

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

BUY

HOLD

SELL

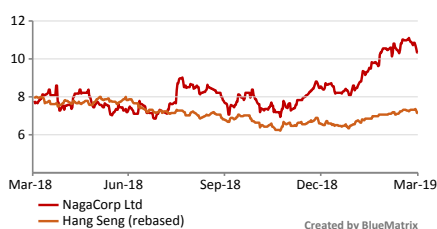
Target Price: HK\$14.00 Current Price: HK\$10.32

52-Week High HK\$11.46
52-Week Low HK\$6.53
EV (MM) HK\$44,002
Market Cap (MM) HK\$44,799
Shares Outstanding (MM) 4,341
Average Daily Trading Volume (MM) 6.3

Priced as of close on 8 March 2019.

Source: FactSet

Price Performance



Source: FactSet

A Golden Dragon Rising in Southeast Asian Gaming

- **NagaCorp owns Phnom Penh's only gaming property: it holds a monopoly on gaming within 200km of the city until 2035. Cambodia is a supply-driven market with high ROI, while products and services continue to be upgraded.**
- **Ramp-up of Naga2 in FY18 was impressive and has further to go. Junket rooms continue opening, while mass ramp-up remains on track. Initiate at BUY with a TP of HK\$14, based on 12x FY19E EV/EBITDA, in line with Macau peers.**

High ROI in a supply-driven market. The company's NagaWorld Phase 2 opened in November 2017. Its ramp-up in the first full year of operation was impressive: hotel rooms/gaming tables increased by 130%/50%, while FY18 gross gaming revenue (GGR) and EBITDA jumped 55% and 60% YoY, respectively. Capex of Naga2 and NagaCity Walk totaled US\$400mn, and the project brought in an additional US\$190mn in EBITDA to the whole NagaWorld complex in 2018 vs. 2017, implying a 48% return on investment.

NagaCorp set to outshine Macau peers in 2019. We expect NagaCorp to record 20% YoY growth in FY19E GGR and EBITDA, with new junket rooms opening and a gradual ramp-up in the slower-growing mass market. By contrast, we expect Macau gaming peers to suffer a YoY GGR decline in 1H19 given the tough China macro environment. With an elevated standard of product and service since the opening of NagaWorld Phase 2, NagaCorp has continued to narrow the gap in the visitor experience between Macau's casinos and NagaWorld, while its high commissions serve to incentivize junkets.

Valuation discount should continue narrowing. With a promising growth outlook and higher ROI than its Macau peers, we believe NagaCorp's valuation gap will continue narrowing, especially with the removal of the overhang related to convertible notes that were converted in 2017. We initiate coverage with a BUY rating and 36% potential upside to our 12-month target price of HK\$14.00. Our target price is based on 12x FY19E EV/EBITDA, which is in line with the Macau gaming sector average.

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.

Summary Financial Data

| Highlights | 2018A | 2019E | 2020E | 2021E |
|-------------------|-------|-------|-------|-------|
| Revenue (MM) (\$) | 1,474 | 1,767 | 1,980 | 2,255 |
| EBITDA (MM) (\$) | 512 | 612 | 689 | 799 |
| EPS (\$) | 0.09 | 0.11 | 0.12 | 0.15 |
| EV/EBITDA | 11x | 9x | 8x | 6x |
| P/E | 15x | 12x | 11x | 9x |
| FCF yield | 4% | 7% | 11% | 12% |
| Dividend yield | 4.1% | 4.9% | 5.5% | 6.9% |

Source: China Renaissance Securities (Hong Kong) Limited

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON APPENDIX A

Investment thesis

Monopolistic position in a market where supply drives demand

NagaCorp's 70-year casino license will last until 2065, while its monopoly position within a 200km radius of Phnom Penh, Cambodia, will expire in 2035. Located in the city center of Phnom Penh, NagaWorld is the only integrated hotel-casino entertainment complex in the city and only casino owned by a public company in Cambodia, which we believe will lead gaming players in the country and high rollers from Southeast Asian (SEA) countries to have more confidence in the casino floor management at NagaWorld.

Protected by a monopoly license, the gaming supply is controlled by NagaCorp, which built NagaWorld 1 and 2 in 2003 and 2017, respectively. However, demand is growing due to: 1) increasing visitor arrivals with improving infrastructure, 2) fast economic growth of Cambodia and surrounding countries boosting the consumption power of expatriates and SEA high rollers, and 3) the gradually tightening relationship with overseas junket operators that are motivated to bring more high rollers to NagaWorld, where they earn higher commissions.

In our view, Phase 2's ramp-up in the first year after opening was impressive: hotel rooms/gaming tables increased by 130%/50%, while FY18 gross gaming revenue (GGR)/EBITDA jumped 55%/60% YoY, respectively. Total capex of Naga2 and NagaCity Walk was US\$400mn, and the project helped bring in an additional US\$190mn in EBITDA to the whole NagaWorld complex in 2018 vs. 2017, implying a 48% return on investment.

The surprise from NagaWorld Phase 2 is not over

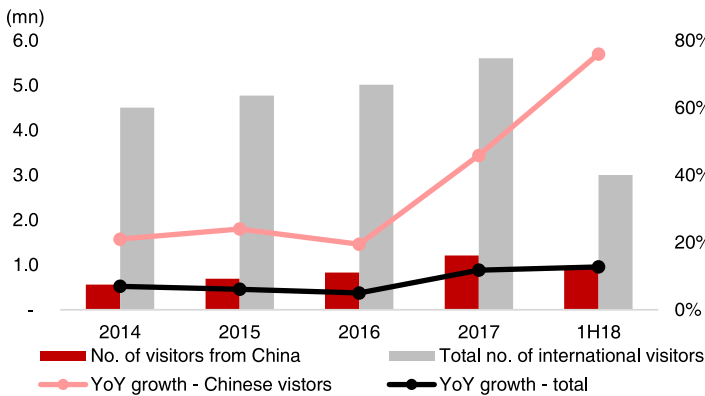
We expect NagaCorp to book another record-breaking GGR/EBITDA with 20%/20% YoY growth, respectively, in FY19E, while we expect Macau peers may suffer from a YoY GGR decline in 1H19E due to decreasing consumption power and visiting frequency from high rollers. With an elevated standard of products and services after opening Phase 2, NagaCorp has continued to narrow the gap of guests' experience between world-class Macau integrated resorts and NagaWorld, while its high junket commissions backed by favorable tax policy are another attraction liked by junket operators. With new junket room openings and a gradual ramp-up of the mass market (which ramps up more slowly than VIP usually), we believe NagaCorp will outshine its Macau peers in FY19.

Valuation discount to Macau should continue narrowing

With a promising growth outlook and higher ROI than its Macau peers, we believe the valuation gap will continue narrowing, with the overhang related to convertible notes removed. Our 12-month target price is based on 12x FY19E EV/EBITDA, which is in line with the Macau gaming sector valuation. We initiate coverage at BUY with a TP of HK\$14.

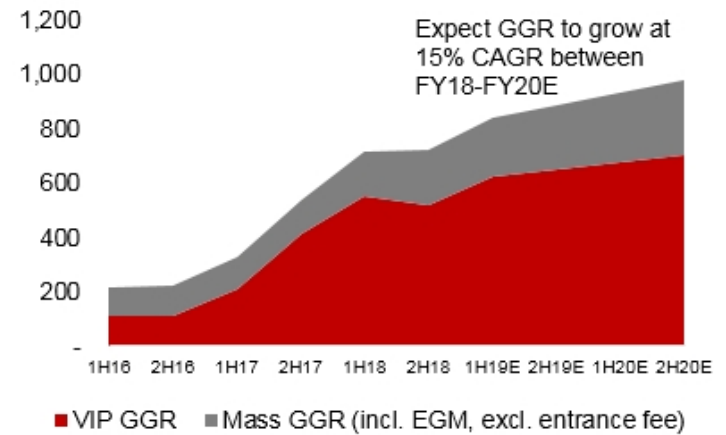
Catalysts are: 1) continued support from the Cambodian government in promoting the tourism industry, improving further foot traffic to NagaWorld. 2) A more favorable regulatory environment in Phnom Penh and/or Vladivostok, boosting market confidence in this newly emerging gaming hub in Southeast Asia.

Exhibit 1 - Increasing visitations from China



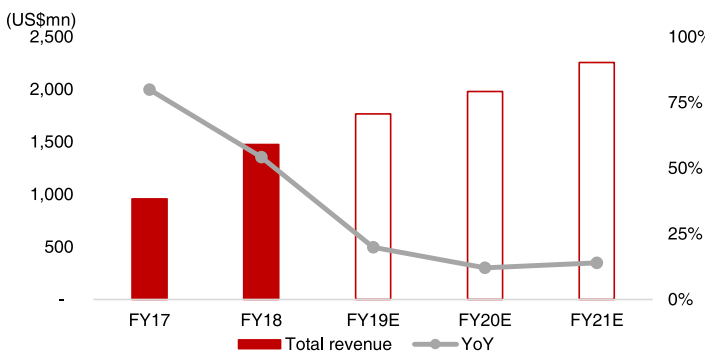
Source: Cambodia Ministry of Tourism, CRSHK compiled

Exhibit 2 - NagaWorld GGR breakdown and forecasts



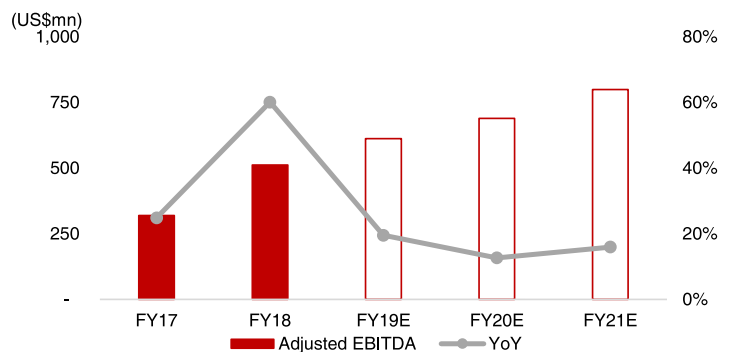
Source: Company data, CRSHK estimates

Exhibit 3 - NagaCorp revenue projections



Source: Company data, CRSHK estimates

Exhibit 4 - NagaCorp adj. EBITDA projections



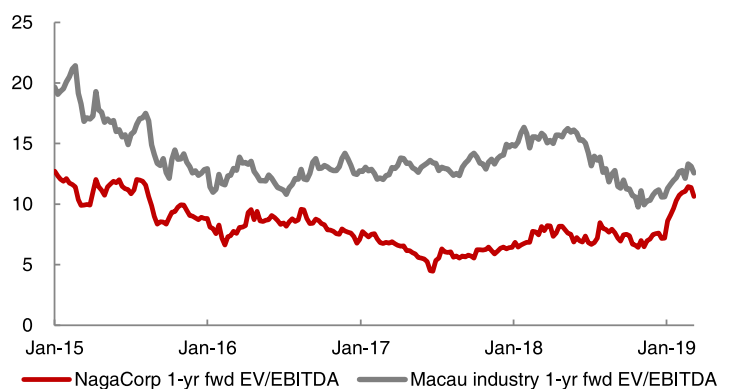
Source: Company data, CRSHK estimates

Exhibit 5 - NagaCorp's one-year forward EV/EBITDA band



Source: Bloomberg, CRSHK estimates

Exhibit 6 - NagaCorp vs. Macau gaming industry 1-year forward EV/EBITDA



Source: Bloomberg, CRSHK estimates

Company introduction

Company background

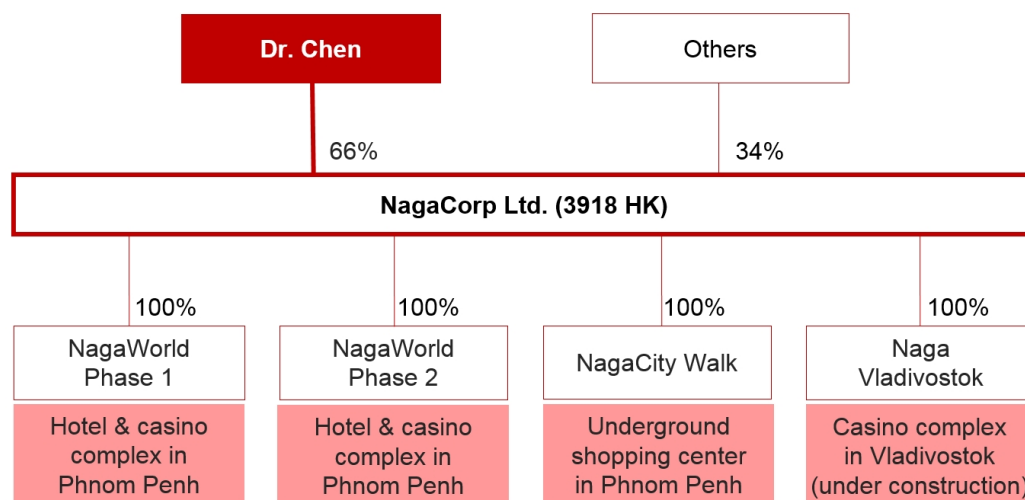
NagaCorp is the largest casino operator in Cambodia in terms of gross gaming revenue. It enjoys a 70-year casino license until 2065, and holds a monopoly license as the only casino operator within a 200km radius of Phnom Penh until 2035. Flagship property NagaWorld, which includes Phase 1 (Naga1) (opened in 2003) and Phase 2 (Naga2) (opened in 2017), is the only integrated hotel-casino entertainment complex in Phnom Penh. The company announced that NagaWorld Phase 3 in Phnom Penh is being planned, although details have not been disclosed. The company also owns NagaCity Walk, an underground duty-free shopping mall connecting Phases 1 and 2 of NagaWorld.

In addition, NagaCorp is currently expanding its casino business by developing Naga Vladivostok, a hotel and casino complex in the Integrated Entertainment Zone (IEZ) of Primorsky, which is close to Vladivostok and is the only gaming-permitted region in the Russian Far East. The property is under construction and is planned to be operational in 2020.

NagaCorp's founder

CEO Dr. Chen Lip Keong is a Malaysian businessman and real estate developer who started seeking opportunities in Cambodia in the early 1990s, following Malaysia's policy of "Prosper Thy Neighbour" – to encourage the Chinese business community to invest in neighboring countries. The wealthy real estate developer was granted a gaming license in 1993 which is good for 70 years since that date and has a 41-year monopolistic right within a 200km radius of Phnom Penh. First operating the casino business in a leased barge in 1995, Naga Resorts Casino began building the gaming complex called NagaWorld on land in 2000 and moved onshore in 2003. The company was listed in Hong Kong in 2006 and currently has a 34% free float with the remaining 66% controlled by Dr. Chen.

Exhibit 7 - Ownership structure



Source: Company data, CRSHK compiled

Properties in operation – NagaWorld Phases 1 and 2

As the flagship property, NagaWorld Phase 1 (Naga1) started operating in 2003. It originally had around 320 gaming tables, 1,700 electronic gaming machines and 700 hotel rooms. As the only integrated resort in Cambodia, the property's high-end feature at the time – gaming facilities, shopping

gallery, F&B (Food & Beverage) outlets and entertainment services – made it one of the few modern complexes in Cambodia able to accommodate foreign visitors who demand decent services.

Following Naga1’s success, and in order to further attract foreign customers, the company launched Naga2 in November 2017. Compared with Naga1, the new property is more luxurious with the purpose of targeting regional high rollers. Meanwhile, it has nearly doubled NagaWorld’s capacity with an additional ~160 gaming tables, ~900 hotel rooms and a theatre with 2,000 seats. Phases 1 and 2 are connected by NagaCity Walk, an underground retail shopping center opened in 2016 with approximately 13,248 square meters of retail and public space.

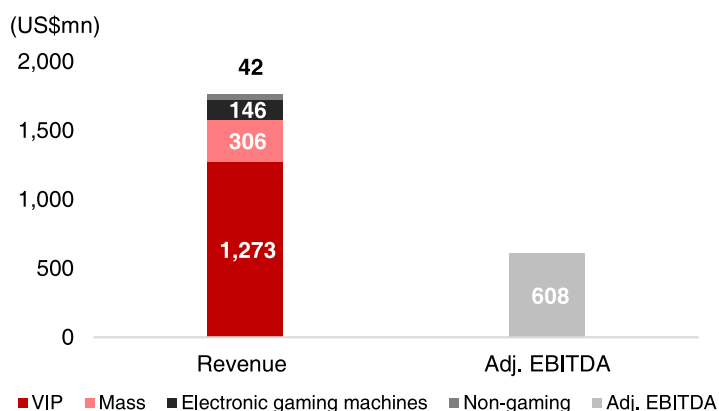
NagaWorld (Phases 1 and 2) is located at the center of Phnom Penh and only 9km away from the airport. By offering free shuttle service, visitors to Phnom Penh by air enjoy easy access to the gaming complex.

Exhibit 8 - NagaWorld (after Phase 2 expansion)

Exhibit 9 - Our FY19E forecast for NagaWorld's GGR and property EBITDA



Source: Company website



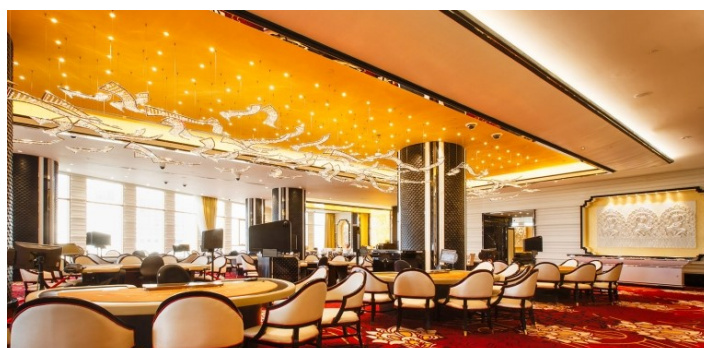
Source: Company reports, CRSHK estimates

Exhibit 10 - Public hall of NagaWorld Phase 1

Exhibit 11 - NagaWorld Phase 2 casino



Source: Company website



Source: Company website

Exhibit 12 - Management background

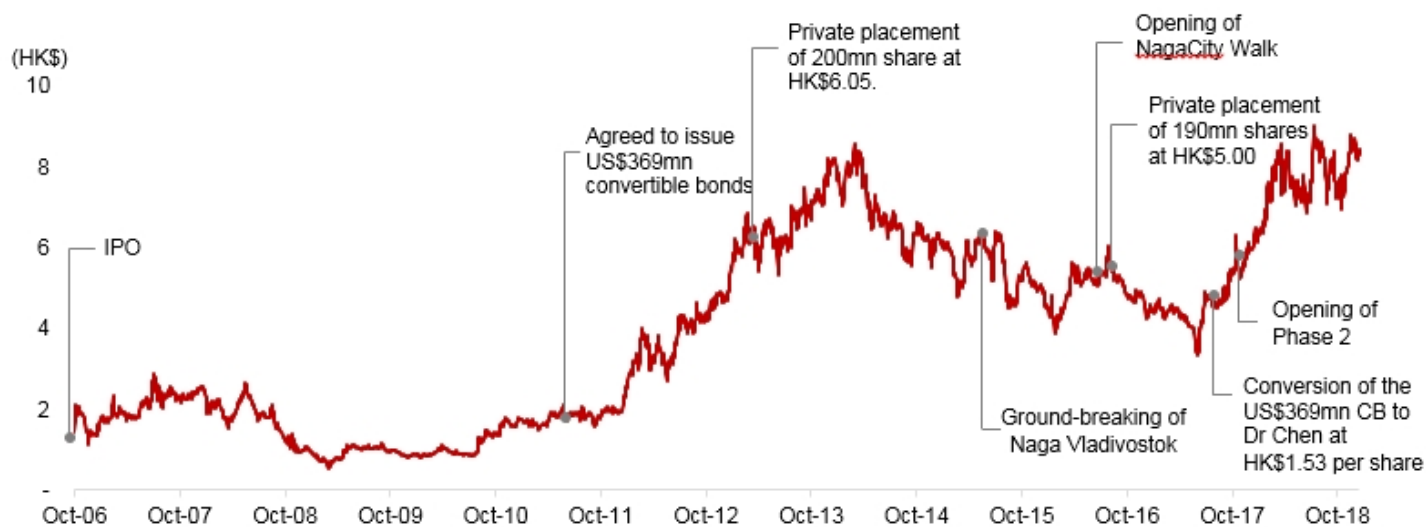
| Name | Position | Profile |
|---------------------------|---------------------------------------|--|
| Timothy Patrick McNally | Chairman | <ul style="list-style-type: none"> Also the chairman of the AML Oversight Committee of the Company Joined the company in 2005 as chairman of the Board Before that, served as executive director of Security and Corporate Legal Services for the Hong Kong Jockey Club Prior to that, worked as Special Agent of FBI for almost 25 years, used to be the head of the FBI's Los Angeles Office |
| Tan Sri Dr Chen Lip Keong | Founder, CEO, Controlling shareholder | <ul style="list-style-type: none"> Extensive business and managerial experiences The controlling shareholder of Karambunai Corp Bhd (KRBN MK), FACB Industries Incorporated Berhad (FACI MK) and Petaling Tin Berhad (PEG MK), all of which are listed on the Bursa Malaysia Securities Berhad Holds a Bachelor of Medicine and Surgery from University of Malaya |
| Tan Sean Czoon | CFO | <ul style="list-style-type: none"> CFO since March 2018 Previously worked as Vice President of Business Development Joined the Group in 2013 Before joining the Company, worked under asset management division of Deutsche Bank (Hong Kong) Chartered Accountants (Australia & New Zealand), CFA |

Source: Company data

Exhibit 13 - Company history

| Year | Event |
|------|---|
| 1994 | Dr. Chen's private company Ariston won the bidding for building an infrastructure-tourism development in the Sihanoukville region, South Cambodia. |
| 1995 | Naga Resorts Casino was officially launched on a barge which was anchored on the bank of Bassac River, central of Phnom Penh. |
| 2003 | Relocated casino from the barge to the ground floor of the entertainment wing of NagaWorld. |
| 2006 | Listed on the Main Board of the Hong Kong Stock Exchange. |
| 2011 | Issued US\$369mn worth of CBs to Dr Chen, which can be converted when NagaCity Walk and Phase 2 were completed. |
| 2012 | Held a ground-breaking ceremony for the NagaWorld Phase 2 development in November. |
| 2013 | Private placement of 200mn new shares at HK\$6.05 for its overseas high-premium direct-players program. |
| 2014 | Ministry of Economy and Finance of Cambodia reaffirmed that company continues to enjoy the exclusivity until the end of 2035. |
| 2015 | Held a ground-breaking ceremony for the Vladivostok IEZ project. |
| 2016 | Opening of NagaCity Walk. |
| 2016 | Private placement of 190mn new shares at HK\$5.00 for the fit-out of Naga Phase 2. |
| 2017 | Conversion of CBs that issued to Dr Chen in 2011 to 1,881mn shares at HK\$1.53 per share, due to the completion of NagaCity Walk and Phase 2. Total share capital increased 76% and Dr Chen's substantial shareholding increased from 39% to 65%. |
| 2017 | Opening of NagaWorld Phase 2. |

Source: Company data, CRSHK compiled

Exhibit 14 - Naga share price performance with major events highlighted


Source: Bloomberg, Company data, CRSHK

Exhibit 15 - Summary of properties under Naga

| Name | NagaWorld 1 | NagaCity Walk | NagaWorld 2 | Naga Vladivostok |
|------------------|-------------|---------------|--------------|------------------|
| Opening date | 2003 | Aug 17, 2016 | Nov 05, 2017 | 2020E |
| Gross floor area | 113,307sqm | 13,248sqm | 96,857sqm | 301,242sqm |
| Hotel rooms | 1,658 | n.a. | 1,033 | 2,719 |
| Gaming tables | 320 | n.a. | 160 | >100 |
| Slot machines | 1,700 | n.a. | 2,500 | >500 |
| Project cost | n.a. | \$94mn | \$275mn | \$350mn |

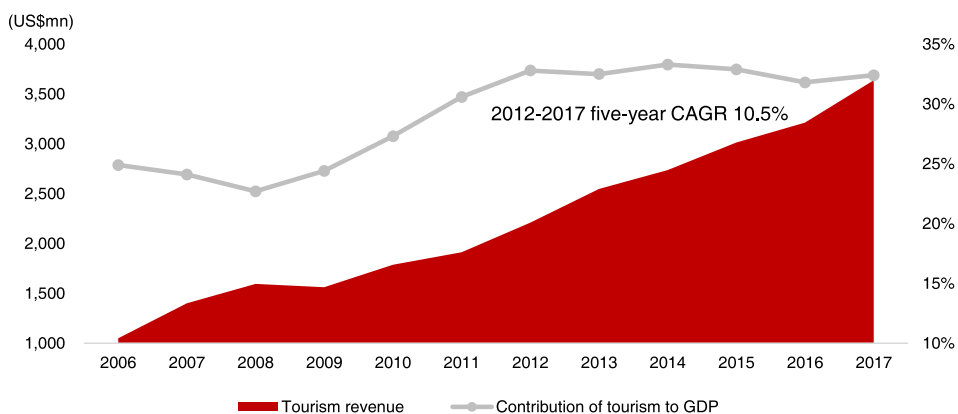
Source: Company data, CRSHK compiled

A favorable environment for the gaming industry in Cambodia

A growing tourism industry and better accessibility

As the political environment in Cambodia is stabilizing, the country has been able to attract a growing number of tourists from neighboring countries. According to the Cambodia Ministry of Tourism, the total inbound visitation to Cambodia has increased from 2.5mn in 2010 to 5.6mn in 2017. As a result, Cambodia's tourism industry revenue is growing at a 10% five-year CAGR through 2017, reaching US \$3,638mn. The tourism industry has become an important economic pillar and accounted for 32.4% of Cambodia's total GDP in 2017, based on data from the World Travel & Tourism Council.

Exhibit 16 - Cambodia's tourism revenue and its contribution to total GDP



Source: World Travel & Tourism Council, CRSHK compiled

Cambodia is located in the center of Southeast Asia – a natural geographic advantage for attracting visitors from neighboring countries. It has adopted a relaxed visa policy as a way of boosting the tourism industry. In 2017, neighboring countries including Vietnam, Laos and Thailand, jointly contributed 31% to Cambodia's inbound tourism totals. The total number of visitations to the country increased around 12% YoY in FY17 and 1H18, and is expected to have reached 6.3mn in 2018, according to Cambodia's Ministry of Tourism. We see great potential for Cambodia to grow its inbound tourism industry. According to statistics from the tourism ministries of Thailand and Vietnam, which have more developed tourism industries, the two countries received 38.3mn and 15.5mn international tourists each in 2018, compared with Cambodia's 6.3mn.

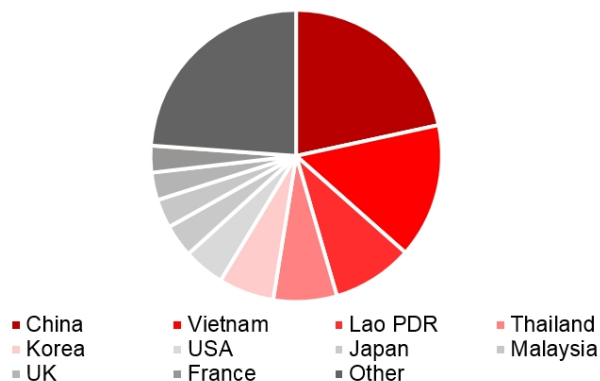
Exhibit 17 - Visa requirements to Cambodia



Source: Cambodia Immigration

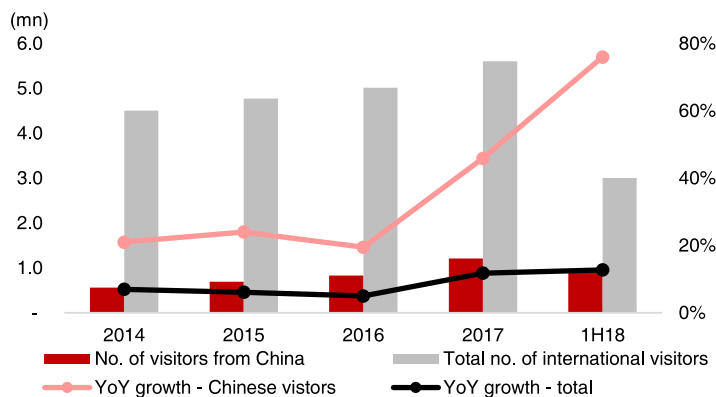
In recent years, China has become a new growth driver for Cambodia's inbound tourism. According to the Cambodian Tourism Ministry, China has surpassed Vietnam to become the top country for tourist arrivals in Cambodia since 2017. The number of Chinese visitors grew 46% YoY in 2017 and 71% YoY in the first nine months of 2018. We expect the strong growth momentum to continue due to the close geopolitical ties between these two countries. In addition, China's One Belt One Road project (OBOR) could potentially bring in more foreign direct investment (FDI) to political allies like Cambodia, and Chinese visitors will also come along with those investments. The Cambodian government is targeting to receive ~2mn arrivals from China in 2020 as compared to the 1.21mn it reported for 2017. This implies an 18% annual growth rate. We believe this is a conservative target – after all, it is modest in comparison with the 9.70mn Chinese arrivals recorded in Thailand in 2018, and the 4.96mn Chinese visitors to Vietnam in 2018, as disclosed by the two countries' tourism ministries.

Exhibit 18 - Top tourism source countries to Cambodia by 2017



Source: Cambodia Ministry of Tourism, CRSHK compiled

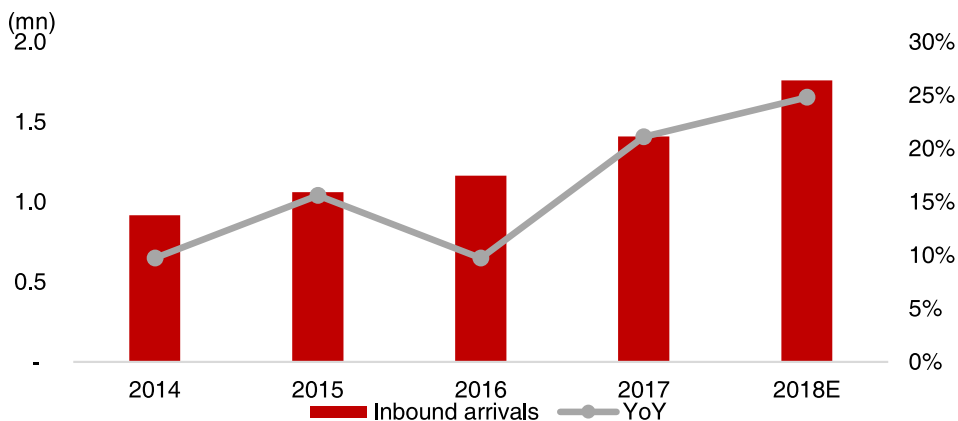
Exhibit 19 - Increasing visitations from China



Source: Cambodia Ministry of Tourism, CRSHK compiled

Phnom Penh, the capital of Cambodia and where NagaWorld is located, is developing its infrastructure to accommodate the increase in visitors. Inbound arrivals and direct flights to Phnom Penh airport, 8km west of the city center, have increased over the years. We believe the uptrend of visitor arrivals to Phnom Penh airport should benefit NagaWorld as the company can easily solicit those visitors to visit its gaming complex via its free shuttle bus service.

Exhibit 20 - Inbound arrivals of Phnom Penh Airport



Source: Cambodia Ministry of Tourism, CRSHK compiled

In January 2018, the Cambodian government approved a proposal to build a new airport to serve Phnom Penh. The new international airport will replace the existing Phnom Penh Airport, with its initial plans to build adjacent to a large lake, about 30km south of Phnom Penh. The planned 2,600 hectares land area is six times larger than the existing Phnom Penh Airport's 400 hectares and considerably larger than the Beijing Capital Airport. The new airport is expected to be operational by 2025. We believe an increase in airport capacity will further facilitate Phnom Penh's positioning as a SEA tourism hub and benefit Naga's business in the long run.

Cambodia/Phnom Penh as a new gaming hub

Cambodia's central location in SEA is a natural advantage for its development into a regional gaming hub. As shown below, Phnom Penh is within a 2.5-hour flight from most SEA countries, making it an optimal choice for casino visitors who prefer short-haul travel. While the high-end gaming complex NagaWorld (Phases 1 and 2) caters to high-end customers flying into Phnom Penh, smaller casinos that operate in Cambodia's border cities – Poipet and Bravet – attract low-end high rollers from Thailand and Vietnam who can easily reach those border casinos by land.

Exhibit 21 - 2.5-hour flight time geographical coverage - Phnom Penh, Macau and Vladivostok



Source: Google map

Compared with other gaming-permitted countries in SEA, we believe Cambodia's gaming industry has huge potential to grow due to: 1) its advantageous location and improving accessibility, 2) its fast-growing inbound tourism industry which has laid a good foundation for casinos to expand their

customer base, 3) the relatively cheap standard of living in Cambodia, as compared with other SEA countries, enabling customers to enjoy the same services but with lower spending, and 4) the increasing FDI (Foreign Direct Investment) should continue to bring foreign expats to Phnom Penh. Those deep-pocketed foreigners are increasingly attracted to NagaWorld as the gaming complex is one of the few places with world-class gaming and entertainment facilities.

The following are other SEA gaming destinations:

Singapore and Malaysia: both are well-established gaming destinations with popular integrated resorts catering to SEA's top high-rollers. In our view, the gaming industry in both countries is relatively mature with a stable customer base and low possibility for expansion.

Philippines: established an entertainment zone with four integrated resorts, but domestic crime, terrorism and civil unrest in recent years have increasingly discouraged inbound visitation.

Vietnam: gaming areas are scattered and small in size, while inconvenient transportation is also an overhang.

Exhibit 22 - Major IRs in SEA



Source: World casino directory, CRSHK compiled

Naga is well positioned to capture growth

A monopolistic gaming license plus tax advantages

Although data from the Cambodia Minister of Finance suggests there are over 150 licensed casinos in Cambodia, NagaWorld is the largest (based on GGR) and the only integrated resort in that nation. Its large scale and revenue size outweigh other casinos. The NagaWorld complex alone contributed up to 4.3% of Cambodia's GDP and 26.3% of tourism income in 2017 (measured by NagaWorld's revenue/GDP and tourism income). While a part of Naga's success results from visionary investments and outstanding operation capability by its management, its monopolistic gaming license and tax advantages have also helped fend off potential competition.

Gaming license: NagaCorp was granted a 70-year gaming license that will expire in 2065 – putting it in an advantageous position compared to its Macau peers, who are facing license renewal uncertainties in 2020 and 2022. In addition, NagaCorp also enjoys a 41-year monopoly on casino operations within a 200km radius of Phnom Penh until 2035. With zero competition in the area, we believe Naga is well positioned to benefit from the country's growing tourism industry.

Gaming tax: With no formal Casino Law promulgated by the government, casinos in Cambodia are currently free from gaming tax and license fees. This compares with gaming tax (tax on gross gaming revenue) of around 39% in Macau, 7.75% in Nevada and 12%-22% in Singapore. However, news sources (e.g., VOA News and I Gaming Times) reported in 2018 that the Cambodian government is close to setting a 4%-5% uniform gaming tax on all casinos, although no timeframe for implementation has been discussed.

Exhibit 23 - Gaming tax levied in different countries/regions

| Region/Country | Effective tax rate on GGR | Details |
|----------------|---------------------------|--|
| Macau | 39% | 35% basic gaming tax + 1.6% contribution to Macau Foundation + 1.4% - 2.4% contribution to infra/tourism/social security fund. |
| Singapore | 12% - 22% | Premium players*: 5% of gaming tax + 7% goods and services tax Other players: 15% gaming tax + 7% goods and service tax |
| Nevada | 7.75% | 6.75% gaming tax + 1% tax in fees |

Source: DICJ, Inland Revenue Authority of Singapore, Nevada Gaming Control Board, CRSHK compiled. Note * above: premium players refer to players who deposited over SGD100,000 (c. US\$74,000) before start playing in the casino.

Even if new gaming tax regulation remains an overhang to NagaCorp's earnings, we do not see substantial risk to the company given its premium location and monopoly position in Cambodia currently.

Profit tax: the company is also exempted from the 20% profit tax for Cambodian corporations. Instead, it makes obligation payments to the government, which are subject to negotiation and not tied to its revenue. As a result, the company generally enjoys a lower effective tax rate than its regional peers of about 5%, although this may reach 10% in some years due to one-off additional obligation payments.

The number of SEA customers keeps growing with China as a new source

Different from border casinos that target low-end customers from neighboring countries, NagaWorld welcomes expats and foreign nationals to the mass floor, while the VIP gaming area caters to high rollers from Malaysia and other SEA nations that tend to visit different casino properties periodically in Singapore, Malaysia and Cambodia. In fact, we believe NagaCorp's status as a public company has also enhanced customers' confidence in the fairness of its house towards its players.

While NagaWorld's major clients are from SEA... That NagaWorld has become one of the top gaming destinations for SEA customers is reflected in its robust financial results. The company's revenue and EBITDA grew at a 34%/24% five-year CAGR (FY13-FY18). The mass segment contributed to the majority of the company's gross profits, with segment GGR growing steadily, backed by customers from its neighboring countries and expats holding foreign passports. VIP GGR continued growing thanks to the capacity expansion after Naga2's opening and wider coverage of junket operators including not only Malaysian junkets but Macau junkets as well. In our view, the growth in VIP rolling demonstrates NagaWorld's evolving reputation as a top integrated resort in SEA.

...The new source of clients is still from SEA, and now also from China. While mass GGR has been driven by expats residing in Cambodia, c.60% of VIP rolling has been driven by SEA clients. Naga2's opening at the end of 2017 has enlarged the capacity, while existing SEA junkets dedicated to Naga1 have started to expand their business to include SEA high rollers for Naga2. Therefore, up until the present, the growth from Naga2 has been mainly from SEA clients.

However, NagaCorp is currently working to attract Chinese high rollers, whose betting size is larger than players from other regions. Some steps taken to accommodate customers from China are:

First, management is adapting its hardware and software to Chinese tourists' taste. NagaWorld has embedded "Chinese elements" in the property by providing signage in Chinese, allocating Mandarin-speaking staff to the front desk and collaborating with China Duty-Free Group to run their duty-free business in NagaCity Walk. China Duty-Free Group's parent company, China International Travel Service (601888 CH, not covered), has a strong presence not only in the duty-free business but also in the China travel industry, enabling NagaCorp to penetrate further into China.

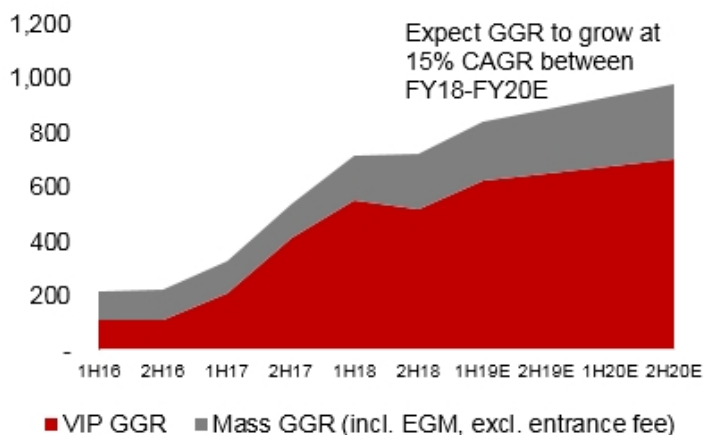
Second, based on the on-going cooperation with the China Duty-Free Group, NagaCorp started providing direct charter flights to Phnom Penh from China's Tier-2 cities through the travel agency arm of China International Travel Service since 3-4 years ago. As a result, NagaWorld is growing its Chinese customer base – currently around 40% of VIPs are from China vs. 25% prior to 2017, according to management.

Third, NagaCorp began appealing to Macau junket operators a few years ago; and this has started showing results over these past two years. With updated hardware after the opening of Phase 2, NagaCorp successfully brought in Macau junket operators such as Suncity Group and Venus Group. Complementary to the existing Malaysia-based junket operators, and thanks to tighter economic collaboration between the two nations, the Macau operators are able to drive two kinds of Chinese high rollers: 1) event-driven Chinese high rollers to Phnom Penh (Macau continues to be the top destination for frequent gamblers), and 2) Chinese people residing in Phnom Penh.

Expecting VIP growth to continue, driving revenue growth

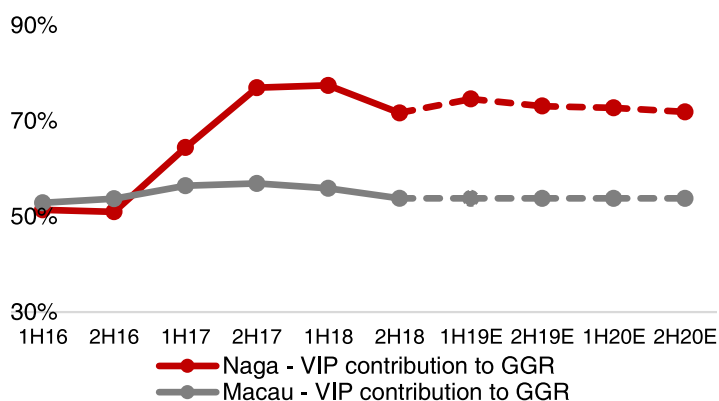
NagaWorld's VIP business has improved significantly since 2017 due to: 1) industry recovery, 2) the company's extended effort to bring in new VIP junkets, and 3) the opening of Naga2 in Nov 2017. VIP rolling, as a result, increased 142%/69% YoY in FY17/18, respectively.

Exhibit 24 - NagaWorld GGR breakdown and forecasts



Source: Company data, CRSHK estimates

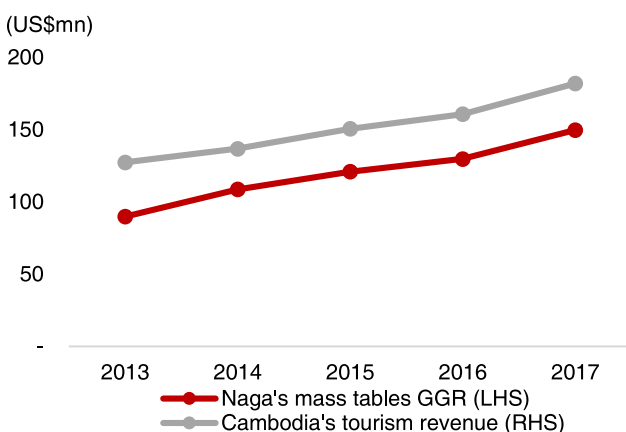
Exhibit 25 - NagaWorld VIP GGR% vs. Macau industry



Source: Company data, CRSHK estimates

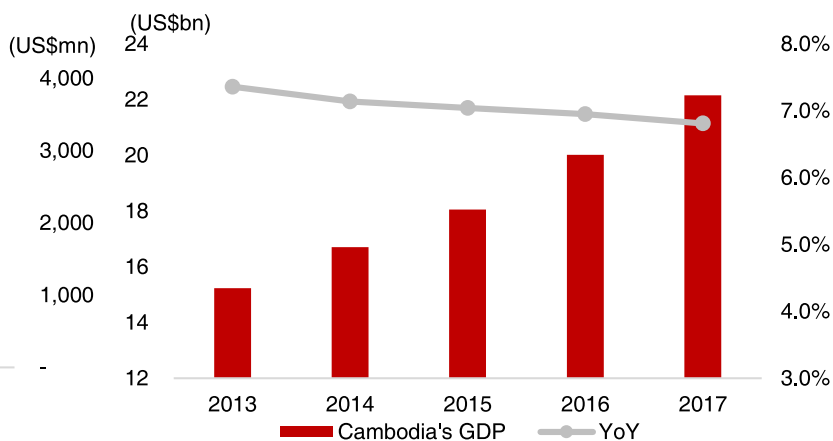
Looking forward, we expect NagaWorld's VIP segment to further expand given: 1) Naga2's luxurious atmosphere and high-end facilities should draw regional high rollers; 2) large Macau based junket operators like Suncity began operations in Naga2 in 1H18, and we expect them to bring in more Chinese customers in 2019; and 3) more Macau junkets are likely to join Naga in the coming years following the top players (Suncity and Venus). We expect NagaWorld's VIP rolling to grow c. 25% in FY19E and to maintain a stable level of 8% growth thereafter (assuming no contribution of Naga3).

Exhibit 26 - NagaWorld mass table GGR vs. tourism revenue in Cambodia



Source: World Travel and Tourism Council, Company data

Exhibit 27 - Cambodia's GDP and growth rate



Source: World Bank

In comparison, NagaWorld's mass GGR (including EGM) has grown steadily at an 16% five-year CAGR through FY18 mainly driven by inbound tourism growth and local expats' contributions. The opening of Naga2, however, led to 52% mass GGR growth in FY18. In the short term, we believe the ramp-up of Naga2 will continue to drive the mass business, delivering 24%/16% GGR growth in FY19E/20E, respectively. In the long term, we expect mass GGR to grow at ~10% per year. Inbound tourism should be the key driver for the mass segment, with local GDP growth being another indicator, given that the mass segment is mainly supported by overseas tourists and local expats.

Exhibit 28 - GDP CAGR comparison between SEA countries 2012-2017



Source: World Bank

NagaWorld was able to maintain an EBITDA margin level of 45%-50% prior to 2017, significantly higher than Macau peers' 20%-30% due to: 1) about 50% of GGR was contributed by the high-margin mass segment before 2017; 2) no gaming tax levied, as compared to a ~40% gaming tax in Macau; and 3) low labor costs. The property's EBITDA margin dropped significantly to 34% in FY17 mainly due to a heavier VIP contribution – VIP GGR grew 177% YoY in that year. NagaWorld provides a higher commission to Macau based junkets as a way to attract those partners and solicit more deep-pocket Chinese high-rollers – Naga offers a 70% of GGR rebate vs. the 45% rebate adopted by Macau gaming operators. Looking forward, we expect NagaWorld's EBITDA margin to be maintained at around 35% as we believe both the VIP and mass sectors should stabilize when Naga2's ramp up is completed. We also factor in a 5% gaming tax with our conservative assumption that the Cambodian government will start to levy this tax in 1H19. As a result, we expect NagaWorld's (Naga1 and 2) property EBITDA to jump 20%/15% YoY in FY19E/FY20E and reverse back to a normal level of 10% from FY21E and onwards.

Further expansion of NagaWorld is in the works

The company has been planning a NagaWorld Phase 3 (Naga3) expansion for more than two years. It purchased the land for NagaWorld Phase 3's core area at a relatively low price and the new building will be within walking distance of Naga1 and 2.

During the 2018 annual results conference, management guided vaguely on the new complex: 1) it would take at least three to four years to open Naga3, and 2) the property will be more non-gaming focused – 92% of the new property's area will be designed for non-gaming activities, following an international standard. Although no detailed plan has been announced at this moment, we expect the company to kick-off Naga3 soon, given the rapid ramp-up of Naga2 and strong demand from both the VIP and mass segments.

We believe NagaCorp is capable of financing its Naga3 project. Assuming the total cost of Naga3 is around US\$400mn-500mn (given that the total cost of Naga2, including the late stage fit-out is projected to be around \$400mn), Naga's total cash reserves – ~US\$500mn/US\$750mn in FY19E/FY20E, respectively, should be sufficient to cover the new project's capital expenditure.

Naga Vladivostok – under development

Introduction – NagaCorp's first property outside Cambodia

In Sep 2013, NagaCorp announced development of a hotel and casino complex named Naga Vladivostok located in the northeast section of the Integrated Entertainment Zone (IEZ) in Primorsky Krai. The company launched construction in 2015, and expects it to be operational in 2020.

Exhibit 29 - Construction site of Naga Vladivostok



Source: IEZ of Primorsky website

Exhibit 30 - Design of Naga Vladivostok



Source: Company website

Among the five places in Russia that are allowed to operate gaming businesses, Primorsky Krai is the only one in the Far East region. So far, nine casino operators including Naga Vladivostok have signed contracts with the local government to develop integrated resorts in the IEZ.

Exhibit 31 - The integrated entertainment zone ("IEZ") of Primorsky Krai



Source: IEZ of Primorsky, CRSHK compiled

Development of the IEZ of Primorsky

In 2009, the Russian government forced all casinos to cease operation in Russia, and defined only four regions as legal gaming areas, including the Integrated Entertainment Zone (IEZ) of Primorsky in the Russian Far East. IEZ is 15km from the Vladivostok Airport and 50km from the city of Vladivostok. With

a total area of 619 hectares, the zone is planned to have nine-plus integrated resorts. The first casino in the zone was Tigre de Cristal by Summit Ascent (102 HK, not covered), which opened in October 2015. Other licensees, including NagaCorp, are currently in the construction phase. Construction of all projects in the zone should be completed by 2022 according to the master plan announced by the IEZ administration.

Exhibit 32 - Properties opened and under development in IEZ

| | Naga Corp (3918 HK) | Summit Ascent (102 HK) | | K International | Diamond Fortune Holdings Prim | | Prim Golden Gate | Gaming Group Primorye | Shambala |
|----------------------|------------------------|---------------------------|---------|--------------------|----------------------------------|--------------|------------------------|-----------------------------|---------------------|
| | Naga Vladivostok | Tigre de Cristal | Phase 2 | - | Selena | Moon Gate | Golden Gate | Sun | Shambala Complex |
| Opening date | 2020E | 2015 | 2020E | n.a. | 2020E | 2021E | 2021E | 2020E | 2020E |
| Area | Lot 20-23,25 | Lot 9 | Lot 10 | Lot 24 | Lot 2,4 | Lot14,15 | Lot 5-7 | Lot 11 | Lot 12,27 |
| Hotel rooms | 279 | 121 | 500 | n.a. | 1,100 | 460 | 576 | 900 | 270 |
| Tables | >100 | 64 | n.a. | n.a. | 459 | 110 | 200 | 376 | n.a. |
| Slot machines | >500 | 333 | n.a. | n.a. | 2,590 | 1,000 | 2,100 | 1,840 | n.a. |
| Budget (US\$) | 300mn | 172mn | 500mn | 300mn | 227mn | 152mn | 320mn | 212mn | 120mn |

Source: IEZ of Primorsky, CRSHK compiled

Building an integrated resort in Vladivostok means both opportunities and challenges for NagaCorp. But we believe the positives will outweigh the negatives. In particular, we have identified three positives and two negatives.

Positive #1: A friendly regulatory environment of IEZ for casino operators

The process of obtaining a gaming license. Interested investors participate in the bidding process for land lots in designated IEZ areas, proposing contracts and project designs to the IEZ government, and complying with the minimum investment requirements. The approved investor automatically obtains a gaming license. If an investor fails to fulfill the obligations such as meeting the timeline, the IEZ government can terminate the contract and withdraw the land lots and license. There is no limit to the number of gaming tables and slot machines an operator can have. Also, the license does not have an expiration date; however, it will be automatically canceled if the operator does not use it within three years.

Gaming tax. As with the Cambodian casinos, the tax environment in the IEZ is favorable compared to Macau's tax rate and that of other surrounding regions. It was ~2% of the GGR according to Summit Ascent's 1H18 financial statement:

- RUB125,000 (c.US\$1,867) per month for each gaming table
- RUB7,500 (c.US\$112) per month for each slot machine
- GGR is exempt from profit tax and VAT
- For property tax, there is a tax holiday for the first five years, and after that a tax of 0.5% for the next five years

We do not expect the gaming tax to be raised until all casinos open. The local government, which ultimately decides the tax, emphasizes the future development of IEZ. Given that eight projects are

under construction and another five land lots are available for investors, there is no motivation for the government to raise the tax rate now.

Positive #2: Good accessibility by air and by land

A one-hour drive from IEZ to downtown Vladivostok has been the major obstacle to attracting local leisure gamblers. However, the drive from the airport to IEZ now takes only 15 to 25 minutes. This is a considerably shorter commute time for overseas players who fly in for entertainment and gaming purposes. Being adjacent to the airport partially offsets the negatives and uncertainties arising from the region's severe winter weather – the place suffers minus-zero Celsius degree temperatures for four months each year, as revealed in exhibit 27.

Flights. Vladivostok Airport is a leading aviation hub in the Russian Far East. It is well connected to cities nearby, with ~400 million people living within a two-hour flight. Thanks to the opening of Tigre de Cristal, the zone is gradually building a reputation as a leisure travel destination, and passenger traffic jumped 19% YoY in the first five months of 2018, recording 8%/38% YoY growth in domestic/international routes, respectively. With more integrated resorts openings, we expect more airlines to add flights since the airport capacity is far from saturated.

Exhibit 33 - International direct flight arrivals in Vladivostok Airport

| Departure | 12/31/2018 | 1/1/2019 | 1/2/2019 | 1/3/2019 | 1/4/2019 | 1/5/2019 | 1/6/2019 | Sub-total | Flight duration |
|----------------------------|------------|-----------|-----------|-----------|-----------|-----------|-----------|------------|-----------------|
| | Mon | Tue | Wed | Thu | Fri | Sat | Sun | | |
| Seoul | 13 | 12 | 10 | 11 | 10 | 13 | 8 | 77 | 2.0hr |
| Busan | 2 | 3 | 3 | 1 | 5 | 1 | 3 | 18 | 2.0hr |
| Khabarovsk | 4 | 5 | 4 | 7 | 4 | 6 | 5 | 35 | 1.3hr |
| Hong Kong | 0 | 4 | 0 | 4 | 0 | 4 | 3 | 15 | 4.6hr |
| Beijing | 3 | 2 | 1 | 0 | 0 | 3 | 2 | 11 | 2.5hr |
| Shanghai | 1 | 0 | 0 | 0 | 1 | 0 | 0 | 2 | 3.5hr |
| Harbin | 0 | 0 | 0 | 2 | 0 | 1 | 2 | 5 | 1.3hr |
| Tokyo | 2 | 3 | 2 | 3 | 5 | 3 | 5 | 23 | 2.5hr |
| P-Kamchatsky | 5 | 2 | 2 | 3 | 4 | 5 | 4 | 25 | 3.5hr |
| Y-Sakhalinsk | 8 | 8 | 8 | 8 | 8 | 9 | 10 | 59 | 2.0hr |
| Other | 18 | 12 | 21 | 16 | 19 | 18 | 17 | 121 | |
| Total no. of flight | 56 | 51 | 51 | 55 | 56 | 63 | 59 | 391 | |

Source: Vladivostok Airport website, CRSHK compiled

Land. Vladivostok is also well connected through railway and inter-city bus to Northeastern China. Since we expect the major rollers to be from Northeastern China, we believe this land route should provide additional accessibility should it turn out that there is not sufficient flight frequency to cater to China's northeastern market. Also, a cross-border high-speed railway between Mudanjiang and Vladivostok was proposed by China in late 2017, with a feasibility study completed in mid-2018. The high-speed railway, backed by both the Chinese and Russia governments, should further tighten the economic relationship between the two nations and benefit the IEZ as a tourism hub.

Positive #3: Simplified visa requirements

Apart from exempting visas for registered tour groups (five to 50 persons) from China, the Russian government has defined Vladivostok as one of the free port zones so that tourists from 18 countries

including China can apply for E-visas. The government is preparing to extend the E-visa solution to other nations such as Vietnam, Malaysia and Cambodia.

Exhibit 34 - Visa requirements to Vladivostok

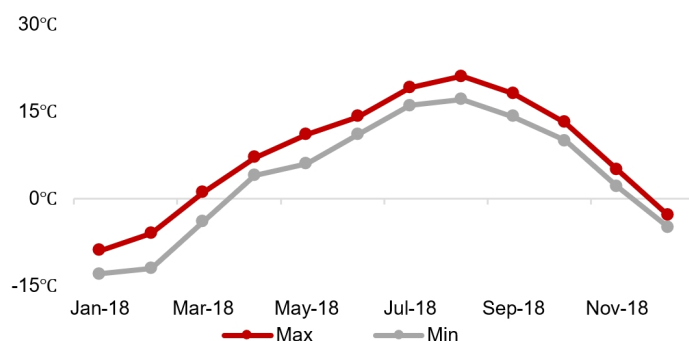
| | Visa type | Duration of stay | Remarks |
|-----------------------|------------------------------|------------------|--|
| Mainland China | E-visa | 8 days | Foreigners can enter and stay in the free port zone (including Vladivostok), but not allowed to leave the territorial limits of the zone |
| | Visa-free (tour groups only) | 15 days | Visa-free for tour groups (from 5 - 50 persons) organized by accredited Chinese travel agencies |
| | Regular visa | 30 days | Need to apply for single and double entry |
| Japan | E-visa | 8 days | Foreigners can enter and stay in the free port zone (including Vladivostok), but not allowed to leave the territorial limits of the zone |
| | Regular visa | 30 days | Need to apply for single and double entry |
| South Korea | Visa-free | 60 days | For non-commercial purposes |
| Hong Kong | Visa-free | 14 days | For non-commercial purposes |

Source: MFA Russia, CRSHK compiled

Negative #1: It is a seasonal destination

The climate of Vladivostok has extreme seasonality: there is a big difference in temperature between the summer and winter seasons. The average temperatures in winter are below 0°C, with some days hitting -20°C, making winter the usual off-season for tourism (Exhibit 35). Also, the summer season is fairly mild. Therefore, unlike Macau and the SEA countries, integrated resorts in the IEZ may suffer from this seasonality.

Exhibit 35 - Average high/low temperature of Vladivostok



Source: worldweatheronline.com, CRSHK compiled

Negative #2: NagaCorp does not have a reputation in Far East Asia yet

With limited tourist attractions at present, Vladivostok's reputation as a tourism and gaming destination is not yet as solid as Macau's, Singapore's and that of other SEA countries. Therefore, casino operators in the IEZ will likely build their client base gradually, either through utilizing their own resources in operating markets or by hiring local marketing teams.

Taking Tigre de Cristal as example, the property was well connected to the Macau gaming market due to its then-controlling shareholder Lawrence Ho, who also controls Melco International (200 HK, TP: HK\$20.9) and Melco Resorts (MLCO US, TP: US\$26.0). Therefore, its ramp up at its initial stage

has relied on the know-how of Macau junket operators, to attract Northeastern Chinese high rollers and nurture the client base, while the local mass market is ramping up gradually.

The primary source of clients may be from Northeast Asia, particularly from China. While NagaCorp is well experienced in the SEA market, we think the Russian Far East is too far for SEA high rollers to travel to. Macau was fed by people living nearby (53%+ of mainland tourists visiting Macau came from Guangdong, Fujian, Hunan and Hubei provinces in 2017). Therefore, we believe NagaCorp will need to build a brand-new base of clients in this region, including Northeastern China, Korea and Japan.

In conclusion, we believe Naga Vladivostok can benefit from the cluster effect

Although the market is new, we think positives outweigh negatives, and that ultimately IEZ will be transformed into a tourism-hub in Far East Asia. With Tigre de Cristal operating already, we think new joiners such as Naga Vladivostok will benefit from the cluster effect, bringing diversified gaming and non-gaming experiences to visitors.

While property details have not yet been disclosed, Naga Vladivostok's capex (US\$300mn) is larger than Tigre de Cristal's (<US\$200mn). Therefore, we expect the offerings of Naga Vladivostok should not be less than Tigre de Cristal. We assume 100 gaming tables and a similar opex structure to Tigre de Cristal. We project Naga Vladivostok should turn profitable at the EBITDA level in 1H21E, assuming that the property opens to public in 2H20E.

Exhibit 36 - Comparison between Tigre de Cristal and Naga Vladivostok

| | Tigre de Cristal (capex<US\$200mn) | | | | | Naga Vladivostok (capex US\$300mn) | | |
|--------------------|------------------------------------|------|------|------|------|------------------------------------|--------------|--------------|
| | 1H16 | 2H16 | 1H17 | 2H17 | 1H18 | 2H20E | 1H21E | 2H21E |
| Capacity | | | | | | | | |
| VIP gaming tables | 9 | 13 | 16 | 17 | 12 | 100 | 100 | 100 |
| Mass gaming tables | 23 | 20 | 21 | 20 | 20 | (VIP & mass) | (VIP & mass) | (VIP & mass) |
| Slot machines | 319 | 319 | 305 | 285 | 285 | 300 | 300 | 300 |
| Hotel rooms | 121 | 121 | 121 | 121 | 121 | 279 | 279 | 279 |
| Revenue | | | | | | | | |
| VIP GGR (US\$mn) | 15.9 | 48.7 | 39.2 | 50.8 | 24.2 | 16.0 | 32.4 | 38.9 |
| Mass GGR (US\$mn) | 7.9 | 7 | 7.3 | 9.7 | 10.8 | 4.5 | 8.5 | 10.1 |
| Slot GGR (US\$mn) | 5.7 | 6.9 | 6.5 | 8.9 | 8.5 | 6.3 | 11.6 | 13.5 |
| Total GGR (US\$mn) | 29.6 | 62.7 | 53.1 | 69.3 | 43.5 | 26.8 | 52.5 | 62.5 |
| EBITDA (US\$mn) | 4.5 | 12.3 | 7.3 | 15.0 | 8.6 | -0.2 | 10.5 | 15.2 |

Source: Company data, CRSHK estimates

Projecting EBITDA CAGR of 16% over FY18-21E

Expect FY19/20 revenue to grow 20%/12%

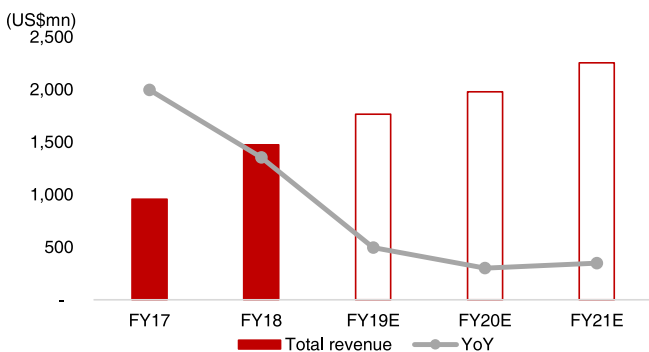
We expect Naga2's further ramp up to be the major driver for FY19 revenue growth. VIP business should continue to deliver satisfactory results as newly joined Macau-based junket operators introduce more Chinese high rollers. The mass segment should maintain its strong momentum, backed by an increasing number of inbound visitations to Cambodia.

In detail, we expect VIP rolling to grow 30% YoY in 1H19, following the 41% VIP volume growth in 2H18. 1H19 GGR is expected to grow 13%, lower than volume growth as the 3.3% win rate in 1H18 sets a high base. Total VIP GGR is expected to grow 19% YoY in FY19 and maintain a single-digit growth onwards as Naga2 fully ramps up.

The mass segment should be less volatile and grow constantly along with Cambodia's booming tourism industry. The company's mass business grew significantly in FY18, recording 53%/61% YoY growth of mass table buy-ins in 1H18/2H18, respectively. Partially credited to the newly opened Naga2 complex, the surge in mass volume has also been driven by increasing numbers of inbound tourists – especially visitor arrivals from China, which grew 71% YoY in the first nine months of 2018, according to Cambodia's Ministry of Tourism. Looking forward, we expect the company's mass GGR (including revenue from electronic gaming machines) to grow 24%/17% in FY19E/FY20E, respectively, and to maintain around 13% growth in later years.

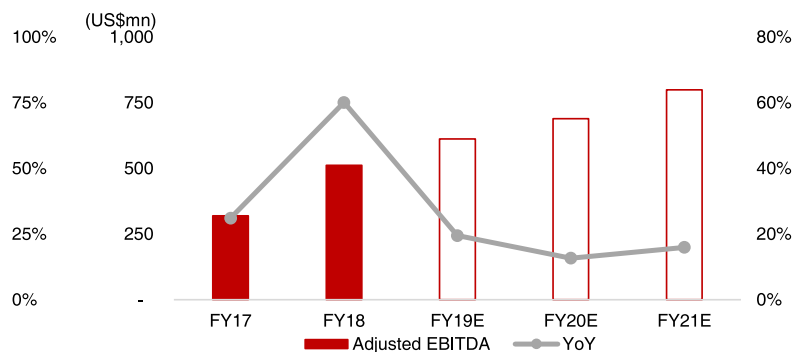
The new property Naga Vladivostok, targeted to open in FY20, should start making a full contribution in FY21E. However, since the Vladivostok gaming industry is still at an early stage, we believe Naga Vladivostok may not make a significant financial contribution in the first few years of its opening. Referring to the operating results of Tigre de Cristal (an existing integrated resort in the IEZ region) as an example, we anticipate Naga Vladivostok may bring only an additional US\$121mn/161mn total revenue in FY21E/22E, on top of NagaWorld's US\$2,134mn/2,326mn revenue – thus, representing only 6%/7% incremental revenue growth for the company in FY21E/22E.

Exhibit 37 - NagaCorp revenue projections



Source: Company data, CRSHK estimates

Exhibit 38 - NagaCorp adj. EBITDA projections



Source: Company data, CRSHK estimates

Expect FY19/20 EBITDA to grow 20%/13%

We project Naga's EBITDA to grow 20%/13%, reaching US\$612mn/689mn in FY19E/FY20E, respectively. The Vladivostok property, in our view, should begin contributing positive EBITDA as of FY21. Naga's EBITDA margin should remain flattish at 35% – more proportion of the high-margin mass business should offset the 5% estimated GGR tax that is projected to negatively impact the EBITDA margin.

Exhibit 39 - Key financials of NagaCorp's income statement

| US\$m | FY18 | FY19E | FY20E | FY21E |
|-----------------------------------|--------------|--------------|----------------|----------------|
| Total Revenue | 1,474 | 1,767 | 1,980 | 2,255 |
| Table GGR | 1,305 | 1,579 | 1,762 | 1,997 |
| EGM GGR | 129 | 146 | 170 | 205 |
| Non-casino revenue | 40 | 42 | 47 | 52 |
| Cost of Sales | (801) | (948) | (1,064) | (1,206) |
| Employee benefit expenses | (92) | (97) | (108) | (122) |
| Operating lease charges | (12) | (12) | (12) | (13) |
| Depreciation and amortisation | (93) | (103) | (116) | (114) |
| Other operating expenses | (57) | (61) | (64) | (68) |
| Adjusted EBITDA | 512 | 612 | 689 | 799 |
| <i>EBITDA margin%</i> | 35% | 35% | 35% | 35% |
| Operating profit | 419 | 505 | 569 | 682 |
| <i>OP margin%</i> | 28% | 29% | 29% | 30% |
| Net profit to shareholders | 391 | 466 | 529 | 658 |
| <i>Net margin%</i> | 26% | 26% | 27% | 29% |

Source: Company data, CRSHK estimates

Expect 5% gaming tax to be levied from 1H19 and major opex to grow 5% YoY

We factor in a 5% gaming tax (directly taxed on GGR) as of 1H19, based on management's guidance as well as market expectations. We expect the company's major operating overheads (including staff costs and rentals) to increase at a steady rate of 5% YoY from FY19E. Annual depreciation and amortization should increase to c.US\$100mn per year due to the opening of Naga2. As a result, we expect the operating profit margin and net profit margin to stabilize at 29%/26%, respectively.

Strong cash flow and balance sheet

The company has strong cash flow and balance sheet positions. Free cash flow is expected to grow 60%/50% in FY19E/20E, respectively, as the ramp-up of Naga2 enhances cash inflow. We expect the company's FY19E CAPEX to be US\$200mn, which includes US\$150mn for Naga1's refurbishment.

Naga's total debt to equity ratio is maintained at a low level of 19% in FY18. The only debt the company holds at present is the ~US\$290mn senior note raised in May 2018 (with a FY21 expiration date) in order to promote its VIP business and renovate the Naga1 building. However, the company had a net cash position of \$102mn at year-end FY18, and we expect it to reach US\$204mn/465mn in FY19E/20E (excluding costs for Naga3), respectively. We expect the company to maintain a stable 60% dividend payout ratio, backed by its strong cash position. The dividend yield for FY19/FY20 is estimated at 4.9%/5.5%, based on closing price of HK\$10.32.

Exhibit 40 - Key financials of NagaCorp's cash flow statement and balance sheet

| US\$mn | FY18 | FY19E | FY20E | FY21E |
|---------------------------|------------|------------|------------|------------|
| Operating cashflow | 496 | 589 | 668 | 773 |
| Investing cashflow | (273) | (197) | (76) | (76) |
| Financing cashflow | 101 | (290) | (331) | (656) |
| Net change in cash | 324 | 102 | 260 | 40 |
| Cash and cash equivalents | 317 | 419 | 679 | 720 |
| Bank deposits and bonds | 76 | 76 | 76 | 76 |
| ST borrowings | - | - | - | - |
| LT borrowings | 291 | 291 | 291 | - |
| Net cash | 102 | 204 | 465 | 796 |

Source: Company data, CRSHK estimates

Valuation

EV/EBITDA our main valuation methodology

Gaming is an industry with high-entry barriers because: 1) the number of operators is limited by gaming licenses, and 2) it requires heavy capital expenditure with substantial initial investment and large depreciation before generating any revenue. We believe EV/EBITDA is the most suitable valuation methodology, given that: 1) Naga is at an investing stage for expansion and renovations, 2) the impact from depreciation remains material during the new properties' ramp-up stages, and 3) the EV/EBITDA multiple offers better comparison with casino operators from Macau and other international markets.

We also cross-checked with other valuation methodologies: 1) P/E ratio is a universal valuation method. 2) Dividend yield is also a key methodology for long-term investors looking for yield names. 3) Free cash flow yield is a way to estimate how much free cash the firm is generating, which can be invested in other long-term projects or distributed as dividends in the future. 4) Net gearing and ROE are also matrices we pay attention to, in order to monitor the balance between financial leverage and return on equity.

Initiating coverage at BUY with TP of HK\$14

We initiate NagaCorp at BUY with a target price of HK\$14. Our TP is based on 12x FY19E EV/EBITDA, implying 17x FY19E P/E.

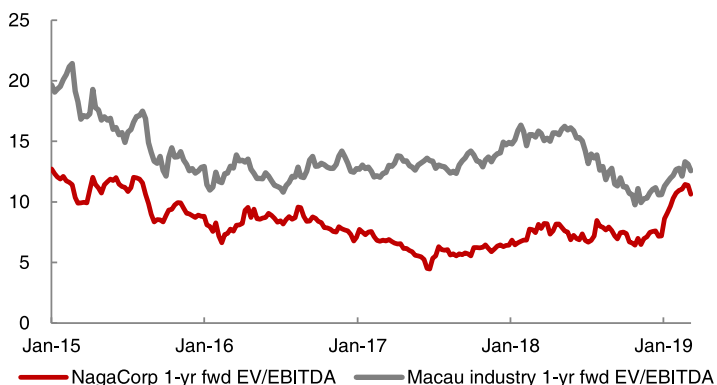
Naga is currently trading at 9x FY19E EV/EBITDA, 12x P/E and 4.9% dividend yield. Historically, Naga has been trading at a significant discount to its Macau gaming peers (around 7x EV/EBITDA for Naga vs. 13x for Macau peers) due to: 1) Cambodia is relatively under-developed, with political and social uncertainties that may compromise its tourism industry and therefore, Naga's business; and 2) NagaCorp has a small size and a relatively unstable customer base as compared to international gaming operators from Macau, which means that it could suffer more in a downside market.

Naga's valuation discount to the Macau gaming players has narrowed recently (as revealed in Exhibits 33, 34) and we believe the trend will continue – Naga deserves a valuation that is in line with Macau peers, in our opinion, due to:

- 1) **A more promising industry outlook:** We believe Cambodia as an SEA tourism destination is gradually accepted by Chinese tourists, which is reflected in the rapid growth of Chinese visitations in recent years. Given that the number of Chinese visitations to Cambodia (expected 1.5mn in 2018) is still significantly lower than visitations to Thailand (9.7mn in 2018) and Vietnam (5mn in 2018), there is still potential to penetrate. More tourists should directly benefit Naga's high-margin mass business, as demonstrated in its FY18 results.
- 2) **Better business quality:** We believe the company is in better shape than in previous years. The opening and ramp-up of Naga2 have demonstrated the company's strength in business execution, as well as its ability to manage a larger integrated resort. While the successful opening of Naga2 has enabled the company to target regional high rollers, it should also enable the whole NagaWorld complex to attract more visitations – after all, a bigger and more comprehensive integrated resort is essential to targeting a broader market and developing a stable customer base.
- 3) **Solid foundation for future expansion:** With a strong cash position and experienced management team, we believe the company is prepared for further expansion. We expect the company's current pipeline projects – Naga Vladivostok and Naga3 – to enhance future growth.

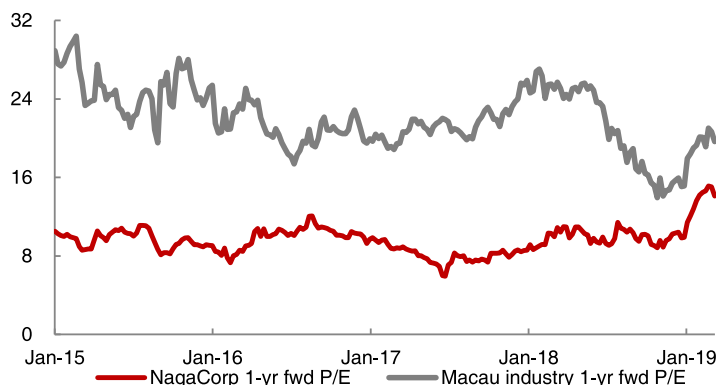
In addition, there should be more growth opportunities as the company gradually becomes an influential regional player.

Exhibit 41 - NagaCorp vs. Macau gaming industry 1-year forward EV/EBITDA



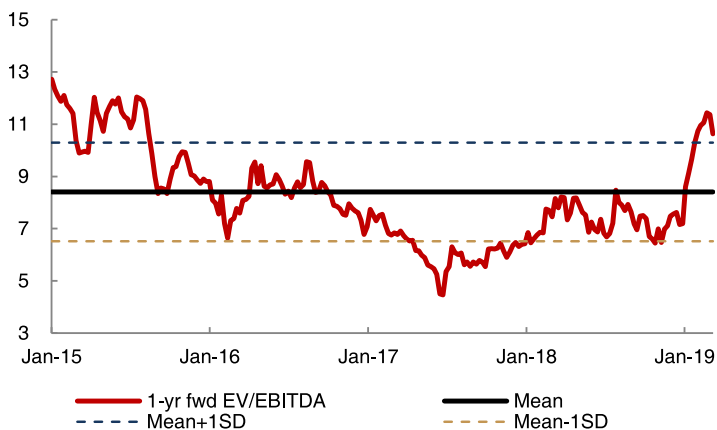
Source: Bloomberg, CRSHK estimates

Exhibit 42 - NagaCorp vs. Macau gaming industry 1-year forward P/E



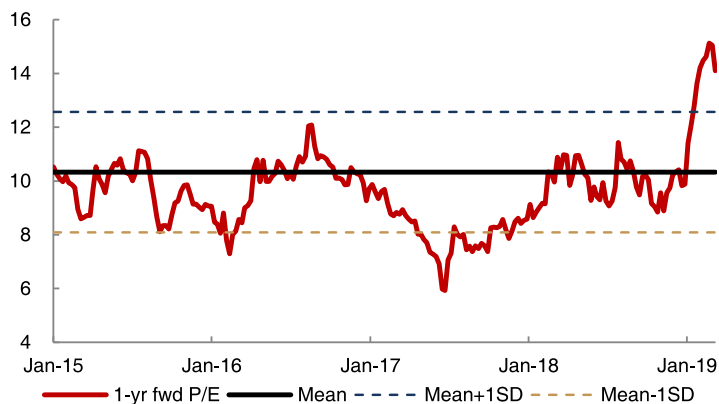
Source: Bloomberg, CRSHK estimates

Exhibit 43 - NagaCorp's one-year forward EV/EBITDA band



Source: Bloomberg, CRSHK estimates

Exhibit 44 - NagaCorp's one-year forward P/E band



Source: Bloomberg, CRSHK estimates

Catalysts for NagaWorld

- 1) The Cambodian government focuses increasingly on promoting its tourism industry, attracting visitors from China and SEA countries. More tourists mean better potential business for Naga, especially in the mass segment.
- 2) A more favorable regulatory environment in Phnom Penh or Vladivostok can be a catalyst for Naga's business expansion, which translates into both better financial results and higher valuation.

Comparative valuations

| Company name | Ticker | Rating | Target Px | Current Px 3/8/2019 | Market Cap (US\$ mn) | Avg T/O (US\$ mn) | EV/EBITDA | | |
|-------------------------|---------|--------|------------|------------------------|-------------------------|----------------------|------------|------------|------------|
| | | | | | | | FY18 | FY19E | FY20E |
| Macau gaming | | | | | | | | | |
| Galaxy | 27 HK | BUY | HK\$ 62.00 | HK\$ 51.60 | 28,643 | 89.2 | 11x | 11x | 10x |
| SJM | 880 HK | HOLD | HK\$ 7.00 | HK\$ 8.93 | 6,484 | 17.8 | 16x | 16x | 13x |
| Wynn Macau | 1128 HK | HOLD | HK\$ 20.00 | HK\$ 18.10 | 12,060 | 30.7 | 11x | 11x | 11x |
| Sands China | 1928 HK | HOLD | HK\$ 40.00 | HK\$ 37.80 | 39,162 | 62.3 | 14x | 14x | 13x |
| MGM China | 2282 HK | HOLD | HK\$ 16.00 | HK\$ 15.82 | 7,708 | 11.3 | 16x | 14x | 12x |
| Melco Resorts | MLCO US | BUY | US\$26.00 | US\$ 22.67 | 11,207 | 57.6 | 10x | 9x | 9x |
| Sector mean | | | | | | | 13x | 12x | 11x |
| Sector median | | | | | | | 13x | 12x | 12x |
| Conglomerate | | | | | | | | | |
| Melco International | 200 HK | BUY | HK\$ 20.90 | HK\$ 17.74 | 3,456 | 6.2 | 8x | 6x | 6x |
| SEA gaming | | | | | | | | | |
| NagaCorp | 3918 HK | BUY | HK\$ 14.00 | HK\$ 10.32 | 5,743 | 6.2 | 11x | 9x | 8x |
| Genting Singapore | GENS SP | NC | n.a. | SGD 1.00 | 8,857 | 30.1 | 7x | 7x | 7x |
| Sector mean | | | | | | | 9x | 8x | 7x |
| Sector median | | | | | | | 9x | 8x | 7x |
| Las Vegas gaming | | | | | | | | | |
| Las Vegas Sands | LVS US | NC | n.a. | US\$ 59.99 | 46,495 | 230.7 | 10x | 10x | 9x |
| MGM Resorts | MGM US | NC | n.a. | US\$ 26.45 | 14,201 | 246.6 | 11x | 10x | 9x |
| Wynn Resorts | WYNN US | NC | n.a. | US\$ 118.67 | 12,773 | 279.5 | 9x | 9x | 8x |
| Sector mean | | | | | | | 10x | 10x | 9x |
| Sector median | | | | | | | 10x | 10x | 9x |

| Company name | Ticker | P/E | | | FCF yield | | | Dividends yield | | |
|-------------------------|---------|------------|------------|------------|-----------|-----------|------------|-----------------|-----------|-----------|
| | | FY18 | FY19E | FY20E | FY18 | FY19E | FY20E | FY18 | FY19E | FY20E |
| Macau gaming | | | | | | | | | | |
| Galaxy | 27 HK | 17x | 15x | 14x | 8% | 6% | 8% | 2% | 2% | 2% |
| SJM | 880 HK | 19x | 23x | 20x | -6% | 0% | 4% | 3% | 3% | 3% |
| Wynn Macau | 1128 HK | 15x | 15x | 14x | 8% | 8% | 8% | 8% | 7% | 6% |
| Sands China | 1928 HK | 19x | 18x | 17x | 6% | 6% | 6% | 5% | 5% | 5% |
| MGM China | 2282 HK | 40x | 19x | 16x | 6% | 3% | 3% | 1% | 2% | 2% |
| Melco Resorts | MLCO US | 30x | 18x | 16x | 6% | 7% | 8% | 3% | 3% | 3% |
| Sector mean | | 23x | 18x | 16x | 5% | 5% | 6% | 4% | 4% | 4% |
| Sector median | | 19x | 18x | 16x | 6% | 6% | 7% | 3% | 3% | 3% |
| Conglomerate | | | | | | | | | | |
| Melco International | 200 HK | 28x | 19x | 15x | 3% | 7% | 8% | 1% | 1% | 1% |
| SEA gaming | | | | | | | | | | |
| NagaCorp | 3918 HK | 15x | 12x | 11x | 6% | 10% | 15% | 4% | 5% | 6% |
| Genting Singapore | GENS SP | 15x | 16x | 15x | 5% | 5% | 5% | 3% | 3% | 3% |
| Sector mean | | 15x | 14x | 13x | 6% | 8% | 10% | 3% | 4% | 4% |
| Sector median | | 15x | 14x | 13x | 6% | 8% | 10% | 3% | 4% | 4% |
| Las Vegas gaming | | | | | | | | | | |
| Las Vegas Sands | LVS US | 17x | 18x | 17x | 8% | 6% | 7% | 5% | 5% | 5% |
| MGM Resorts | MGM US | 23x | 20x | 15x | 1% | 5% | 6% | 2% | 2% | 2% |
| Wynn Resorts | WYNN US | 18x | 19x | 14x | 5% | 5% | 7% | 2% | 3% | 3% |
| Sector mean | | 19x | 19x | 15x | 5% | 6% | 7% | 3% | 3% | 3% |
| Sector median | | 18x | 19x | 15x | 5% | 5% | 7% | 2% | 3% | 3% |

Source: Bloomberg, CRSHK estimates. Note: USD:HKD = 7.8

Risks

- **Economic risks.** 1) A sudden cool down in Southeast Asian economies, which are NagaCorp's key target markets, due to weaker global consumption demand (in particular in the garment industry) could result in lower-than-expected EBITDA growth. 2) A substantial drop in foreign direct investment 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.
- **Gaming license-related policy risks.** Gaming policies in Cambodia might experience more frequent changes than in other nations, since Phnom Penh does not have a long history of regulating the gaming market. Thus, we cannot rule out the possibility of potential changes in regulations: 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.** NagaWorld sources clients from SEA and China. Therefore, Phnom Penh's gaming industry competes with other gaming hubs such as Malaysia's Genting Highlands, Singapore, and Vietnam's Da Nang. 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 the demand side. In that case, the company may not be able to maintain its rate of revenue growth.
- **Rising wages.** Labor costs in Cambodia are relatively low and NagaWorld pays employees in US dollars. Since Cambodia is an emerging market and faces rapid potential hikes in wages, we cannot rule out the possibility that the government raises the minimum wage.
- **Financing needs might result in dividend cuts.** The company is paying dividends with a high payout ratio of 60%. Since the company is building Naga Vladivostok and planning NagaWorld Phase 3, we think it may need additional cash flow to support its business expansion. This could be through debt financing, but other forms of financing cannot be ruled out, such as cutting the dividend payout ratio.

NagaCorp's financial statements

Statement of financial position

| US\$ mn | FY18 | FY19E | FY20E | FY21E |
|-------------------------------------|--------------|--------------|--------------|--------------|
| Current assets | 512 | 638 | 916 | 978 |
| Cash and cash equivalents | 317 | 419 | 679 | 720 |
| Account and other receivables | 117 | 140 | 157 | 179 |
| Inventories | 2 | 2 | 2 | 3 |
| Other current assets | 76 | 76 | 76 | 76 |
| Non-current assets | 1,455 | 1,552 | 1,516 | 1,482 |
| Property and equipment | 1,276 | 1,376 | 1,344 | 1,314 |
| Intangible assets | 59 | 56 | 52 | 48 |
| Interest in leasehold land | 27 | 26 | 26 | 26 |
| Other non-current assets | 94 | 94 | 94 | 94 |
| Total assets | 1,967 | 2,190 | 2,431 | 2,460 |
| Current liabilities | 92 | 107 | 118 | 132 |
| ST borrowings | - | - | - | - |
| Account payables | 80 | 94 | 106 | 120 |
| Other current liabilities | 12 | 12 | 12 | 12 |
| Non-current liabilities | 335 | 335 | 335 | 44 |
| LT borrowings | 291 | 291 | 291 | - |
| Other non-current liabilities | 44 | 44 | 44 | 44 |
| Total liabilities | 427 | 442 | 454 | 177 |
| Share capital | 54 | 54 | 54 | 54 |
| Treasury shares | - | - | - | - |
| Reserves | 1,486 | 1,693 | 1,923 | 2,229 |
| Minority interest | - | - | - | - |
| Shareholders equity | 1,540 | 1,748 | 1,978 | 2,283 |
| Total equity and liabilities | 1,967 | 2,190 | 2,431 | 2,460 |

Statement of cash flows

| US\$ mn | FY18 | FY19E | FY20E | FY21E |
|-------------------------------|--------------|--------------|--------------|--------------|
| Operating cashflow | 496 | 589 | 668 | 773 |
| Net income | 391 | 466 | 529 | 658 |
| Depreciation and amortization | 93 | 103 | 116 | 114 |
| Change in working capital | (14) | (9) | (6) | (8) |
| Other operating cashflow | 27 | 29 | 28 | 9 |
| Investing cashflow | (273) | (197) | (76) | (76) |
| CAPEX | (245) | (200) | (80) | (80) |
| Interest received | 3 | 3 | 4 | 4 |
| Investment in bonds | (76) | - | - | - |
| Other investing cashflow | 45 | - | - | - |
| Financing cashflow | 101 | (290) | (331) | (656) |
| Net proceeds from | 272 | (32) | (32) | (304) |
| Share issue (repurchase) | - | - | - | - |
| Dividend paid | (171) | (258) | (299) | (353) |
| Other financing cashflow | - | - | - | - |
| Foreign exchange rate adj. | - | - | - | - |
| Net change in cash | 324 | 102 | 260 | 40 |

Income statement

| US\$ mn | FY18 | FY19E | FY20E | FY21E |
|-----------------------------------|--------------|--------------|--------------|--------------|
| Total revenue | 1,474 | 1,767 | 1,980 | 2,255 |
| Cost of sales | (801) | (948) | (1,064) | (1,206) |
| Employee benefit expenses | (92) | (97) | (108) | (122) |
| Operating lease charges | (12) | (12) | (12) | (13) |
| Gaming tax | - | (40) | (46) | (52) |
| Depreciation and amortisation | (93) | (103) | (116) | (114) |
| Other operating expenses | (57) | (61) | (64) | (68) |
| Adjusted EBITDA | 512 | 612 | 689 | 799 |
| Operating profit | 419 | 505 | 569 | 682 |
| Interest expense | (19) | (32) | (32) | (12) |
| Interest income | 3 | 3 | 4 | 4 |
| Other non-operating items | (3) | - | - | - |
| Pre-tax profit | 399 | 477 | 541 | 673 |
| Income tax expense | (9) | (10) | (12) | (15) |
| After-tax profit | 391 | 466 | 529 | 658 |
| Non-controlling interests | - | - | - | - |
| Net profit to shareholders | 391 | 466 | 529 | 658 |
| Basic EPS (US\$) | 0.09 | 0.11 | 0.12 | 0.15 |
| Diluted EPS (US\$) | 0.09 | 0.11 | 0.12 | 0.15 |
| DPS (US\$) | 0.05 | 0.06 | 0.07 | 0.09 |

Ratios

| | FY18 | FY19E | FY20E | FY21E |
|-----------------------------|------|-------|-------|-------|
| YoY | | | | |
| Total revenue | 54% | 20% | 12% | 14% |
| Adjusted EBITDA | 60% | 20% | 13% | 16% |
| Operating profit | 59% | 21% | 13% | 20% |
| Net profit | 53% | 19% | 14% | 24% |
| Profitability | | | | |
| EBITDA margin | 35% | 35% | 35% | 35% |
| OP margin | 28% | 29% | 29% | 30% |
| NP margin | 26% | 26% | 27% | 29% |
| ROE | 25% | 27% | 27% | 29% |
| ROIC | 25% | 28% | 32% | 39% |
| Liquidity | | | | |
| Debt/equity | 19% | 17% | 15% | 0% |
| Net debt/equity | -2% | -7% | -20% | -32% |
| Current ratio | 5.6x | 6.0x | 7.7x | 7.4x |
| Quick ratio | 4.7x | 5.2x | 7.1x | 6.8x |
| Operating efficiency | | | | |
| Asset turnover | 0.7x | 0.8x | 0.8x | 0.9x |
| Valuation ratios | | | | |
| EV/EBITDA | 11x | 9x | 8x | 6x |
| P/E | 15x | 12x | 11x | 9x |
| FCF yield | 4% | 7% | 11% | 12% |
| Dividend yield | 4.1% | 4.9% | 5.5% | 6.9% |

Source: Company data, CRSHK estimates

Appendix A

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|--------|-------|---------|----------|---------|
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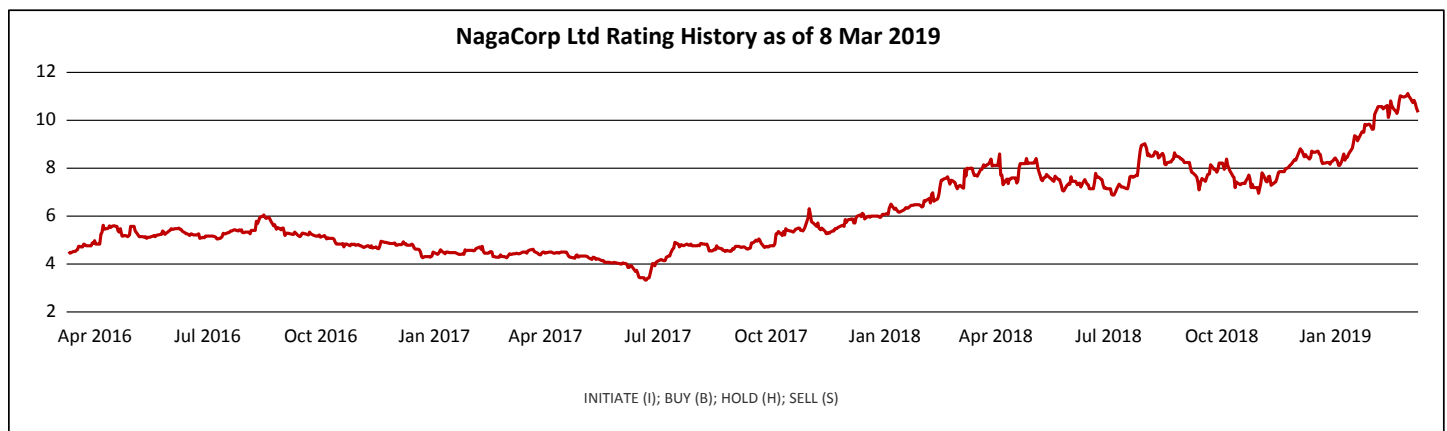
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Underweight – Expect sector to underperform the relevant market.



Valuation Methodology

3918 HK:

Our target price for NagaCorp is HK\$14.00, based on 12x FY19E EV/EBITDA, implying 17x 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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