga2 is still ramping, and was likely responsible for most of the sequential growth seen in 2Q19 over 1Q19 (VIP volume +83%, mass table volume +20%, and slot volume +1%). We are raising our estimates as detailed herein for both 2H19 and 2020 on the heels of strong operating results and our bullish outlook. Importantly, we believe Naga continues to expand its premium mass segment, which is primarily captured at Naga2 and driven by continued growth in Chinese expats to Phnom Penh, as well as regional players. Prior to the opening of Naga2, this was a much more difficult segment to penetrate, especially for overseas customers.

Outlook. Very strong demand argues for more supply in Phnom Penh. The company's proposed Naga3 has yet to be formalized via shareholder approval, the results of which are the pacing item we're waiting on to reflect Naga3 in valuation. Based on current trends, we believe Naga should generate enough FCF to support the current ~60% dividend payout ratio and also fund its proposed share of Naga3 development costs. Importantly, we continue to view Phnom Penh/Naga as the most insulated operator/market from the volatility associated with China (i.e. proxy/online crackdown leading to a decline in brick-and-mortar business) driven in part by the close relationship between China/Cambodia. Further, this same close relationship is a key driver of FDI into Phnom Penh, Cambodia and underpins the exceptional growth reported during 1H19 and our expectations of continued strong growth over the near, medium, and longer terms. Beyond this there are numerous levers, including strong tourism growth, robust economic trends generating increased wealth, the continuing refurbishment of Naga1 (including converting non-gaming space to gaming space), and various company-specific marketing and efficiency initiatives. Based on our continued bullish outlook on the market and the company, we are maintaining our Buy rating and HK\$12 price target.

Analysts

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Year to Dec	Net Revenue	Adjusted EBITDA	EPS
2019E	1,801	627	0.11
Prior	1,687	531	0.09
2020E	2,061	603	0.11
Prior	1,842	576	0.10

*Please see analyst certification and required disclosures starting on page 3 of this report.

Earnings model

We note that our earnings model, as highlighted in the table below, assumes the implementation of a GGR tax in 2020 of approximately 5.5% of GGR. Absent this GGR tax our 2020 EBITDA estimate of \$603mm would be closer to \$715mm (vs. consensus of \$742mm). Therefore, any delays to the implementation of the GGR tax could yield material upside to our estimates.

Figure 1: NagaCorp earnings model

NagaCorp	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E
Year ends December 31									
Revenue									
Casino Operations	223.0	296.8	343.8	355.3	775.0	1,305.1	1,599.5	1,798.0	1,930.3
Income from Gaming Machines	101.9	84.6	136.8	145.5	150.9	129.3	154.3	211.0	226.4
F&B, Hotel and Other	20.0	22.9	23.1	30.7	30.4	39.9	46.9	52.5	58.8
Total revenue	\$344.9	\$404.3	\$503.7	\$531.5	\$956.4	\$1,474.3	\$1,800.7	\$2,061.5	\$2,215.5
Administrative expense	(47.0)	(51.5)	(47.2)	(52.6)	(67.2)	(79.3)	(74.3)	(76.5)	(78.8)
Other operating expenses	(57.9)	(82.5)	(97.2)	(111.8)	(150.2)	(185.6)	(223.5)	(256.2)	(275.1)
Gaming taxes @ 5.5% on GGR	0.0	0.0	0.0	0.0	0.0	0.0	0.0	(112.7)	(121.2)
Total EBITDA	\$171.8	\$176.0	\$228.5	\$256.1	\$319.7	\$511.8	\$627.4	\$602.6	\$648.4
Interest income (expense)	0.0	0.0	0.0	0.0	0.0	(19.5)	(31.4)	(28.1)	(28.1)
Profit before taxation	145.4	142.0	189.0	208.2	263.3	399.4	502.8	488.4	534.3
Taxation	(5.1)	(5.9)	(16.4)	(24.1)	(8.1)	(8.8)	(20.1)	(22.7)	(25.5)
Profit attributable to equity holders	140.3	136.1	172.6	184.2	255.2	390.6	482.7	465.8	508.8
EPS	\$0.063	\$0.060	\$0.076	\$0.070	\$0.059	\$0.090	\$0.111	\$0.107	\$0.117
Shares outstanding	2235.1	2281.9	2270.0	2616.9	4341.0	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\$12 (unchanged) and is based on a 10x multiple of our 2020 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 07/25/2019)

Coverage Universe

Ratings	Count	Pct.
BUY	22	73%
HOLD	8	27%
SELL	0	0%

Investment Banking Services / Past 12 Months

Rating	Count	Pct.
BUY	7	32%
HOLD	0	0%
SELL	0	0%

NagaCorp Ltd. Rating History as of 07/23/2019

powered by: BlueMatrix



General Disclosures

Additional information is available upon request.

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