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NagaCorp

Valuation Getting Rich;
Downgrading to EW

Stock Rating
Equal-weight

Industry View
Attractive

Price Target
HK\$8.50

Since Naga 2 opened in Nov. 2017, the stock has outperformed the Hang Seng by 42%. However, 1Q18 GGR missed our estimate by 24% and we reduce our revenue estimates by 5% in both 2018 and 2019. We see limited upside to our new PT.

WHAT'S
CHANGED?

NagaCorp (3918.HK)	From:	To:
Price Target	HK\$8.20	HK\$8.50
Rating	Overweight	Equal-weight

Investment conclusion - We believe NagaCorp remains a unique gaming company with a monopoly casino license in Phnom Penh that benefits from China BRI investments and visitations which should drive more than 20% per annum earnings growth from 2017 to 2020. With lower tax and a higher dividend yield, the stock deserves to trade at a premium to its historical trading range, in our view. However, recent price appreciation (42% outperformance since Naga 2 opening in November 2017) has pushed its valuation (12x EV/EBITDA, 15x PE, 6.6% FCFE yield and 3.7% dividend yield on 2018e) to 1SD higher than its long-term average since 2011. This, along with weaker than expected 1Q18 GGR results and limited upside to our PT, drives our rating change to EW from OW.

1Q18 missed MS expectations - 1Q18 GGR of US\$243mn (-36% QoQ and +181% YoY) was below our estimate by 24% due to weaker VIP rolling chip volume (-44% QoQ to US\$5.6bn) amid seasonally weak February. Mass table drop was 8% above our estimate, while EGM missed as well. If we annualize the current 1Q18 run rate, full-year GGR would be 27% below our estimate. We expect the gap to be bridged with the help of strong mass visitation and VIP business from junkets (ramp of SunCity and addition of MegStar in 2Q18).

What's changed? We lower our VIP revenue forecasts by 13% for 2018 and 14% for 2019, based on lower volume in 1Q18 and a reduction in total number of VIP tables from 365 to 280 by end-2019. We now forecast 12 more VIP tables to be added for the MegStar VIP Hall opening in 2Q18. We raise our mass revenue forecasts by 2% for 2018 and 11% for 2019 on more tables and higher table yield assumptions, driven by strong visitation growth. We increase our maintenance capex assumption for 2018/19 to US\$70mn, from US\$40mn previously. We now use 8% FCFE yield (earlier 9%) to arrive at our price target of HK\$8.50 (previously HK\$8.20); this implies 10x EV/EBITDA, similar to other regional casinos under our coverage (Bloomberg). Our higher multiple is supported by strong visitation and revenue YOY growth registered by the company YTD.

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NagaCorp (3918.HK, 3918 HK)

ASEAN Gaming / Hong Kong

Stock Rating	Equal-weight
Industry View	Attractive
Price target	HK\$8.50
Shr price, close (Apr 3, 2018)	HK\$8.58
52-Week Range	HK\$8.58-3.29
Sh out, dil, curr (mn)	4,341
Mkt cap, curr (mn)	US\$4,746
Avg daily trading value (mn)	HK\$29

Fiscal Year Ending	12/17	12/18e	12/19e	12/20e
ModelWare EPS (US\$)	0.059	0.068	0.084	0.094
Prior ModelWare EPS (US\$)	-	0.070	0.084	0.103
Revenue, net (US\$ mn)	956	1,458	1,704	1,879
EBITDA (US\$ mn)	312	374	455	502
ModelWare net inc (US\$ mn)	255	295	367	408
P/E	13.2	16.1	12.9	11.6
P/BV	3.3	3.1	2.8	2.6
RNOA (%)	20.5	18.2	20.5	22.4
ROE (%)	20.4	21.3	24.3	24.4
EV/EBITDA	14.4	12.6	10.0	8.7
Div yld (%)	4.6	3.7	4.6	5.2

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

US\$ million	2017	2018E	2019E	2020E
Revenue	956	1,458	1,704	1,879
VIP Revenue	625	1,008	1,176	1,297
Mass Revenue	150	212	255	281
EGM Revenue	151	177	200	224
Non-Gaming Revenue	30	62	73	77
Cost of sales	(483)	(781)	(912)	(1,005)
Gross profit	473	677	792	874
VIP	154	247	288	318
Mass	145	206	248	273
EGM	149	174	197	220
Non-Gaming	25	50	60	62
Administrative expenses	(67)	(97)	(107)	(118)
Other operating expenses	(94)	(136)	(149)	(164)
EBITDA	312	374	455	502
Depreciation	(53)	(81)	(90)	(95)
Amortization of license	(4)	(4)	(4)	(4)
EBIT	256	290	362	403
Profit before tax	263	297	369	411
Income Tax	(8)	(3)	(3)	(3)
Profit after tax	255	295	367	408
EPS (HK cents)	61.6	52.6	65.5	72.9
DPS (HK cents)	27.4	31.6	39.3	43.7

Balance Sheet

US\$ million	2017	2018E	2019E	2020E
Fixed Assets	1,149	1,288	1,318	1,292
Intangible Assets	63	59	56	52
Other Assets	95	95	95	95
Non-Current Assets	1,306	1,442	1,468	1,439
Stock	2	2	3	3
Debtors	101	155	181	199
Investment in bonds	-	-	-	-
Cash and deposits	53	40	172	370
Current Assets	156	196	355	573
Creditors	78	126	147	162
Current tax	2	2	2	2
Current Liabilities	80	128	149	164
Non-Current Liabilities	-	-	-	-
Share Capital	54	54	54	54
Reserves	1,328	1,456	1,620	1,794
Shareholders' Equity	1,383	1,510	1,675	1,848

Cash Flow Statement

US\$ million	2017	2018E	2019E	2020E
Profit before Tax	263	297	369	411
Depreciation & Amortization	56	84	94	99
Other non-cash adjustments	(7)	(3)	(3)	(3)
Changes In Working Capital	10	(5)	(6)	(4)
Operating cash flows	322	374	454	503
Capex	(355)	(220)	(120)	(70)
Others	0	-	-	-
Investing cash flows	(355)	(220)	(120)	(70)
Dividends Paid	(126)	(167)	(202)	(235)
Issuance of shares	-	-	-	-
Others	-	-	-	-
Financing cash flows	(126)	(167)	(202)	(235)
Change in Cash	(158)	(13)	132	198
Ending cash	53	40	172	370

Ratios	2017	2018E	2019E	2020E
Current ratio	2.0	1.5	2.4	3.5
Gross Profit Margin%	49%	46%	46%	47%
- VIP	25%	25%	25%	25%
- Mass	97%	97%	97%	97%
- EGM	99%	98%	98%	98%
- Non-gaming	81%	81%	81%	81%
EBITDA Margin%	33%	26%	27%	27%
Net Margin%	27%	20%	22%	22%
Dividend Payout Ratio (total)	60%	60%	60%	60%
EBITDA to operating CF	97%	100%	100%	100%
GGR Growth	85%	51%	17%	10%
VIP Growth	177%	61%	17%	10%
Mass Growth	15%	41%	20%	10%
EGM Growth	4%	17%	13%	12%
EBITDA Growth	25%	20%	22%	10%
Net Profit Growth	39%	16%	24%	11%

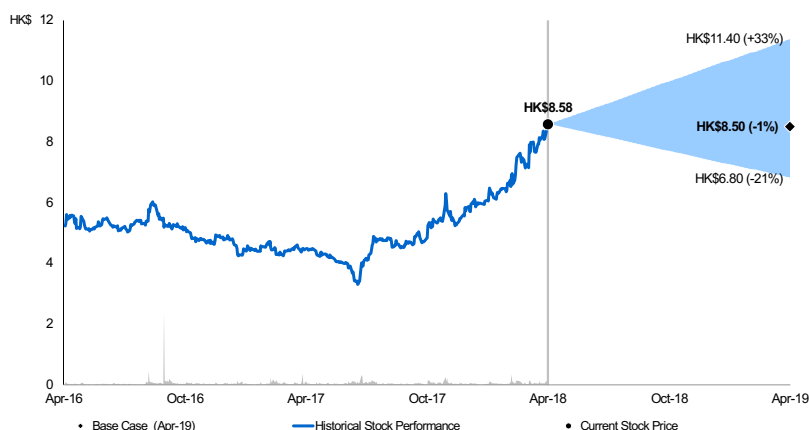
Operating Data

VIP Tables (avg)	229	264	280	280
Mass Tables (avg)	112	166	196	196
EGM Machines (avg)	1,949	2,500	3,000	3,500
VIP win/table/Day (US\$)	7,498	10,461	11,507	12,658
Mass win/table/Day (US\$)	3,679	3,495	3,564	3,921
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



Source: Morgan Stanley Research estimates

Price Target **HK\$8.50**

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

Bull **HK\$11.40****6.0% recurring FCFE yield 2019e**

Stronger visitation growth; quicker than expected ramp of Naga2.

Base **HK\$8.50****8.0% recurring FCFE yield 2019e**

Continued Naga 2 ramp in 2018/19. VIP revenue growth of 60% in 2018 and 17% in 2019; mass revenue growth of 35% in 2018 and 20% in 2019.

Bear **HK\$6.80****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 in strong VIP and mass earnings.
- Less attractive valuation trading at 8% FCFE yield, 10x EV/EBITDA, and 12x P/E on our 2019 estimates.

Key Value Drivers

- Visitors growth, especially from China
- VIP roll, driven by new junkets addition (Suncity on 1 March 2018 and Meg-Star in 2Q18)
- Naga2 boost with at least 300 tables, 903 rooms, 2500 slots and additional non-gaming areas

Potential Catalysts

- Stronger than expected earnings growth in 2018
- Meg-Star opening in 2Q18
- 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, etc.)
- **Upside:**
 - Faster ramp of Naga 2
 - Dividend increase

Investment Conclusion

In our assumption report on 5 March 2018 ([Monopoly Casino License, BRI Beneficiary - Assuming Coverage with OW Rating](#)), we highlighted our preference for the stock based on its monopoly casino license in Phnom Penh, BRI benefits, stable dividend and better tax profile. We continue to believe that the opening of Naga2 could drive EBITDA growth of >20% p.a. through 2020. However, the stock has seen multiple re-rating from 7x to 10x 12M EV/EBITDA based on consensus numbers since the opening of Naga 2 in November 2017, and we see limited upside unless the company grows faster than our and consensus expectations.

While the stock rallied after the company reported strong YoY growth in 1Q18 GGR, the number came in below our expectation by 24%. VIP rolling was below our forecast by 36%, and fell 44% QoQ to US\$5.6bn. If we annualize the 1Q18 run-rate, full-year GGR and VIP rolling would be 27% and 34% below our estimates respectively. However, we think the gap is likely to narrow in upcoming quarters with strong mass visitation and the help of junkets (ramp of SunCity and addition of MegStar in 2Q18).

The stock is now trading at 12x EV/EBITDA with 7% FCFE yield on our 2018 estimates. This is the highest multiple the stock has ever traded at, and seems rich to us. Even though we have increased our PT to HK\$8.50 (from HK\$8.20) by using a higher multiple of 8% FCFE yield (earlier 9%), we see limited upside and thus downgrade to EW. We believe a higher multiple is justified based on strong visitation and revenue YOY growth registered by the company YTD. The implied EV/EBITDA multiple is similar to Bloomberry, another regional casino under our coverage.

Exhibit 2: 1Q18 operations data vs. our estimates

US\$ mn	1Q17	4Q17	1Q18	QOQ	YOY	1Q18 A vs. E	1Q18 Run-rate	2018E	Run-rate vs. E
GGR (ex one-off slot)	87	380	243	-36%	181%	-24%	973	1,336	-27%
VIP roll	3,733	10,123	5,644	-44%	51%	-36%	22,576	34,170	-34%
VIP revenue	37	314	169	-46%	354%	-33%	677	1,008	-33%
Win rate	1.00%	3.11%	3.00%	-3%	200%	5%	3.00%	2.95%	5bps
Mass drop	169	221	264	19%	56%	8%	1,055	1,144	-8%
EGM Bills-in	417	496	515	4%	24%	-14%	2,062	2,325	-11%
Total mass volume	587	718	779	9%	33%	-7%	3,117	3,469	-10%

Note: Numbers in blue are actual numbers provided by the company. VIP revenue and win rate are calculated based on our assumptions. Source: Company data, Morgan Stanley Research estimates.

What's changed?

Revenue: We lowered our revenue forecasts by 5% in both 2018 and 2019, to US\$1.5bn and US\$1.7bn, respectively, still above consensus by 3% and 8%. We cut our VIP revenue estimates by 13% and 14% for the respective years as we reduced the number of VIP tables from 365 to 280 by end-2019. We now forecast 12 more VIP tables to be added for MegStar VIP Hall opening in 2Q18. We raised our mass revenue forecasts by 2% for 2018 and 11% for 2019 based on more tables and higher table yield assumptions, driven by strong visitation growth.

EBITDA: Our EBITDA estimates of US\$374m and US\$455m are below consensus by 14% for 2018 and 8% for 2019, largely reflecting inclusion of potential gaming tax of 5% starting 2018. Excluding the tax impact, we are still above consensus EBITDA by 9% in 2019, although those estimates have also risen recently. Reflecting our expectations of a better mix with stronger mass but weaker VIP, our 2018 EBITDA estimate declines 2% while our 2019 forecast is unchanged.

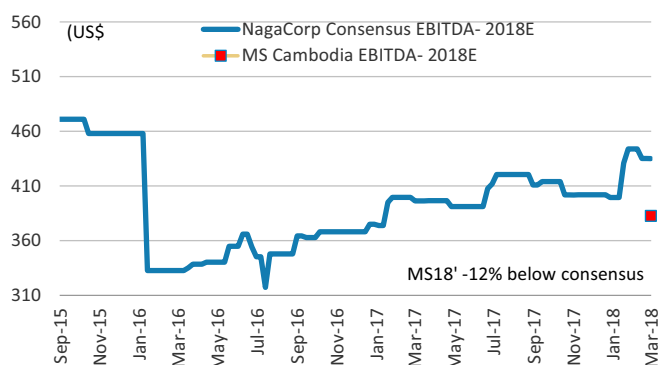
Exhibit 3: Earnings revisions and comparisons with consensus

US\$ mn	MS			YoY growth			Consensus		Variance	
	2017	2018E	2019E	2017	2018E	2019E	2018E	2019E	2018E	2019E
Revenue	956	1,458	1,704	80%	52%	17%	1,411	1,576	3%	8%
EBITDA	312	374	455	25%	20%	22%	435	494	-14%	-8%
EBITDA before gaming tax adj.	312	444	537	25%	42%	21%	435	494	2%	9%
Net Income	255	295	367	39%	16%	24%	313	354	-6%	4%
EPS (US cents)	7.9	6.8	8.4	1%	-14%	24%	7.2	8.0	-6%	6%

US\$ mn	New			YoY growth			Old		Variance	
	2017	2018E	2019E	2017	2018E	2019E	2018E	2019E	2018E	2019E
Revenue	956	1,458	1,704	80%	52%	17%	1,535	1,794	-5%	-5%
EBITDA	312	374	455	25%	20%	22%	383	454	-2%	0%
Net Income	255	295	367	39%	16%	24%	303	364	-3%	1%
EPS (US cents)	7.94	6.79	8.45	1%	-14%	24%	6.97	8.39	-3%	1%

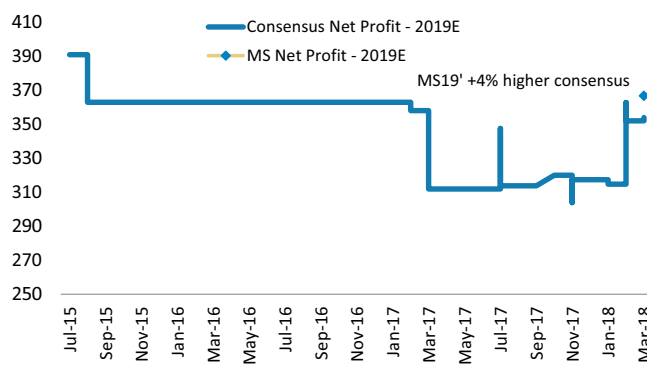
Source: Thomson Reuters, Morgan Stanley Research (E) estimates

Exhibit 4: Consensus EBITDA revision history



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

Exhibit 5: Consensus net income revision history



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

Exhibit 6: Revenue and productivity forecast revisions

US\$ mn	Actual			New		Old		New vs. Old	
	2015	2016	2017	2018E	2019E	2018E	2019E	2018E	2019E
VIP revenue	223	226	625	1,008	1,176	1,160	1,371	-13%	-14%
Mass revenue	121	130	150	212	255	208	229	2%	11%
EGM revenue	134	127	143	184	220	182	211	1%	4%
GGR	478	483	918	1,403	1,651	1,550	1,811	-9%	-9%
Revenue growth YoY	2015	2016	2017	2018E	2019E	2018E	2019E	2018E	2019E
VIP revenue	18%	1%	177%	61%	17%	86%	18%	-28%	-8%
Mass revenue	11%	7%	15%	41%	20%	39%	10%	6%	102%
EGM revenue	12%	-5%	12%	28%	20%	27%	16%	4%	26%
GGR	15%	1%	90%	53%	18%	69%	17%	-23%	5%
Productivity (US\$)	2015	2016	2017	2018E	2019E	2018E	2019E	2018E	2019E
VIP w/t/d	3,311	3,015	7,498	10,461	11,507	10,092	10,294	4%	12%
Mass w/t/d	3,872	4,083	3,679	3,495	3,564	3,584	3,154	-2%	13%
EGM w/u/d	231	211	201	201	201	223	229	-10%	-12%
Productivity growth YoY	2015	2016	2017	2018E	2019E	2018E	2019E	2018E	2019E
VIP w/t/d growth	-19%	-9%	149%	40%	10%	35%	2%	NA	NA
Mass w/t/d growth	14%	5%	-10%	-5%	2%	-3%	-12%	NA	NA
EGM w/u/d growth	8%	-9%	-4%	0%	0%	11%	3%	NA	NA

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

Valuation

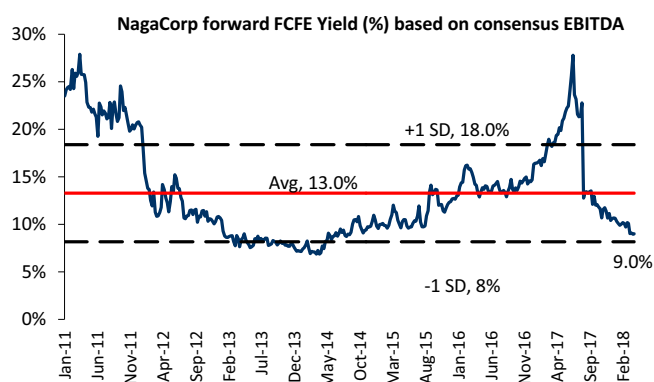
Our price target of HK\$8.50 is based on 8% FCFE yield (previously 9%) on 2019e, above the Macau peers' average of 6.0%. Our 8% target FCFE yield is below the long-term average of 13% since 2011 in view of its monopoly position in Phnom Penh in the fast-growing market of Cambodia, as well as its stable dividend and tax profile. However, we consider the stock as fairly priced trading at 9% forward FCFE yield and 10x 12M EV/EBITDA on consensus numbers, and with no upside to our price target.

Exhibit 7: FCFE Valuation and multiples

FCFE Valuation				
FCFE Valuation (US\$ mn)	2017	2018E	2019E	2020E
Company EBITDA	312	374	455	502
Less: Income tax*	(8)	(3)	(3)	(3)
Less: Maintenance Capex	(50)	(70)	(70)	(70)
FCFE	254	301	383	429
Target FCFE Yield			8.0%	
Equity Value	3,173	3,768	4,784	5,367
Number of shares			4,341	
Price Target (HK\$)			8.50	
Upside/downside			-1%	
Current multiples				
	2017	2018E	2019E	2020E
EV/EBITDA	14.3	12.0	9.6	8.3
P/E	17.8	15.4	12.4	11.1
Recurring FCFE Yield	5.6%	6.6%	8.4%	9.5%
Div Yield%	3.2%	3.7%	4.6%	5.1%

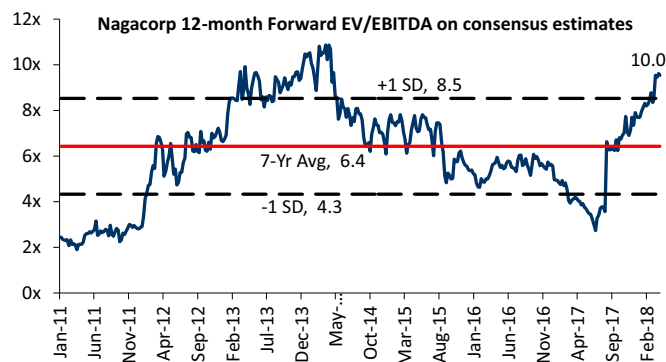
Source: Thomson Reuters data (as of 3 April 2018), Morgan Stanley Research (E) estimates.

Exhibit 8: NagaCorp forward FCFE yield (%) based on consensus EBITDA



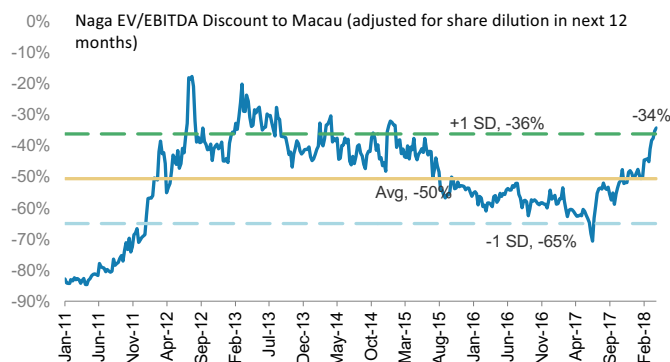
Source: Thomson Reuters data (as of 2 April 2018), Morgan Stanley Research (E) estimates.

Exhibit 9: NagaCorp 12M forward EV/EBITDA on consensus estimates



Source: Thomson Reuters data (as of 2 April 2018), Morgan Stanley Research (E) estimates.

Exhibit 10: NagaCorp EV/EBITDA discount vs. Macau on consensus estimates



Source: Thomson Reuters data (as of 2 April 2018), Morgan Stanley Research (E) estimates.

Exhibit 11: Valuation comps – Macau vs. NagaCorp

3-Apr-18	Current Price LOC\$	Mkt Cap (US\$ m)	6M Avg Vol. (US\$ m)	EV/EBITDA		P/E		Recurring FCFF Yield		Recurring FCFE Yield		Div Yield		Net Debt / EBITDA		2017 Perf.	2018 Perf.
				2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2017E	2018E	2017E	2018E		
MACAU																	
Sands China	42.50	43,423	81	16.0	14.9	19.7	18.3	5.4%	6.0%	5.5%	6.1%	4.7%	4.9%	1.3	1.2	20%	5%
Galaxy	72.65	39,161	100	16.1	13.9	22.8	19.5	6.0%	6.9%	5.5%	6.3%	1.0%	1.3%	(2.2)	(1.9)	87%	14%
Wynn Macau	28.50	18,835	36	14.4	13.2	19.2	17.2	6.6%	7.1%	6.8%	7.4%	3.4%	5.2%	2.7	1.7	101%	15%
MGM China	20.45	9,804	25	15.1	9.5	29.5	15.6	5.9%	9.7%	5.9%	9.3%	1.0%	2.9%	3.1	1.5	47%	-14%
SJM	6.77	4,917	14	10.4	9.0	18.4	28.3	8.4%	9.4%	7.3%	9.3%	3.0%	3.2%	(2.4)	(0.9)	15%	-3%
Simple average				14.4	12.1	21.9	19.8	6.5%	7.8%	6.2%	7.7%	2.6%	3.5%	0.5	0.3	54%	3%
ASEAN Gaming																	
Genting Singapore	1.07	9,869	26	8.5	8.1	17.7	16.8	11.2%	10.9%	7.3%	7.6%	3.3%	3.3%	(2.3)	(2.5)	45%	-17%
NagaCorp	8.58	4,480	5	11.8	9.4	16.1	12.9	6.9%	9.0%	6.8%	8.6%	3.2%	4.7%	(0.2)	(0.1)	138%	34%
Simple average				10.4	8.9	18.1	16.5	8.8%	10.0%	7.3%	8.3%	2.2%	2.8%	(0.7)	(0.3)	87%	16%

Source: Thomson Reuters data (as of 3 April 2018), Morgan Stanley Research (E) estimates.

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Global Stock Ratings Distribution

(as of March 31, 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 MISC
Overweight/Buy	1189	38%	315	41%	26%	555	39%
Equal-weight/Hold	1355	43%	364	47%	27%	644	45%
Not-Rated/Hold	53	2%	4	1%	8%	7	0%
Underweight/Sell	545	17%	84	11%	15%	214	15%
TOTAL	3,142		767			1420	

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.

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

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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.

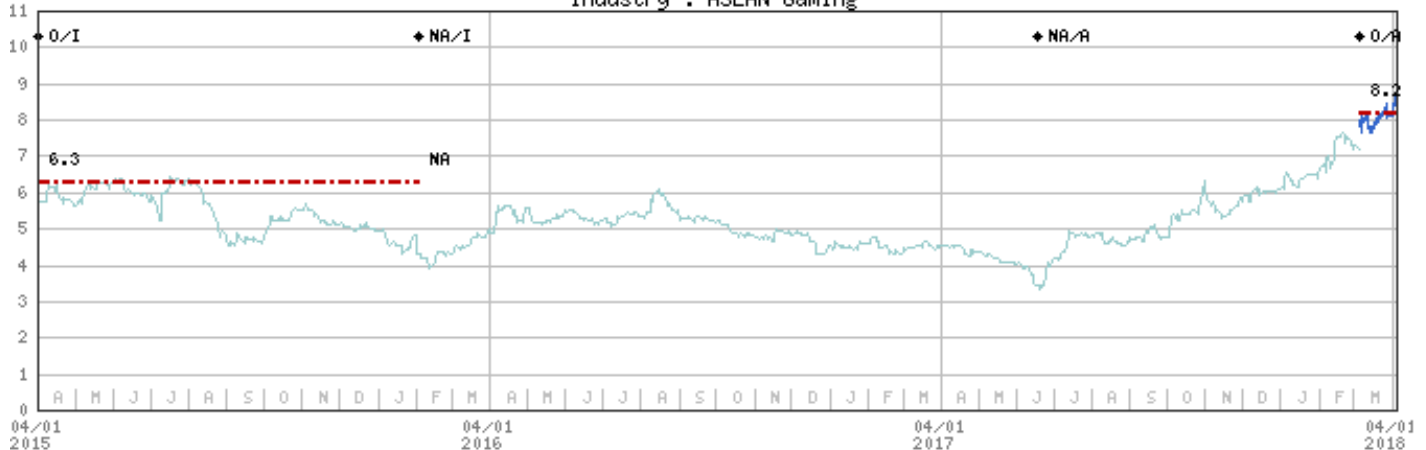
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.

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)

NagaCorp (3918.HK) - As of 4/3/18 in HKD
Industry : ASEAN Gaming



Stock Rating History: 4/1/15 : 0/I; 2/3/16 : NA/I; 6/18/17 : NA/A; 3/6/18 : 0/A

Price Target History: 3/19/15 : 6.3; 2/3/16 : NA; 3/6/18 : 8.2

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)

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INDUSTRY COVERAGE: ASEAN Gaming

COMPANY (TICKER)	RATING (AS OF)	PRICE* (04/03/2018)
Praveen K Choudhary		
Bloomberry Resorts Corporation (BLOOMP.S)	O (03/26/2018)	PP14.30
Genting Singapore PLC (GENS.S)	E (02/26/2018)	S\$1.07
NagaCorp (3918.HK)	E (04/03/2018)	HK\$8.58

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* Historical prices are not split adjusted.

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