Macau Gaming | CHINA

CONGLOMERATES

NOMURA

NOMURA INTERNATIONAL (HK) LIMITED

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NEW THEME

Action

Given a high base, converging consensus expectations and market volatility, monthly gaming revenue may become a less important driver of share prices for the time being. We favour bottom-up stock selection, and our top picks are Sands China (mass market, laggard) and Galaxy (new casino opening). We also like SJM, but caution that investor confidence may take time to rebuild.

Catalysts

We don't expect a broad-based sector re-rating until 2Q11, when positive seasonality kicks in. Laggard Sands China should perform ahead, as we expect 1Q11 to surprise on the upside, and Galaxy's new opening is a positive catalyst.

Anchor themes

We look for 26% growth in gaming revenue in 2011, with a resilient mass market and potential for upside surprise in the VIP segment. The underlying macro story remains the multi-year momentum in Chinese consumption.

Stocks for action

We think consensus numbers have begun to converge because of a shared focus on monthly gaming revenue numbers, and thus see potential for surprise in company-specific stories.

Stock	Rating	Price (HK$)	Price target	Up/down-side (%)
Sands China (1928 HK)	BUY	17.02	24.0↑	41
Galaxy (27 HK)	BUY *	11.32	13.35↑	18
SJM (880 HK)	BUY	12.8	15.5↑	21
Wynn Macau (1128 HK)	NEUTRAL	21.0	23.5↑	12
Melco Crown (MPEL US)	REDUCE	US$7.35	US$6.9↑	(6)
Melco Int'l (200 HK)	REDUCE	5.13	4.83↑	(6)

* Upgrading from Neutral. ↑ Raising PT.
Note: 11 March closing prices

Not just a macro call

① Headline revenue not enough to drive share prices?

Despite strong gaming revenue in January and February, Macau names seem to lack strength to trade up higher (see exhibit on page 4). Gaming revenue looks to have failed to re-rate the sector, as we believe: 1) consensus expects 25-30% growth, an implied monthly run rate of MOP20bn, given the February number; revenue is meeting but not beating expectations; and 2) investors worry about a delayed impact from credit tightening, so they are looking beyond the current strength. For the sector to re-rate, investors may need to see consecutive months of very strong revenue surprise, which likely have to be in the MOP 22-24bn range. Data takes time to accumulate; the re-rating will more likely come during the end of 2Q11, we think. Strong 1Q11 results (announced in May / June) may also help provide further valuation support for the sector.

② When macro = consensus call / micro factors come to the fore

The bullish assumption of a 25-30% y-y revenue increase has become a consensus call. We reckon that a slowdown risk is low, since: 1) mass market has been robust and could be boosted further in 2H11 amid infrastructural upgrades; and 2) VIP has room to surprise, as junket liquidity remains abundant and sustainable. But, as discussed, the growth estimate is unlikely to be re-rated in the shorter run, and thus we think it is important to become more selective in our stock picks as micro factors / stock-specific factors become more important.

③ Picking the right exposure

Buy a combo: Sands China (1928 HK) is our top pick: 1) it has lagged the sector; 2) it should show stronger earnings resilience in case of a VIP slowdown due to its higher exposure to mass market and non-gaming revenue; and 3) positive news flow is in the pipeline – progress on Lot 5&6 and sales of Four Seasons apartments. **Galaxy (27 HK) is our beta hedge:** As a VIP-centric name (prior to opening of Galaxy Macau), Galaxy is more likely to continue to benefit should market momentum turn strong, in our view. More importantly, amid bullish sentiment, investors could become more ready to assign a premium to its option value – Galaxy Macau, the mega resort project on Cotai, which is due to open on 15 May 2011.

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Still growing: 26% revenue growth for 2011 (up from 18%)

After recording 58% y-y growth in 2010, Macau gaming revenue remained resilient to test new records

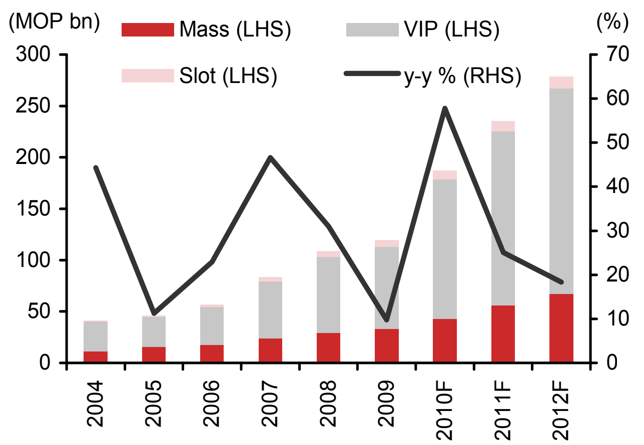
After recording 58% y-y growth in 2010, Macau gaming revenue remained resilient to test new records. The sector surprised the market by delivering record revenue of MOP19.9bn (47% y-y growth) in a seasonally weaker and the shortest month of the year – February. In our view, the strong momentum provides a solid foundation for the sector to continue its robust growth going forward, especially amid healthy growth in internal consumption in China, Chinese currency appreciation (3-5 % in 2011) and strong China economic backdrop (GDP to grow by 9.8% according to Nomura).

We expect the sector to grow at 26% y-y in 2011 (up from our original estimate of 18%). This is driven by underlying growth of 25% in the VIP segment (from 16%) and 30% growth in the mass market revenue (from 25%).

Drivers: mass market remains robust, VIP could surprise

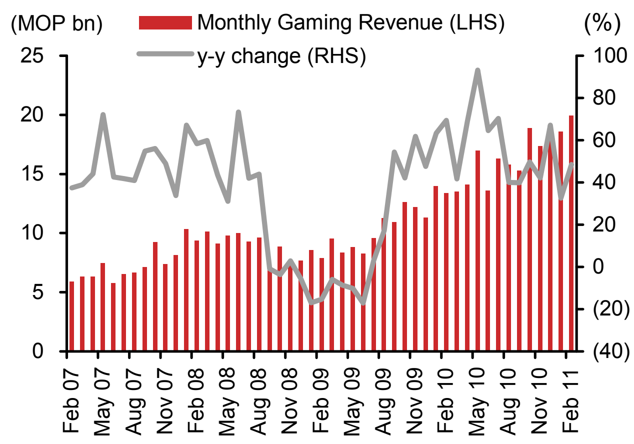
- **VIP remains the wild card — abundant junket liquidity drives VIP segment:** Three sources support junket working capital: 1) retained earnings of junkets (remains strong given robust growth from 2010); 2) private equity sources, ie, VIP (stays on, as they are investing for an equity stake, thus are not easy to redeem); and 3) a casino's credit line (likely to remain relatively stable).
- **Mass market growth remains robust, as expected, and may be boosted in 2H11:** January and February recorded very strong mass market revenue mainly on higher spending per visitor (mass market revenue up 27%, vs visitation of 1%, Exhibit 11), we may see another boost to mass market business from increased visitation in 2H11, driven by infrastructural improvement (intercity train / border gate expansion) and the opening of a new casino, Galaxy Macau.

Exhibit 1. Macau: gaming revenue forecast



Source: Direcção de Inspecção e Coordenação de Jogos

Exhibit 2. Macau: monthly gaming revenue



Source: DICJ, Nomura estimates

But strong headline revenue not enough to drive share prices

Despite strong revenues in both January and February, Macau names are still trading at around the same level as the beginning of the year. Gaming revenue looks to have failed to re-rate the sector, as we believe:

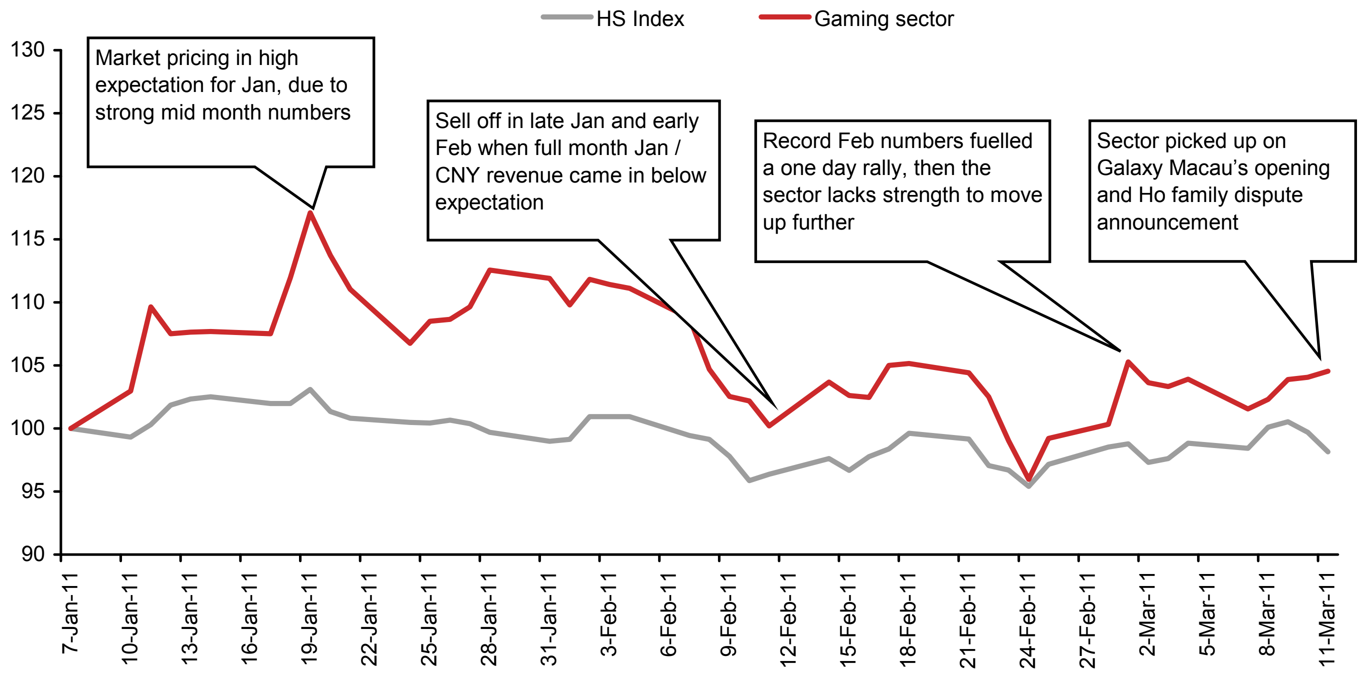
- **Higher expectation caps share price performance:** The consensus assumption now centres on 25-30%, with an implied monthly run rate of MOP20bn. Given the February number, current revenue is meeting but not beating expectations, thus the share prices may be rangebound before any re-rating kicks in in 2Q11.

- **Concerned about a potential slowdown, investors look further ahead:** Recent share price performance has replicated that of 1H10; even after a few months of strong revenue in 1H10, the share prices did not respond, as investors worried about the impact of China property tightening. Investors are now worried about the delayed impact from credit tightening stemming from rate hikes.

On the macro front, the sector will likely be re-rated toward the end of 2Q, in our view. This is because for the sector to re-rate, investors need to see consecutive months of very strong revenue surprise, likely in the MOP 22-24bn range due to the expectation gap. Besides, monthly revenue data takes time to accumulate. Strong 1Q11 results, which are usually announced in May, may also help provide support to share prices.

On the macro front, the sector will likely be re-rated toward the end of 2Q

Exhibit 3. Headline is not sufficient to drive share prices?



Source: Bloomberg

When macro = consensus call / micro factors come to the fore

As the consensus growth assumption is now concentrated in the 25-30% range, versus being rooted in the 10-15% range in 2010, more room has been created for disappointment and there is less room for a re-rating on gaming revenue upside surprise. Since the bullish y-y growth assumption of 25-30% has become a consensus call, and is unlikely to change in the short run, we think it is important to become more selective in our stock picks as micro factors / stock specific factors become more pertinent.

Important to become more selective in our stock picks as micro factors / stock specific factors become more pertinent

Picking the right exposure

To maintain exposure while minimising downside risk, we are selective in our stock picks:

- **Sands China (1928 HK) is our top pick**: 1) it has lagged the sector year to date, providing less room for downward correction; 2) it should experience stronger earnings resilience in case of a VIP slowdown due to its higher exposure to mass market and non-gaming revenue; and 3) there is positive news flow in the pipeline – progress on Lot 5&6 and sales of Four Seasons apartments.
- **Galaxy (27 HK) is beta hedge:** As a VIP-centric name (prior to the opening of Galaxy Macau), Galaxy is more likely to continue to benefit should the market momentum turn strong. More importantly, amid bullish sentiment, investors could become more ready to assign a premium to its option value – Galaxy Macau, the mega resort project on Cotai due to open on 15 May 2011.

Exhibit 4. Valuation comp table

Stock	Bloomberg code	Rating	Market cap. (US$mn)	Share price (Loc)	Price Target (Loc)	Potential up/down-side (%)	P/E (x) 10F	P/E (x) 11F	P/E (x) 12F	EV/EBITDA (x) 10F	EV/EBITDA (x) 11F	EV/EBITDA (x) 12F
Macau Casino Operators (HK-listed)												
Galaxy	27 HK	BUY	5,957	11.32	13.35	18	33.9	22.3	17.9	24.8	14.8	9.4
Melco	200 HK	REDUCE	811	5.13	4.83	(6)	NM	NM	NM	NM	NM	NM
Melco-Crown	MPEL US	REDUCE	3,909	7.35	6.90	(6)	NM	NM	NM	12.2	10.6	9.3
Sands China Ltd	1928 HK	BUY	17,589	17.02	24.00	41	27.5	19.4	15.7	15.9	12.5	9.1
SJM	880 HK	BUY	9,001	12.80	15.50	21	19.3	14.7	12.5	13.1	9.8	8.4
Wynn Macau	1128 HK	NEUTRAL	13,988	21.00	23.50	12	24.1	18.5	16.0	19.0	14.9	13.2
Macau Casino Operators (HK-listed) average						**11**	**26.2**	**18.7**	**15.5**	**17.0**	**12.5**	**9.9**
Singapore and Malaysia												
Genting Malaysia	GENM MK	BUY	6,525	3.35	4.12	23	15.1	14.2	13.2	7.2	6.3	5.4
Genting Singapore	GENS SP	REDUCE	18,829	1.96	1.01	(48)	39	39.6	31.8	23.3	22.4	19.1
Overall sector average						**7**	**26.5**	**21.5**	**17.9**	**16.5**	**13.0**	**10.6**

Prices as of 11 March 2011

Source: Bloomberg for non-rated stocks, Nomura estimates

Valuation methodology and risks for Genting Malaysia:

Valuation methodology: We set our price target based on the stock's average historical discount to DCF-based RNAV since 1997. Risks: Although we believe that to a large extent concern of potential loss of revenue to the two Singapore casinos has been largely priced in, a sharper-than-expected fall in GENM's revenue would likely see the shares trading at a sharper discount to RNAV. Conversely, a lower-than-expected loss in revenue could be an upside risk to our estimates and price target.

Valuation methodology and risks for Genting Singapore:

Valuation methodology: We value GENS using an EV/EBITDA multiple of 12x. Upside risks to our REDUCE call include: 1) higher-than-expected wins per table and slots for its table games and slot machines; we have assumed wins per table per day at 50% of Macau average for VIP tables and 67% of Macau average for mass market tables. For slot machines, we assume wins per slot per day in-line with Macau averages. 2) Higher-than-expected visitors to both its Universal Studios theme park and casino.

Still growing

No sign of slowdown

2010 finished with 58% y-y growth in Macau gaming revenue for the full year, even given the high base effect stemming from 2H09. An increase in VIP revenue played a large role in driving this result — VIP grew 70% versus mass market growth of only 30%. The strong liquidity spilt over to 2011 to fuel strong revenue numbers in the past two months. February surprised the market with record revenue of MOP19.9bn (47% y-y growth), given that it is usually a seasonally weaker period and is the shortest month of the year. We think this upbeat momentum sets a foundation for the sector to continue its robust growth. Our view and assumption is also supported by a strong China economic backdrop (Nomura expects GDP to grow by 9.8%), the healthy expected growth in internal consumption in China as well as Chinese currency appreciation (3-5% in 2011 according to Nomura).

Strong China economic backdrop (Nomura expects GDP to grow by 9.8%), the healthy expected growth in internal consumption in China as well as Chinese currency appreciation

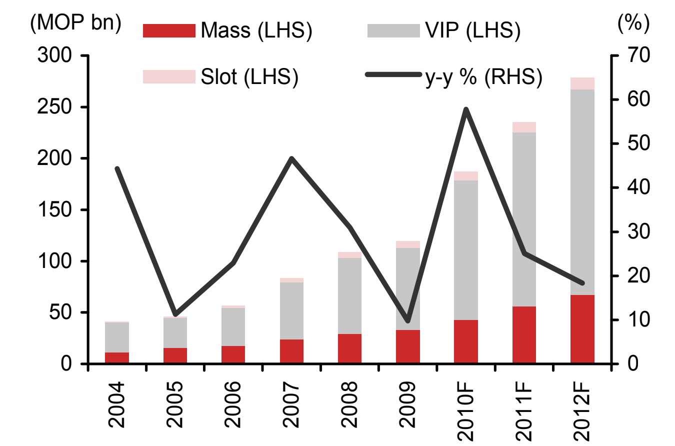
Expecting 26% revenue growth

We are not worried about the risk of a slowdown. February, a month that is physically shorter and was further dampened by an initially slow start, still delivered MOP19.9bn in gaming revenue. Evidence points toward the fact that liquidity within the junket system remains adequate, and shows no sign of slowing. We also expect mass market growth to persist. On that note, our original assumption of 16% growth in VIP gaming revenue seems understated. Therefore, we have increased our VIP revenue assumption to 25% from 16% y-y. We deem the new assumption achievable, but we note that the room to move the estimate further up may be limited at least for the time being, as the growth rate is already implying a monthly run rate of close to MOP20bn. Therefore, current reported revenue is meeting rather than beating expectations, in our view. This could change, however, if Macau were to start delivering monthly gaming revenue of MOP23-24bn.

We expect the strong mass market growth trend to further pick up in 2H11. This is because mass market growth is driven by two forces – visitation growth and spending per visitor. As mentioned, currently, the growth comes predominantly from higher spending per visitor (mass market revenue up 27%, vs visitation of 1% in January 2011; see Exhibit 13). However when we enter the second half of the year, during which the Guangzhou-Zhuhai train line and expansion work at the Gongbei border gate are expected to be completed, we believe that mass market growth could see further upside, fuelled by visitation uptake.

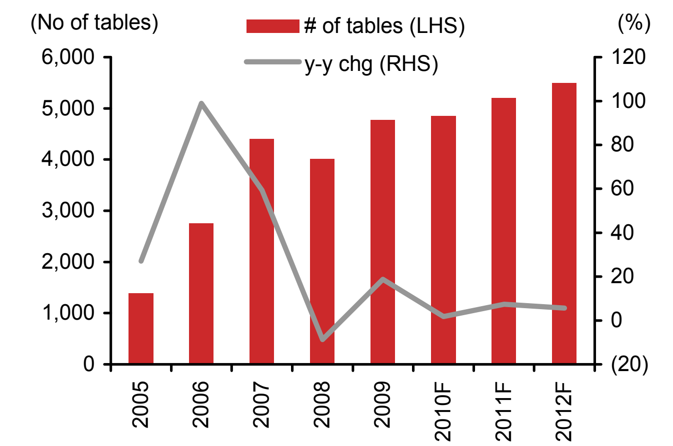
When we enter 2H, during which the Guangzhou-Zhuhai train line and expansion work at the Gongbei border gate are expected to be completed, we believe that mass market growth could see further upside

Exhibit 5. Macau gaming revenue forecast



Source: DICJ

Exhibit 6. Table supply growth



Source: DICJ & Nomura estimates

Mass market and VIP

Mass market robust, VIP could surprise

VIP remains the wild card – abundant junket liquidity shields credit tightening impact

Tighter liquidity could put pressure on VIP business in Macau, but we think that the impact would be far more contained versus 2008

The PBOC hiked the reserve requirement ratio (RRR) by 50bps (effective 24 February, 2011) for a second consecutive time in 2011 and the eighth time since 2010. The benchmark RRR will rise to 19% (19.5% for large financial institutions and 17.5% for small and medium-sized institutions) after the 50bps hike. Our banking team thinks that frequent RRR hikes since November 2010 could be having a cumulative impact on the liquidity condition of China's banking sector. Tighter liquidity could put pressure on VIP business in Macau, but we think that the impact would be far more contained versus 2008.

Junkets have three major sources of funding:

- Retained earnings.
- Private equity sources that invested in the junkets in exchange for an equity stake in the operation.
- Credit lines from casino operators.

All evidence points toward the fact that liquidity remains strong in the sector

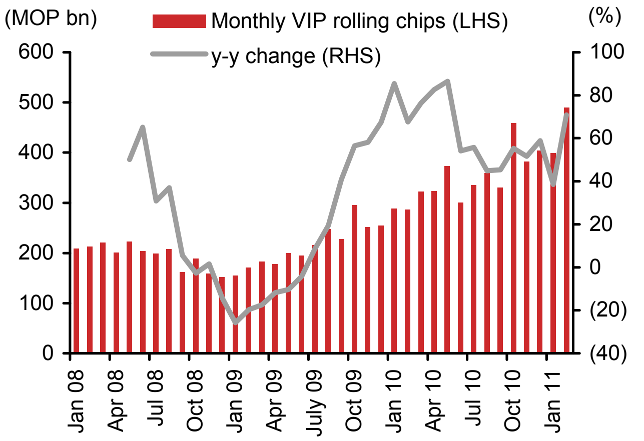
We think retained earnings have become much more abundant as junkets, VIP business promoters, like operators, would have benefited from the robust business growth in 2010. Their balance sheets would also have gotten much stronger versus 2008 as a result – allowing for an initial buffer in the event of a slowdown. Also, junkets have gotten more experienced in managing their cash and screening clients, ie, lending to the "right" people in our view. This helps them to minimise default risk. Based on our recent channel checks, junkets are suggesting that the average number of days for collection lies between 10 days and two weeks, which is healthy, in our view. This ratio implies that the junkets could potentially roll their working capital roughly 2-3 times a month. In addition, some junkets we spoke to stated that they have skipped hosting their annual fund raising party and are stocked up in liquidity. All evidence points toward the fact that liquidity remains strong in the sector.

Another concern on liquidity stems from potential fear of private equity sources pulling out their funding amid tighter credit conditions. However, in reality it is much easier to invest than to pull money out, as the private equity sources / the VIPs are invested in the junkets in exchange for an equity stake in their operations. We think the impact on the way up (as the money flows in) will be much more magnified / faster versus on the way down (as the money gets pulled out) because it won't be an easy quest. Based on junkets that we talked to, it is rare for people to take their money out, in any case.

We expect VIP revenue to grow at 25% y-y in 2011

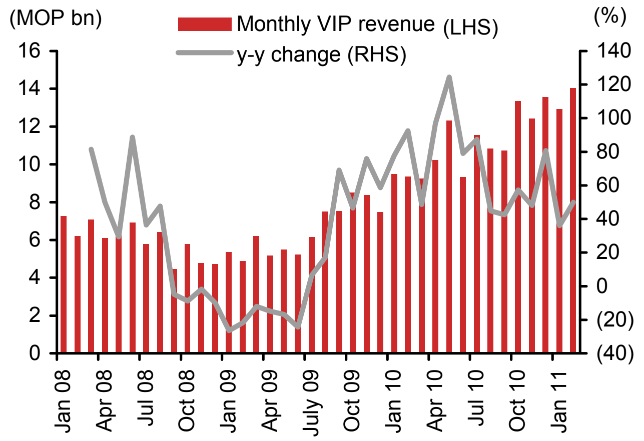
The final source of funding is from casinos. Casinos' credit line accounts for roughly 20% of total working capital of junkets. This seems a relatively stable source, especially given the close working relationship and interdependence between the casinos and the junkets. We think some casinos might be giving out more generous credit lines, helping to boost junkets' working capital at their properties. We expect VIP revenue to grow at 25% y-y in 2011.

Exhibit 7. VIP monthly turnover



Source: DICJ

Exhibit 8. VIP monthly revenue



Source: DICJ & Nomura estimates

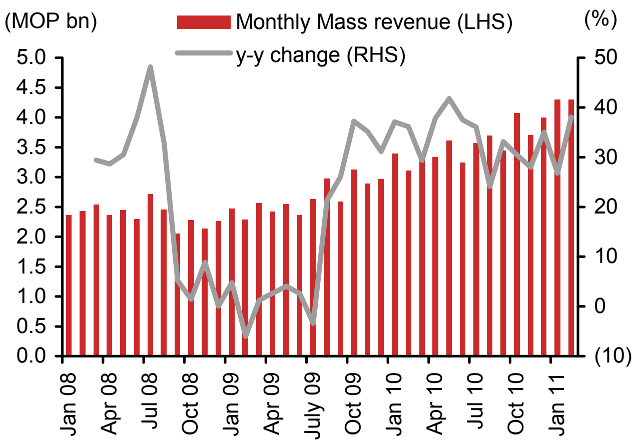
Mass market sees more upside in 2H11

Mass market growth remains robust, as expected and infrastructure upgrades and new openings should drive the mass market higher in 2H11

Mass-market results were relatively muted at the top line, as they only constitute 30% of total gaming revenue versus VIP. But we should not overlook the fact that 1) mass market in January hit a record high with close to 27% growth y-y and 2) this robust trend persisted into Chinese New Year in February. Since we did not see a major pickup in visitation during the given period, we reckon that the growth came primarily from higher spending per visitor. This is as evidenced by our observation as we strolled the mass gaming floors of a few key casinos in Macau during Chinese New Year holiday, a good proportion of the table limits had been lifted from the HK$200-300 average up to HK$500-1,000 average per bet.

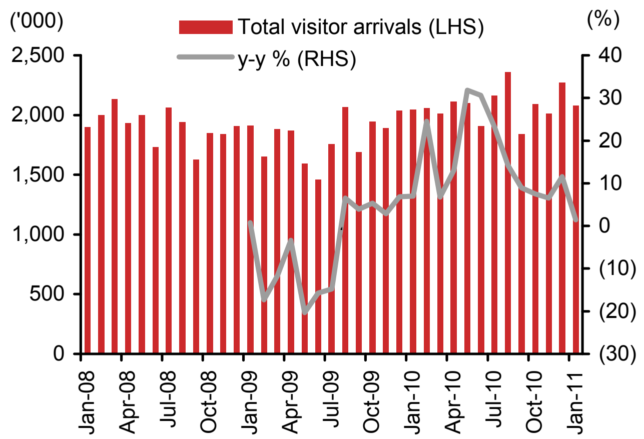
While the spending factor could continue to fuel the mass market, we may see another boost to mass market business from increased visitation in 2H11 driven by infrastructure improvement. The intercity train line that runs from Guangzhou to Zhuhai will likely be completed in 2H11, as well as the expansion work for the Gongbei Border Gate. The opening of a new casino, Galaxy Macau, in May could also help in attracting more visitors to Macau. Overall, we expect mass market revenue to grow at 30% y-y for 2011.

Exhibit 9. Mass market monthly volume



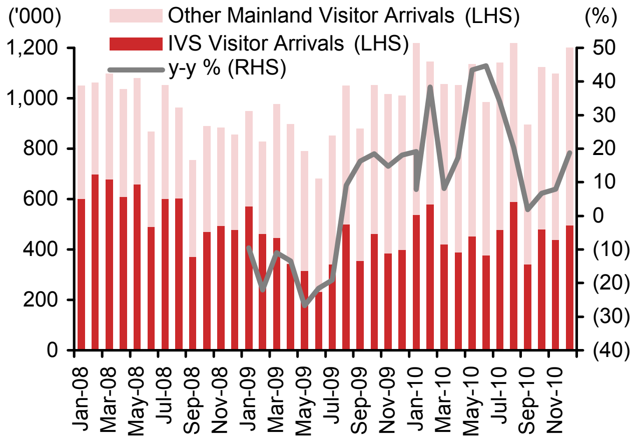
Source: DICJ

Exhibit 10. Macau monthly visitation



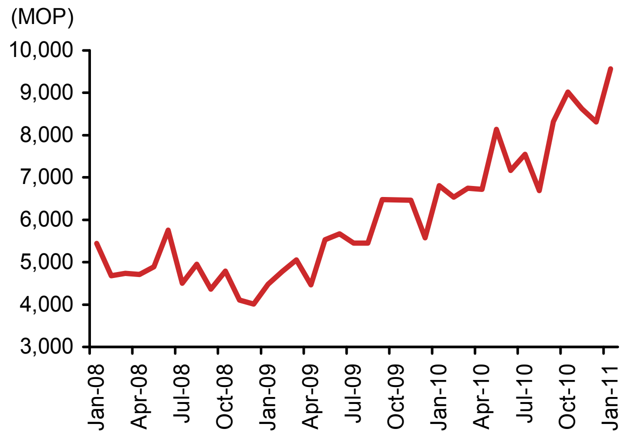
Source: DICJ & Nomura estimates

Exhibit 11. Chinese visitors growth to Macau



Source: DSEC

Exhibit 12. Macau gaming spending per visitor



Source: CEIC

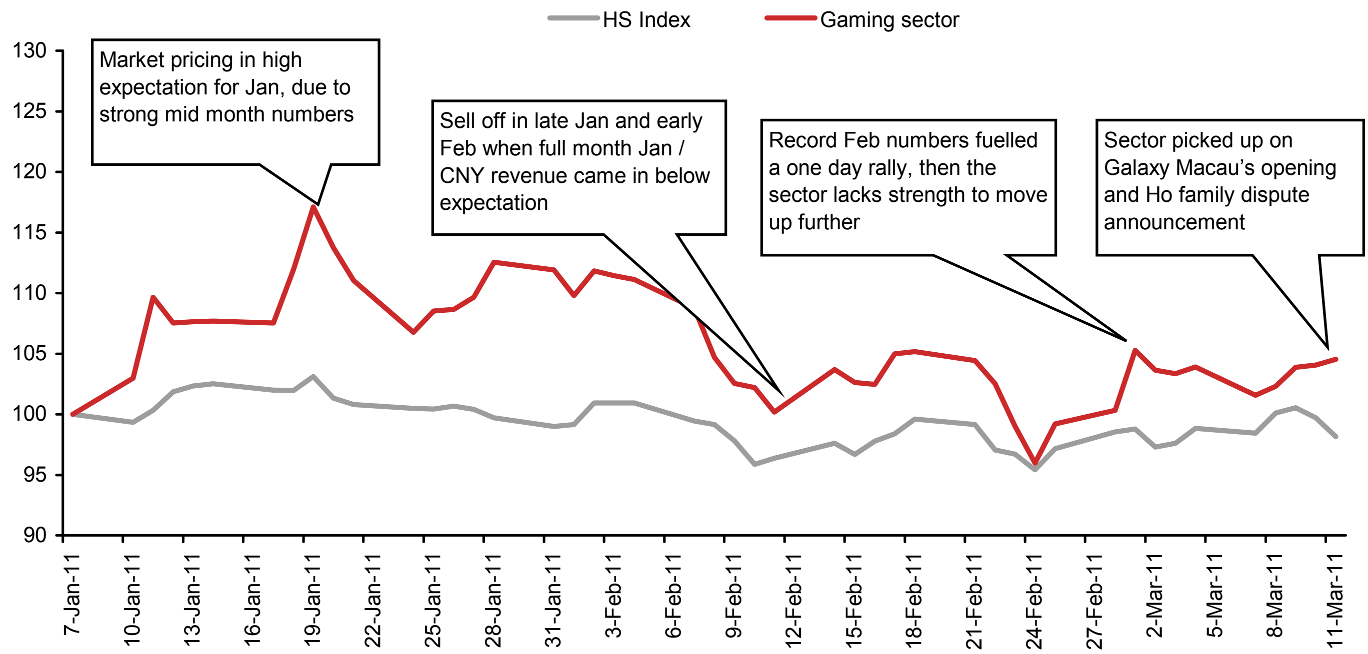
Share price performance

Headline insufficient to drive share prices

Stocks are not budging

Despite seeing strong gaming revenues — January and February delivered 30% and 47% y-y growth, respectively — share prices seem to continue to resist trading up.

Exhibit 13. Macau share price performance



Source: Bloomberg

Share prices seem to be lingering at a similar level as at the beginning of the year. We think this could be explained by the following reasons:

1) Expectation gap

Consensus growth expectation of 25-30% growth creates less room for surprise for the upside and more room for disappointment

The consensus growth rate assumption is now concentrated at 25-30% (implied monthly revenue of MOP20bn), versus the 10-15% recorded in 2010. The high expectation creates less room for upside surprise and more room for disappointment. For example, the sector rallied only on the initial day, when the record revenue number for February was being announced. In the days that followed, the stocks trended slightly down and in a rangebound manner. This is because the MOP19.9bn was already expected and thus in the price. On the flip side, the sector was under noticeable pressure in late January and early February when the full month figure for January and initial Chinese New Year numbers came in shy of expectation (sector down 10% on average versus HSI down 2%), the magnitude of the sell-off mirrored the previous gain of the stocks, ie, the higher it had rallied, pricing in more of the optimism from a potentially strong revenue figure, the more it sold off. The slightest sign of a slowdown in monthly or weekly figures, even though this may only have been due to seasonality, was treated by investors as a structural slowdown, resulting in a large sell-off. Investors prefer to remain cautious.

2) Slowdown = credit tightening, investors look beyond current strength

Investors are worried about a delayed impact from credit tightening

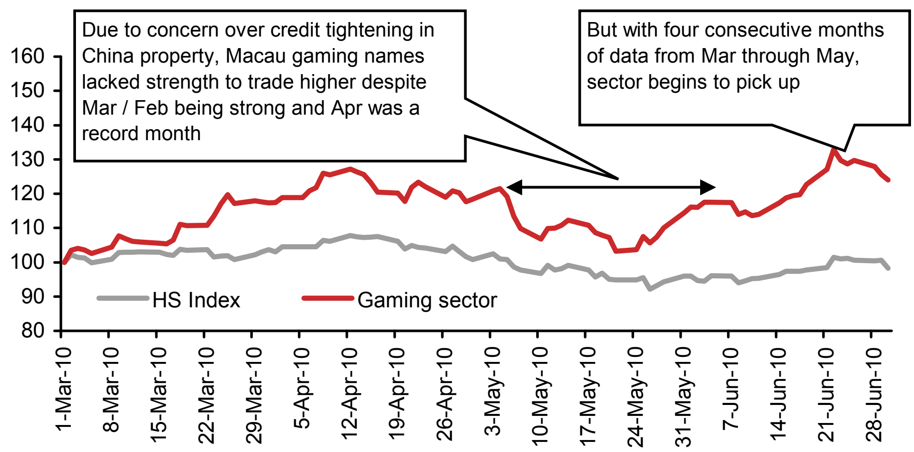
Apart from the gap in expectations that created room for disappointment, another reason for the sell-off was that investors were making a connection between the slowdown and the potential drying up of junket liquidity, which could potentially be a drag on gaming revenue growth in the VIP segment. Even though current gaming revenue appears strong, investors are forward looking. In short, they want to look beyond the strength now, as they fear that credit tightening will have a delayed impact on Macau gaming revenue. Amid rising CPI and inflationary concerns, investors may find themselves more reluctant to pay a premium for this sector in general. On that conservative sentiment, the sector faces difficulty in finding the strength to break through and trade up higher in our view.

If sector re-rates, likely to come in 2Q

Strong data that counter slowdown concern takes time to accumulate, thus re-rating will likely take time as well

With this expectation gap overhang in place, it could take a least a few months of strong revenue to dismiss the concerns of a slowdown from a less exciting economic backdrop. The gap between 15% (expectation) and 58% (actual) is much higher than 30% (expectation) versus 58% (if it were to become actuality). Unless we were to see consecutive months of MOP23-24bn in monthly gaming revenue, it is difficult to prompt consensus to move its growth estimates further up to trigger a re-rating of the sector. Since it takes time to accumulate a few months of strong data, the share price movement will likely replicate this gradual process and move up slowly. This could also be seen in the share price performance during 1H10. Even though we saw a flow of healthy and strong revenue figures from January through May 2010, share prices would not respond, only moving sideways. This is because investors were worried about a delayed impact from credit tightening targeting China property specifically; therefore, even with the current data looking encouraging investors are fixated on the future. In 2010, the stock price really only picked up toward the end of 2Q, and we think the pattern could repeat itself this year, as we worry not about a potential slowdown but the risk introduced by an expectation gap.

Exhibit 14. Macau share price performance in 1H10



Source: Bloomberg

3) Strong 1Q11 results may provide support

Strong mass market revenue in Jan / Feb forms strong foundation for 1Q11 results, which may give sector valuation support

Both January and February reported strong mass market revenue. Since mass market is on average 3-4x the margin of VIP business, the strong momentum in the mass market should have positive implications for earnings in the coming quarter, in our view, especially for mass market focused plays such as Sands China (1928 HK) and SJM (880 HK).

Yet we reckon that strong earnings growth could take longer (one/two quarters) for investors to appreciate, because they are not disclosed as promptly as revenue numbers. This does not change the fact that valuation is ultimately driven by earnings, not revenue. Therefore, even when the top line does not surprise on the upside, earnings could potentially provide a positive surprise, keeping the sector attractive. Lastly, we think the power of earnings growth for the sector will find further support from favourable supply/demand dynamics (6-7% supply and 26% demand growth – up from 18%) which should allow for better operating leverage over the course of this year. Since 1Q results are expected to start coming in May, strong earnings reports may act as an extra force in the re-rating of the sector.

Macro/micro factors

When macro=consensus, micro matters

Consensus call on 25-30% growth estimate brings micro factors to the fore in stock picking

The sector started 2010 with 15-18% q-q growth assumptions. Therefore, top-line revenue numbers more readily beat expectation, sometimes by a large margin. This benefited the whole Macau sector for casino operators. All stocks delivered very strong upside, including Melco International, which had been a loss-making company. However, for this year, beating the bullish 25-30% growth assumption has become harder, especially when 25-30% is the consensus call. On that note, the strategy of buying a whole basket of Macau stocks will most likely no longer work or maximise upside for investors. Micro, stock-specific factors have come to the fore and will begin to matter more, we think, requiring investors to be selective.

Picking the right exposure

The combo

The slowdown risk for the sector is relatively low, as fundamentals are intact amid favourable supply/demand dynamics and still robust liquidity, but the expectation gap continues to introduce higher risk on the downside than upside to the gaming sector, in our view. This is especially true for stocks that have delivered very strong performance, pricing in much of the optimism from growth expectations. We recommend a combo to get exposure to the sector.

Core holding: defensive laggard play

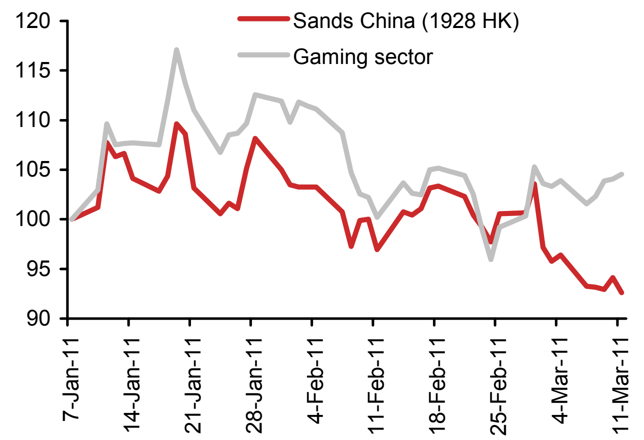
First, to counter this risk to minimise downside in case of a revenue growth disappointment, investors should pick stocks which have:

- lagged the sector year to date, providing less room for downward correction;
- stronger earning resilience in case of a VIP slowdown due to a higher exposure to mass market and non-gaming revenue;
- positive news flow in the pipeline.

We like Sands China (1928 HK)

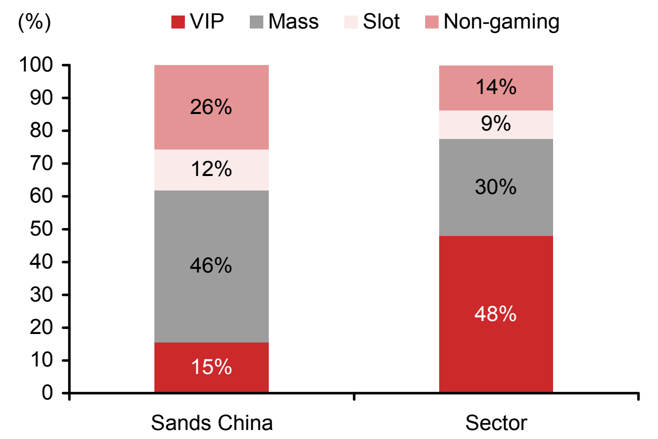
- Sands China is down 0.4%, lagging the sector, which has been up 14% year to date, and therefore in the case of a revenue slowdown, Sands China should find itself less susceptible than other names that have priced in relatively more upside.
- Its mass gaming and non-gaming EBITDA contributes roughly 85% of total EBITDA, and therefore in the case of a top-line revenue slowdown driven by VIP growth, Sands China should be affected less; also, its high mass market exposure should allow it, in our view, to better capture growth potential from the visitation boost driven by infrastructural upgrades, most of which will be completed in 2H11.
- Its share price has been hit lately due to an investigation and allegations held against its parent company, but given the recent correction we think the negatives have been priced in. The stock should find support from 1) strong 1Q11 results due to the strong mass gaming revenue collected in January and over the Chinese New Year period; 2) additional updates on the labour hiring progress of 5 & 6, especially after Galaxy Macau opens, which should help to free up labour; and 3) the eventual sale of the Four Seasons apartment building (likely in 1H11), which could help Sands China to unlock value from its portfolio of non-core assets.

Exhibit 15. Sands China vs. sector performance



Source: DICJ

Exhibit 16. Sands China EBITDA breakdown vs. sector



Source: DICJ & Nomura estimates

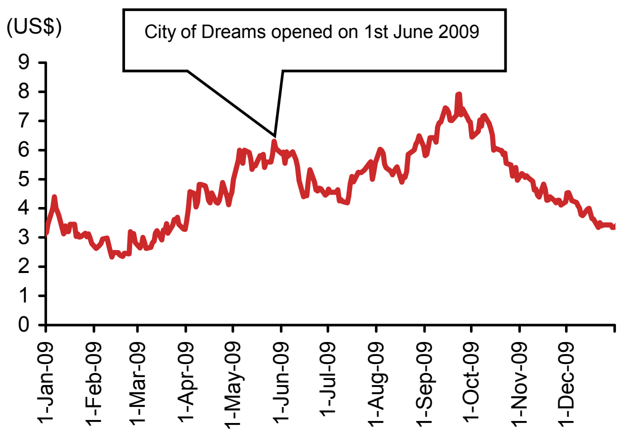
Hedge: high beta name boosted by catalysts

As a hedge against a potential change in sentiment, where March potentially posts another month of record revenue which is off the radar at MOP22-24bn, we recommend owning Galaxy in the portfolio to capture upward momentum.

Galaxy is a beta play (27 HK)

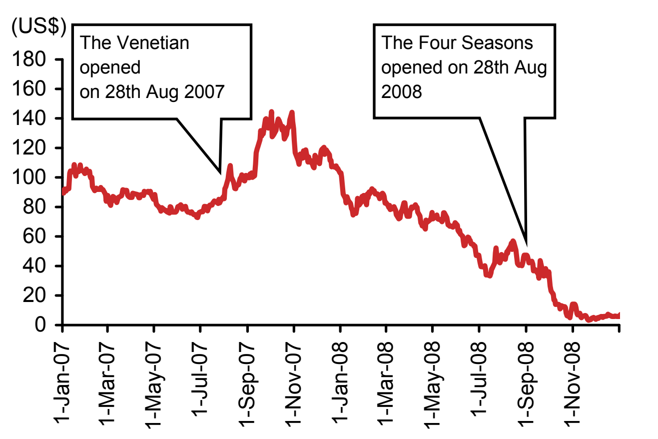
As a VIP-centric name (prior to opening to Galaxy Macau), Galaxy is more likely to continue to benefit should market momentum turn strong. More importantly, amid bullish sentiment, investors could become more ready to assign a premium to its option value – Galaxy Macau, the mega resort project on Cotai due to open in early 2011. The logic is that investors could be more upbeat and confident about the earnings ability of the project if revenue continues to be strong. A new project typically triggers the operator's stock to rally two months prior to the opening. Galaxy's management will likely provide guidance on the process at its newly scheduled party on 16 March, which could clear up any uncertainty and give further support to the share price.

Exhibit 17. Share price impact from the opening of City of Dreams on MPEL



Source: Bloomberg

Exhibit 18. Share price impact from the opening of Venetian on LVS



Source: Bloomberg

Sands China 1928 HK

GAMING, HOTELS & LEISURE | CHINA

Maintained

BUY

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Action

We like Sands China (SC) as it has: 1) lagged the sector by 14% ytd; 2) high mass market business that reduces the impact of top-line volatility and maximizes benefits from potential visitation growth in 2H11 on infrastructure upgrades; 3) positive catalysts in the pipeline (visibility on Lot 5&6; Four Seasons apartment sales). Overreaction on litigation and govt investigation has led to a good entry point, and we do not think its Macau concession is at risk. Valuation is attractive at 12.5x FY11F EBITDA (11x ex-Lot 5&6). Maintain BUY; raise PT to HK$24.

Catalysts

Easing of labour constraints gives improved visibility to progress of Lot 5&6; sales of Four Seasons apartments; and clarification around Jacobs' case.

Anchor themes

We favour stocks with resilient qualities in a downturn as the expectation gap has introduced higher downside risk.

Closing price on 11 Mar	HK$17.02
Price target	**HK$24.00**
	(from HK$20.00)
Upside/downside	41.0%
Difference from consensus	**4.3%**
FY11F net profit (US$mn)	904
Difference from consensus	**14.6%**

Source: Nomura

Nomura vs consensus

The consensus price target spans a wide range of HK$18 to HK$27, distorting the comparison.

Attractive risk/reward profile

① Three reasons to BUY

We like SC as it has: 1) lagged the sector by 14% ytd, making it more resilient than peers if revenue growth falls short of expectation; 2) high mass market exposure, thus making it more immune to a potential VIP slowdown and better positioned to capture visitation growth in 2H11; and 3) positive newsflow catalysts – namely, progress on Lot 5&6 and Four Seasons-serviced apartment sales. These factors should provide valuation support, in our view. We think concern over the corruption investigation and litigation from the ex-CEO is overdone, as the charges and potential fines (likely modest) are pressed against the parent company, not SC. Thus, we see no threat to SC's Macau concession at present and believe the recent correction presents a buying opportunity.

② Valuation is attractive when allowing for fair adjustment

SC is trading at 12.5x FY11F EBITDA, still viewed as high by investors. However, we see EBITDA as understated by a lack of contribution from Lot 5&6 and EV as overstated by capex spending on the project. Adjusted for those factors, SC trades at 11x FY11F EBITDA. For FY12F, the first year with an earnings impact stemming from Lot 5&6 (assumed opening in 2Q12), the multiple stands at 9x.

③ In-line 4Q10, expect stronger 1Q11

EBITDA was also flat q-q due to a lower than theoretical win rate in the VIP business at Four Seasons, but this was in part compensated by the non-gaming revenue gain at the Venetian. We expect to see stronger q-q improvement in 1Q11 due to strong mass market revenue and market share recorded in Jan and CNY holiday in Feb.

④ Maintain BUY, raise price target to HK$24

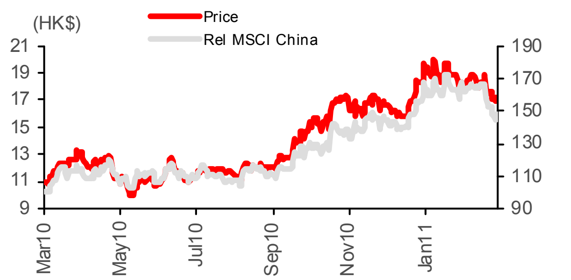
Our higher PT reflects higher expected earnings. Downside risks include: 1) regulatory risks, especially from China; 2) substantial delays from its Cotai project on unresolved labour issue; and 3) more market share losses from competition.

Key financials & valuations

31 Dec (US$mn)	FY09	FY10F	FY11F	FY12F
Revenue	3,301	4,144	4,989	7,007
Reported net profit	213	639	904	1,116
Normalised net profit	213	639	904	1,116
Normalised EPS (US$)	0.026	0.079	0.112	0.139
Norm. EPS growth (%)	20.7	200.4	41.5	23.5
Norm. P/E (x)	82.6	27.5	19.4	15.7
EV/EBITDA (x)	24.5	15.9	12.5	9.1
Price/book (x)	4.8	4.1	3.4	2.8
Dividend yield (%)	0.0	0.0	0.0	0.0
ROE (%)	8.6	15.9	18.9	19.3
Net debt/equity (%)	51.9	31.8	21.2	5.7
Earnings revisions				
Previous norm. net profit		584	647	976
Change from previous (%)		9.4	39.7	14.4
Previous norm. EPS (US$)		0.073	0.080	0.121

Source: Company, Nomura estimates

Share price relative to MSCI China



	1m	3m	6m
Absolute (HK$)	(4.5)	1.7	40.4
Absolute (US$)	(4.5)	1.4	40.0
Relative to Index	(8.6)	2.8	34.9
Market cap (US$mn)			17,579
Estimated free float (%)			29.7
52-week range (HK$)			20.15/10.14
3-mth avg daily turnover (US$mn)			21.47
Stock borrowability			Easy
Major shareholders (%)			
Las Vegas Sands Corp			70.3

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

We continue to value Sands China using a sum-of-the-parts methodology:

Casino operation: 13x FY11F EBITDA with the exception of Venetian and Sands Macao at 14.5x FY11F EBITDA

- For its existing operations – The Plaza and other operations less corporate expenses – we continue to apply a multiple of 13x FY11F EBITDA, toward the higher end of the industry average range of 12-14x. We believe that SC's existing casino operations have a competitive advantage over its peers in terms of earnings quality (more mass market), and this is particularly true for Venetian Macao and Sands Macao, which are considered "must-see" attractions in Macau. Therefore, we continue to use 14.5x to value those two properties (at the high end of the industry average range of 12-14.5x).

Four Seasons serviced apartments: HK$9,000/sq ft

- We lift the attributed value for the Four Seasons serviced apartments to US$923mn or HK$9,000/sq ft, in line with the transaction price of Mandarin Oriental serviced apartments in the secondary market. We consider the latter a more relevant reference than the One Central Apartments (which we have previously been using as a reference), another high-end project in Macau.

Lot 5&6: 12x FY12F EBITDA

- For Lot 5&6, we now apply 12x annualized FY12F EBITDA of US$410mn (10% RoIC), adjusted for the incremental capex and discounted back to FY10F. We have lifted our target multiple to 12x from 10x to capture improved visibility on the project amid the easing of labour constraints. Our revised multiple is consistent with that we use for Galaxy Macau by Galaxy Entertainment.

Our valuation methodology is unchanged; the upward revision to our price target mainly reflects our higher EBITDA and revenue forecasts, which are supported by stronger overall sector growth.

Exhibit 19. Sands China: NEW sum-of-the-parts valuation

Divisions	Valuation methodology	2011F NAV (US$mn)	Per share (US$)	Per share (HK$)
Gaming				
Sands Macao	14.5x FY11F EBITDA	5,294	0.66	5.13
Venetian Macao	14.5x FY11F EBITDA	14,601	1.81	14.15
Four Seasons	13x FY11F EBITDA	2,252	0.28	2.18
Ferry business	13x FY11F EBITDA	(490)	(0.06)	(0.48)
Less: Corporate expense	13x FY11F EBITDA	(234)	(0.03)	(0.23)
Gross asset value		21,423	2.66	20.76
less net debt/(cash)	FY11F year-end forecast	*(1,109)*	(0.14)	(1.07)
Net asset value ex-Lot 5&6		**20,314**	**2.52**	**19.69**
Four season apartment sale	HK$9,000/sq ft, 0.8m salable GFA	923	0.11	0.89
Lot 5&6	12x FY12F annualized EBITDA of US$410mn, discount back to 2011 at 11.5%, less US$1bn capex	3,524	0.44	3.42
Target valuation by end-FY11				**24.00**

Source: Nomura estimates

Exhibit 20. Sands China: OLD sum-of-the-parts valuation

Divisions	Valuation methodology	2011F NAV (US$mn)	Per share (US$)	Per share (HK$)
Gaming				
Sands Macao	14.5x FY11F EBITDA	4,971	0.62	4.82
Venetian Macao	14.5x FY11F EBITDA	12,603	1.57	12.22
Four Seasons	13x FY11F EBITDA	2,114	0.26	2.05
Ferry business	13x FY11F EBITDA	(478)	(0.06)	(0.46)
Less: Corporate expense	13x FY11F EBITDA	(234)	(0.03)	(0.23)
Gross asset value		18,976	2.36	18.39
less net debt/(cash)	FY11F year-end forecast	(1,728)	(0.21)	(1.67)
Net asset value ex-Lot 5&6		**17,249**	**2.14**	**16.72**
Four season apartment sale	HK$6,000/sq ft, 0.8m saleable GFA	615	0.08	0.60
Lot 5&6	10x FY12F annualized EBITDA of US$404mn, discounted back to 2011 at 11.5% less US$950mn capex	2,771	0.34	2.69
Target valuation by end-FY11				**20.00**

Source: Nomura estimates

Risks to our investment view

Downside risks include: 1) regulatory risks, especially from China; 2) substantial delays from its Cotai project; and 3) more market share losses from competition.

Financial statement analysis

Earnings revisions

After factoring in our new market share and gaming revenue assumptions, we have increased our EBITDA forecasts for Sands China.

- Our market share assumptions remain largely unchanged with the exception for the Lot 5&6 project, as we trimmed market share assumptions to factor in more conservative expectations for opening dates.

Below we summarise the changes to our assumptions

Exhibit 21. Sands China: Earnings estimate revisions

Operating assumptions	Group gaming revenue			VIP segment			Mass segment		
	FY10	FY11F	FY12F	FY10	FY11F	FY12F	FY10	FY11F	FY12F
Old									
Revenue (US$mn)	4,463	5,027	7,301	2,620	2,935	4,498	1,521	1,734	2,394
Market share (%)	19	18	23	17	15	20	27	26	30
New									
Revenue (US$mn)	**4,525**	**5,428**	**7,647**	**2,614**	**3,200**	**4,829**	**1,582**	**1,864**	**2,400**
Market share (%)	**19**	**18**	**21**	**16**	**15**	**19**	**27**	**26**	**28**

Financial assumptions	EPS (US$)			EBITDA (US$mn)			EBITDA margin (%)		
Old	0.07	0.08	0.12	1,152	1,320	1,843	23	23	22
New	**0.08**	**0.11**	**0.14**	**1,207**	**1,490**	**1,963**	**23**	**24**	**22**
Change	0.01	0.03	0.02	55.2	169.7	120.4	0.7	1.0	0.2
Change (%)	9	40	14	5	13	7	3	4	1

Note: Group gaming revenue also includes revenue from slots, which is not broken down separately

Source: Nomura estimates

Financial statements

Due to higher depreciation from the development of Lot 5&6 in 2012F

Income statement (US$mn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Revenue	3,054	3,301	4,144	4,989	7,007
Cost of goods sold					
Gross profit	**3,054**	**3,301**	**4,144**	**4,989**	**7,007**
SG&A	(2,663)	(2,838)	(3,319)	(3,909)	(5,718)
Employee share expense					
Operating profit	**391**	**463**	**825**	**1,080**	**1,288**
EBITDA	**671**	**796**	**1,190**	**1,490**	**1,963**
Depreciation	(268)	(320)	(347)	(392)	(658)
Amortisation	(12)	(13)	(19)	(18)	(17)
EBIT	**391**	**463**	**825**	**1,080**	**1,288**
Net interest expense	(118)	(150)	(146)	(146)	(147)
Associates & JCEs					
Other income	(97)	(100)	(40)	(30)	(25)
Earnings before tax	**176**	**213**	**639**	**904**	**1,116**
Income tax					
Net profit after tax	**176**	**213**	**639**	**904**	**1,116**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**176**	**213**	**639**	**904**	**1,116**
Extraordinary items					
Reported NPAT	**176**	**213**	**639**	**904**	**1,116**
Dividends	-	-	-	-	-
Transfer to reserves	**176**	**213**	**639**	**904**	**1,116**
Valuation and ratio analysis					
FD normalised P/E (x)	99.7	82.6	27.5	19.4	15.7
FD normalised P/E at price target (x)	140.6	116.5	38.8	27.4	22.2
Reported P/E (x)	99.7	82.6	27.5	19.4	15.7
Dividend yield (%)	-	-	-	-	-
Price/cashflow (x)	68.5	24.9	15.2	11.8	8.9
Price/book (x)	14.1	4.8	4.1	3.4	2.8
EV/EBITDA (x)	32.6	24.5	15.9	12.5	9.1
EV/EBIT (x)	56.0	42.1	23.0	17.3	13.9
Gross margin (%)	100.0	100.0	100.0	100.0	100.0
EBITDA margin (%)	22.0	24.1	28.7	29.9	28.0
EBIT margin (%)	12.8	14.0	19.9	21.6	18.4
Net margin (%)	5.8	6.4	15.4	18.1	15.9
Effective tax rate (%)	-	-	-	-	-
Dividend payout (%)	-	-	-	-	-
Capex to sales (%)	64.6	11.7	11.3	21.4	15.3
Capex to depreciation (x)	7.4	1.2	1.4	2.7	1.6
ROE (%)	15.3	8.6	15.9	18.9	19.3
ROA (pretax %)	7.3	7.3	12.7	15.6	17.3
Growth (%)					
Revenue	55.4	8.1	25.6	20.4	40.5
EBITDA	31.3	18.6	49.5	25.1	31.8
EBIT	(1.6)	18.3	78.3	30.9	19.4
Normalised EPS	(10.1)	20.7	200.4	41.5	23.5
Normalised FDEPS	(10.1)	20.7	200.4	41.5	23.5
Per share					
Reported EPS (US$)	0.02	0.03	0.08	0.11	0.14
Norm EPS (US$)	0.02	0.03	0.08	0.11	0.14
Fully diluted norm EPS (US$)	0.02	0.03	0.08	0.11	0.14
Book value per share (US$)	0.16	0.46	0.54	0.65	0.79
DPS (US$)	-	-	-	-	-

Source: Nomura estimates

Cashflow (US$mn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
EBITDA	671	796	1,190	1,490	1,963
Change in working capital	(113)	54	3	25	26
Other operating cashflow	(302)	(146)	(42)	(32)	(25)
Cashflow from operations	**256**	**704**	**1,152**	**1,483**	**1,965**
Capital expenditure	(1,974)	(386)	(470)	(1,070)	(1,070)
Free cashflow	**(1,717)**	**319**	**682**	**413**	**895**
Reduction in investments	(45)	(338)	-	-	-
Net acquisitions					
Reduction in other LT assets	(92)	70	(2)	(3)	-
Addition in other LT liabilities	6	(0)	0	0	-
Adjustments	255	275	3	3	1
Cashflow after investing acts	**(1,594)**	**325**	**683**	**414**	**896**
Cash dividends	-	(146)	-	-	-
Equity issue	-	1,701	-	-	-
Debt issue	1,836	(1,403)	914	(125)	(619)
Convertible debt issue					
Others	(198)	(93)	(147)	(147)	(148)
Cashflow from financial acts	**1,637**	**59**	**766**	**(272)**	**(768)**
Net cashflow	**43**	**384**	**1,449**	**141**	**128**
Beginning cash	499	542	926	2,375	2,516
Ending cash	541	926	2,374	2,516	2,644
Ending net debt	4,342	1,911	1,376	1,109	362

Source: Nomura estimates

Capex for development of Lot 5&6

Balance sheet (US$mn)					
As at 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Cash & equivalents	542	926	2,375	2,516	2,644
Marketable securities					
Accounts receivable	288	295	340	357	375
Inventories	11	10	10	10	11
Other current assets					
Total current assets	**841**	**1,231**	**2,724**	**2,883**	**3,029**
LT investments	338	677	677	677	677
Fixed assets	5,510	5,305	5,410	6,070	6,465
Goodwill					
Other intangible assets	46	41	41	41	41
Other LT assets	152	82	85	87	87
Total assets	**6,888**	**7,336**	**8,937**	**9,758**	**10,299**
Short-term debt	1,285	104	893	637	764
Accounts payable	741	801	849	892	936
Other current liabilities	0	0	0	0	0
Total current liabilities	**2,027**	**905**	**1,742**	**1,528**	**1,700**
Long-term debt	3,599	2,733	2,857	2,988	2,242
Convertible debt					
Other LT liabilities	13	13	13	13	13
Total liabilities	**5,638**	**3,651**	**4,612**	**4,530**	**3,955**
Minority interest					
Preferred stock					
Common stock	-	80	80	80	80
Retained earnings					
Proposed dividends					
Other equity and reserves	1,250	3,605	4,243	5,147	6,263
Total shareholders' equity	**1,250**	**3,685**	**4,324**	**5,228**	**6,344**
Total equity & liabilities	**6,888**	**7,336**	**8,936**	**9,758**	**10,299**
Liquidity (x)					
Current ratio	0.41	1.36	1.56	1.89	1.78
Interest cover	3.3	3.1	5.6	7.4	8.7
Leverage					
Net debt/EBITDA (x)	6.47	2.40	1.16	0.74	0.18
Net debt/equity (%)	347.5	51.9	31.8	21.2	5.7
Activity (days)					
Days receivable	31.6	32.3	28.0	25.5	19.1
Days inventory	na	na	na	na	na
Days payable	na	na	na	na	na
Cash cycle	na	na	na	na	na

Source: Nomura estimates

Galaxy Entertainment Group 27 HK

GAMING, HOTELS & LEISURE | CHINA

From Neutral

BUY

NOMURA

NOMURA INTERNATIONAL (HK) LIMITED

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Action

We upgrade the stock to BUY with a new PT of HK$13.35. As a current VIP-centric play with an option value from the opening of Galaxy Macau (GM), Galaxy is a beta play, in our view, and a hedge on potential positive revenue growth surprise, because the option value often trades at a premium in a bullish market. The recent share price correction presents a good buying opportunity, underpinned further by its less-demanding valuation at 9x FY12F EBITDA, when we believe GM will have its first full-year impact on Galaxy.

Catalysts

More updates on pre-booking and from analysts as property tours of GM are being organized now that the official date of opening has been announced.

Anchor themes

We favour stocks with resilient qualities in a downturn as the expectation gap has introduced higher downside risk.

Closing price on 11 Mar	HK$11.32
Price target	**HK$13.35**
	(from HK$7.50)
Upside/downside	18.0%
Difference from consensus	**2.1%**
FY11F net profit (HK$mn)	2,042
Difference from consensus	**18.7%**

Source: Nomura

Nomura vs consensus

Our estimate is slightly ahead of consensus due to our more optimistic assumptions for Galaxy Macau at US$200mn EBITDA for FY11F.

A beta play – hedge on the upside

① Hedge on potential upside growth

Among the six operators we cover, Galaxy has the highest financial and operating leverage due to its VIP-centric exposure (before GM opens). If revenue growth surprises on the upside, we believe its share price, especially after recent corrections, could rally. In addition, as the demand-supply gap widens further, we believe more optimism will be priced in for its option value on the upcoming GM opening.

② Delay overhand gone; GM opening to buffer downside

The official opening date of GM has been announced as 15 May 2011, removing the stock's biggest perceived overhang. While the announced opening date is slightly behind the original guided date of late 1Q11, GM does not have to compete against others in terms of timeline since it is the only casino scheduled to open in 2011. The Street's average FY12F EBITDA forecast of ~US$400mn for GM seems achievable (vs City of Dreams at >US$300mn and Venetian at >US$800mn as reported in 2010). Last, with Galaxy's clear major catalyst in the pipeline (ie, new opening), investors are likely to hold the stock into the opening of GM, thus giving the downside a buffer.

③ Expect flat 4Q10F – likely be overlooked

Galaxy expects to report its 4Q10 results on 31 Mar, and we expect a 5% q-q decline in revenue due to a lower win rate. We estimate 4Q10F EBITDA will be flat q-q at HK$616mn due to operating leverage.

④ Valuation and risk

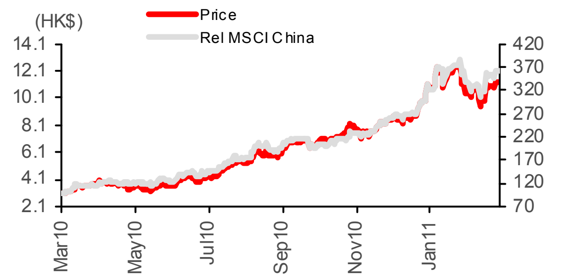
We continue to value Galaxy based on a sum-of-the-parts approach. Downside risks: 1) regulatory risks like visitation quotas; 2) credit tightening on the VIP business; and 3) a significant delay in the opening of GM (we expect the project to launch in 2Q11, likely in May).

Key financials & valuations

31 Dec (HK$mn)	FY09F	FY10F	FY11F	FY12F
Revenue	12,426	19,709	32,044	40,371
Reported net profit	1,149	1,329	2,042	2,573
Normalised net profit	463	1,329	2,042	2,573
Normalised EPS (HK$)	0.12	0.34	0.51	0.64
Norm. EPS growth (%)	na	185.5	52.2	24.7
Norm. P/E (x)	96.3	33.9	22.3	17.9
EV/EBITDA (x)	43.8	24.8	14.8	9.4
Price/book (x)	5.5	4.7	3.9	3.3
Dividend yield (%)	0.0	0.0	0.0	0.0
ROE (%)	15.1	15.0	19.4	20.1
Net debt/equity (%)	28.5	89.0	78.1	36.2
Earnings revisions				
Previous norm. net profit		1,187	1,653	1,901
Change from previous (%)		11.9	23.5	35.4
Previous norm. EPS (HK$)		0.30	0.41	0.47

Source: Company, Nomura estimates

Share price relative to MSCI China



	1m	3m	6m
Absolute (HK$)	8.0	33.2	88.4
Absolute (US$)	8.1	32.9	87.8
Relative to Index	7.5	37.6	86.3
Market cap (US$mn)			5,954
Estimated free float (%)			24.4
52-week range (HK$)			12.48/3.05
3-mth avg daily turnover (US$mn)			17.34
Stock borrowability			Hard
Major shareholders (%)			
Lui Che Woo			75.6

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

We value Galaxy based on a sum-of-the-parts (SOTP) approach, applying slightly different EBITDA multiples to each business segment, based on our view of earnings predictability, property quality and growth potential. Our 12-month PT of HK$13.35 includes: 1) the StarWorld casino at 12x FY11F EV/EBITDA; 2) City Clubs at 6x FY11F EV/EBITDA; and 3) the construction business at book value. Our target valuation of a 12x EV/EBITDA multiple is in line at the low end of the industry average range of 12-14x.

Since it is now near the opening of Galaxy Macau, we apply 13x EV/EBITDA to value Galaxy Macau, up from 10x. This is because we believe that in a bullish market, the market could assign a premium to this option value that sits on Galaxy's valuation.

In short, our valuation methodology remains unchanged.

Exhibit 22. Galaxy: NEW sum-of-the-parts valuation

Divisions	Valuation methodology	FY11F NAV (HK$mn)	Per share (HK$)
Gaming		**58,566**	**14.57**
Galaxy StarWorld	12x FY11F EBITDA (net of corporate expenses)	18,717	4.65
Galaxy Macau	13x FY12E EBITDA discounted at 11.5%	38,879	9.67
CityClubs	6x FY11F EBITDA	970	0.24
Construction materials	**9x FY11F EBITDA**	**4,131**	**1.03**
Gross Asset Value		**62,697**	**15.59**
Less net debt	FY11F year-end forecast	9,008	2.24
Target valuation end-FY11		**53,689**	**13.35**

Source: Nomura estimates

Exhibit 23. Galaxy: OLD sum-of-the-parts valuation

Divisions	Valuation methodology	FY11F NAV (HK$mn)	Per share (HK$)
Gaming		**37,648**	**9.36**
Galaxy StarWorld	12x FY11F EBITDA (net of corporate expenses)	14,254	3.54
Galaxy Macau	10x FY11F annualized EBITDA	22,589	5.62
CityClubs	6x FY11F EBITDA	805	0.20
Construction materials	**9x FY11F EBITDA**	**1,720**	**0.43**
Gross Asset Value		**39,369**	**9.79**
Less net debt	FY11F year-end forecast	9,226	2.29
Target valuation end-FY11		**30,143**	**7.50**

Source: Nomura estimates

Investment risks

Potential downside risks include: 1) regulatory risks from China; and 2) a slower-than-expected completion of Galaxy Macau leading to a significant delay.

Financial statement analysis

Earnings revisions

After factoring in our new market share and gaming revenue assumptions, we increase our EBITDA forecasts for Galaxy.

- The adjustment to FY11F EBITDA is due mainly to a change in our assumed EBITDA for StarWorld. Previously, we assumed StarWorld's EBITDA would drop 17% y-y in FY11 due to the impact of the opening of Galaxy Macau. Given that the opening is now slightly delayed and with our higher industry growth and margin assumptions, however, we now look for StarWorld's EBITDA to be almost flat y-y in FY11F.
- We also revise our FY12F EBITDA estimates to account for our higher projections for GM and, to a lesser degree, StarWorld. Having observed the turnaround achieved by a similar mega resort property, City of Dreams, which delivered US$213mn in EBITDA in 2H10, we revise upwards our FY12F EBITDA for Galaxy Macau from US$380mn to US$430mn to realize its full potential.

Below we summarize the changes to our assumptions:

Exhibit 24. Sands China: Earnings estimate revisions

Operating assumptions

	Group gaming revenue			VIP segment			Mass segment		
	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F
Old									
Revenue (HK$mn)	17,682	26,132	33,111	15,058	20,813	26,314	1,040	3,187	4,389
Market share (%)	12	14	14	14	16	17	5	8	9
New									
Revenue (HK$mn)	**17,613**	**29,084**	**35,997**	**14,874**	**23,773**	**28,052**	**1,154**	**3,287**	**5,683**
Market share (%)	**11**	**14**	**14**	**13**	**16**	**16**	**5**	**8**	**10**

Financial assumptions

	EPS (HK$)			EBITDA (HK$mn)			EBITDA margin (%)		
	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F
Old	0.30	0.41	0.47	1,973	3,223	4,625	10.0	11.0	12.3
New	**0.34**	**0.51**	**0.64**	**2,134**	**3,666**	**5,390**	**10.8**	**11.4**	**13.4**
Change	0.0	0.1	0.2	161.0	443.0	765.3	0.9	0.4	1.0
Change (%)	12	24	35	8	14	17	9	4	8

Note: Group gaming revenue also includes revenue from slots, which is not broken down separately

Source: Nomura estimates

Financial statements

Income statement (HK$mn)					
Year-end 31 Dec	FY08	FY09F	FY10F	FY11F	FY12F
Revenue	10,619	12,426	19,709	32,044	40,371
Cost of goods sold	(3,249)	(4,426)	(7,293)	(12,043)	(14,905)
Gross profit	**7,370**	**8,000**	**12,416**	**20,001**	**25,466**
SG&A	(8,025)	(7,515)	(10,867)	(17,553)	(21,940)
Employee share expense					
Operating profit	**(655)**	**484**	**1,548**	**2,448**	**3,526**
EBITDA	**489**	**1,026**	**2,134**	**3,666**	**5,390**
Depreciation	(352)	(348)	(348)	(992)	(1,650)
Amortisation	(792)	(194)	(238)	(225)	(214)
EBIT	**(655)**	**484**	**1,548**	**2,448**	**3,526**
Net interest expense	(225)	(111)	(136)	(224)	(697)
Associates & JCEs	52	86	80	80	80
Other income	(1,402)	89	10	10	10
Earnings before tax	**(2,231)**	**548**	**1,502**	**2,315**	**2,919**
Income tax	1,503	(76)	(163)	(256)	(325)
Net profit after tax	**(728)**	**472**	**1,339**	**2,058**	**2,593**
Minority interests	165	(9)	(10)	(16)	(20)
Other items					
Preferred dividends					
Normalised NPAT	**(563)**	**463**	**1,329**	**2,042**	**2,573**
Extraordinary items	(10,828)	685	-	-	-
Reported NPAT	**(11,390)**	**1,149**	**1,329**	**2,042**	**2,573**
Dividends	-	-	-	-	-
Transfer to reserves	**(11,390)**	**1,149**	**1,329**	**2,042**	**2,573**
Valuation and ratio analysis					
FD normalised P/E (x)	na	96.3	33.9	22.3	17.9
FD normalised P/E at price target (x)	na	113.6	40.0	26.3	21.1
Reported P/E (x)	na	38.9	33.7	22.2	17.8
Dividend yield (%)	-	-	-	-	-
Price/cashflow (x)	958.3	15.1	12.7	7.1	4.4
Price/book (x)	6.4	5.5	4.7	3.9	3.3
EV/EBITDA (x)	87.0	43.8	24.8	14.8	9.4
EV/EBIT (x)	na	85.4	33.7	21.9	14.3
Gross margin (%)	69.4	64.4	63.0	62.4	63.1
EBITDA margin (%)	4.6	8.3	10.8	11.4	13.4
EBIT margin (%)	(6.2)	3.9	7.9	7.6	8.7
Net margin (%)	(107.3)	9.2	6.7	6.4	6.4
Effective tax rate (%)	na	13.8	10.9	11.1	11.2
Dividend payout (%)	na	-	-	-	-
Capex to sales (%)	14.0	18.8	35.7	7.9	0.8
Capex to depreciation (x)	4.2	6.7	20.2	2.6	0.2
ROE (%)	(89.6)	15.1	15.0	19.4	20.1
ROA (pretax %)	(3.3)	4.1	8.4	10.3	14.2
Growth (%)					
Revenue	(19.7)	17.0	58.6	62.6	26.0
EBITDA	(60.2)	109.7	108.1	71.8	47.0
EBIT	na	na	219.6	58.1	44.0
Normalised EPS	na	na	185.5	52.2	24.7
Normalised FDEPS	na	na	183.9	52.2	24.7
Per share					
Reported EPS (HK$)	(2.89)	0.29	0.34	0.51	0.64
Norm EPS (HK$)	(0.14)	0.12	0.34	0.51	0.64
Fully diluted norm EPS (HK$)	(0.14)	0.12	0.33	0.51	0.63
Book value per share (HK$)	1.78	2.07	2.39	2.87	3.48
DPS (HK$)	-	-	-	-	-

Source: Nomura estimates

Galaxy Macau as the main earnings driver in FY12F

Cashflow (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09F**	**FY10F**	**FY11F**	**FY12F**
EBITDA	489	1,026	2,134	3,666	5,390
Change in working capital	(39)	718	(581)	(670)	(141)
Other operating cashflow	(403)	1,221	1,971	3,410	5,065
Cashflow from operations	**47**	**2,965**	**3,523**	**6,406**	**10,314**
Capital expenditure	(1,487)	(2,332)	(7,035)	(2,535)	(335)
Free cashflow	**(1,441)**	**633**	**(3,512)**	**3,871**	**9,979**
Reduction in investments	(326)	(170)	(80)	(80)	(80)
Net acquisitions	(21)	-	-	-	-
Reduction in other LT assets	309	(62)	-	-	-
Addition in other LT liabilities	(1,995)	103	-	-	-
Adjustments	2,104	212	122	128	199
Cashflow after investing acts	**(1,369)**	**715**	**(3,470)**	**3,919**	**10,098**
Cash dividends	(2)	(0)	-	-	-
Equity issue	1	2	-	-	-
Debt issue	103	(1,798)	7,763	-	-
Convertible debt issue					
Others	(440)	(368)	(535)	(816)	(816)
Cashflow from financial acts	**(338)**	**(2,164)**	**7,228**	**(816)**	**(816)**
Net cashflow	**(1,707)**	**(1,449)**	**3,758**	**3,103**	**9,281**
Beginning cash	8,230	6,042	3,516	5,151	4,597
Ending cash	6,524	4,593	7,274	8,253	13,879
Ending net debt	670	2,327	8,455	9,008	5,107

Source: Nomura estimates

Debt restructuring to re-finance Galaxy Macau

Balance sheet (HK$mn)					
As at 31 Dec	**FY08**	**FY09F**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	6,042	3,516	5,151	4,597	8,499
Marketable securities					
Accounts receivable	1,799	986	1,774	2,660	3,028
Inventories	94	85	85	85	85
Other current assets	18	38	38	38	38
Total current assets	**7,953**	**4,625**	**7,047**	**7,379**	**11,649**
LT investments	833	1,003	1,083	1,163	1,243
Fixed assets	8,086	11,589	18,528	20,509	19,088
Goodwill					
Other intangible assets	1,488	1,391	1,260	1,141	1,033
Other LT assets	292	354	354	354	354
Total assets	**18,651**	**18,963**	**28,271**	**30,545**	**33,366**
Short-term debt	436	1,383	3,221	3,221	3,221
Accounts payable	4,255	4,120	4,326	4,542	4,769
Other current liabilities	11	62	62	62	62
Total current liabilities	**4,702**	**5,565**	**7,609**	**7,826**	**8,053**
Long-term debt	6,276	4,460	10,384	10,384	10,384
Convertible debt					
Other LT liabilities	400	503	503	503	503
Total liabilities	**11,378**	**10,528**	**18,496**	**18,713**	**18,940**
Minority interest	263	267	277	293	313
Preferred stock					
Common stock	394	394	394	394	394
Retained earnings					
Proposed dividends					
Other equity and reserves	6,617	7,774	9,103	11,146	13,719
Total shareholders' equity	**7,011**	**8,169**	**9,498**	**11,540**	**14,113**
Total equity & liabilities	**18,651**	**18,963**	**28,271**	**30,546**	**33,366**
Liquidity (x)					
Current ratio	1.69	0.83	0.93	0.94	1.45
Interest cover	(2.9)	4.3	11.4	10.9	5.1
Leverage					
Net debt/EBITDA (x)	1.37	2.27	3.96	2.46	0.95
Net debt/equity (%)	9.5	28.5	89.0	78.1	36.2
Activity (days)					
Days receivable	54.8	40.9	25.6	25.2	25.8
Days inventory	10.4	7.4	4.2	2.6	2.1
Days payable	459.4	345.3	211.3	134.4	114.3
Cash cycle	(394.3)	(297.0)	(181.5)	(106.6)	(86.5)

Source: Nomura estimates

SJM Holdings 880 HK

GAMING, HOTELS & LEISURE | CHINA

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NOMURA INTERNATIONAL (HK) LIMITED

Maintained

BUY

Action

SJM management's ability and wealth of experience has our vote of confidence, and we expect the team to continue to deliver strong execution and solid operation as reflected in SJM's resilient market share. Last week's announcement that the Ho family dispute had been resolved has helped alleviate some of the concern and should serve as a short-term catalyst, with strong 4Q10 results (16 March) likely to offer valuation support. But investor confidence will likely take time to re-build before the stock re-rates, in our view. Maintain BUY; PT raised to HK$15.50.

Catalysts

Government approval and announcement of a detailed development plan for SJM's new project in Cotai in the near future could re-rate the stock.

Anchor themes

We favour stocks with resilient qualities in a downturn, given that the expectation gap has introduced higher downside risk.

Closing price on 11 Mar	HK$12.80
Price target	**HK$15.50**
	(from HK$15.00)
Upside/downside	21.1%
Difference from consensus	**0.1%**
FY11F net profit (HK$mn)	4,674
Difference from consensus	**5.7%**

Source: Nomura

Nomura vs consensus

Our estimates are largely in line with consensus.

Solid fundamentals; investor confidence needs time to rebuild

① First-class execution and operation

We remain confident in SJM management's ability and long-standing experience in delivering strong execution and solid operation, as reflected in the company's resilient market share, especially amid stiffer competition in the VIP market. With a 40%-plus share in the mass market segment, strong mass gaming revenue recorded in January and February is likely to benefit SJM relatively more than others, in our view, forming a strong base for FY11F.

② Investor confidence may take time to re-build

We are confident in the fundamentals of the company, and we reckon that the 10 March, 2011 announcement that the Ho family has reached on an agreed resolution will work in the best interest of the company. Given the lack of details on the ownership breakdown, however, some investors may remain sceptical. Thus, it may take time for investors to fully regain confidence before the stock re-rates.

③ Potential boost from 4Q10F results

We expect SJM to deliver robust 4Q10F EBITDA at HK$1.4bn, benefiting from resilient market share amid strong sector growth, in part due to higher yield from reconfiguration at Grand Lisboa, its flagship property. The stock price may find short-term strength from a 4Q10F earnings surprise.

④ Valuation and risk

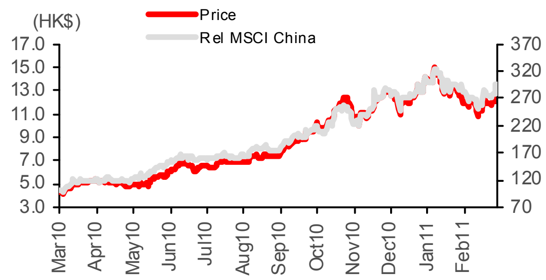
We continue to use SOTP valuation, but adjust down our valuation multiple to reflect weakened investor confidence, which may take time to re-build. Downside risks include: 1) regulatory change in China; 2) underperformance of the Oceanus/legacy casinos; and 3) uncertainty over the chairman's health and new round of family disputes.

Key financials & valuations

31 Dec (HK$mn)	FY09	FY10F	FY11F	FY12F
Revenue	34,408	57,468	73,138	83,821
Reported net profit	906	3,427	4,674	5,494
Normalised net profit	1,106	3,437	4,684	5,504
Normalised EPS (HK$)	0.22	0.66	0.87	1.02
Norm. EPS growth (%)	10.1	199.4	31.5	17.5
Norm. P/E (x)	57.8	19.3	14.7	12.5
EV/EBITDA (x)	29.5	13.1	9.8	8.4
Price/book (x)	7.6	5.3	4.3	3.6
Dividend yield (%)	0.7	2.5	3.4	4.0
ROE (%)	11.5	31.9	32.2	31.3
Net debt/equity (%)	net cash	net cash	net cash	net cash
Earnings revisions				
Previous norm. net profit		3,174	4,127	4,854
Change from previous (%)		8.3	13.5	13.4
Previous norm. EPS (HK$)		0.61	0.77	0.90

Source: Company, Nomura estimates

Share price relative to MSCI China



	1m	3m	6m
Absolute (HK$)	6.8	(0.9)	74.9
Absolute (US$)	6.9	(1.2)	74.3
Relative to Index	5.4	2.7	72.0
Market cap (US$mn)			8,996
Estimated free float (%)			25.0
52-week range (HK$)			14.98/4.15
3-mth avg daily turnover (US$mn)			31.24
Stock borrowability			Easy
Major shareholders (%)			
STDM			61.0
Stanley Ho			8.0

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

We continue to derive our revised price target of HK$15.50 (up from HK$15.00) using a sum-of-the parts valuation, but we have adjusted down our valuation multiple from 14x to 12x for Grand Lisboa and the Oceanus. We had applied our previous target multiple of 14x to reflect the two properties' high exposure to the mass market segment, which we believe is more defensive and presents better growth prospects. However, until concerns over the family dispute ease and investors fully regain confidence in the stock, the market is unlikely to pay a premium for SJM, in our view. Thus, we apply 12x to value all lines of business, which is at the low end of the industry's average range:

- All casino businesses, including flagship property Grand Lisboa, the legacy casinos and the mass market-focused Oceanus, at 12x FY11F EBITDA (at the low end of the industry's average range); and
- Hotel and other income unchanged at 12x and 5x FY11F EBITDA, respectively.

Exhibit 25. SJM Holdings: NEW valuation summary

Division	Valuation methodology	FY11E NAV (HK$mn)	Per share (HK$)
Gaming			
Grand Lisboa	12x FY11F EBITDA	33,615	6.26
Legacy casinos	12x FY11F EBITDA	30,800	5.73
Oceanus	12x FY11F EBITDA	5,716	1.06
Hospitality			
Grand Lisboa	12x FY11F EBITDA	1,556	0.29
Other corporate income	5x FY11F EBITDA	309	0.06
Gross Asset Value		71,995	13.40
Add: net cash	FY11F year-end forecast	11,289	2.10
Target valuation end-FY11		**83,284**	**15.50**

Source: Nomura estimates

Exhibit 26. SJM Holdings: OLD valuation summary

Division	Valuation methodology	FY11F NAV (HK$mn)	Per share (HK$)
Gaming			
Grand Lisboa	14x FY11F EBITDA	35,466	6.60
Legacy casinos	12x FY11F EBITDA	28,772	5.35
Oceanus	14x FY11F EBITDA	5,404	1.01
Hospitality			
Grand Lisboa	12x FY11F EBITDA	842	0.16
Other corporate income	5x FY11F EBITDA	309	0.06
Gross Asset Value		70,793	13.17
Add: net cash	FY11F year-end forecast	9,826	1.83
Target valuation end-FY11		**80,619**	**15.00**

Source: Nomura estimates

Investment risks

Potential downside risks include: 1) regulatory change in China that could harm the gaming industry; 2) underperformance of the Oceanus casino; 3) weaker-than-expected performance for its legacy casinos; and 4) uncertainty over the health of the company's chairman, Dr Stanley Ho, as well as a new round of family dispute.

Financial statement analysis

Earnings revisions

After factoring in our new market share and gaming revenue assumptions, we have increased our EBITDA forecasts for SJM.

Below we summarise the changes to our assumptions.

Exhibit 27. SJM Holdings: earnings revisions

Operating assumptions

	Group gaming revenue			VIP segment			Mass segment		
	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F
Old									
Revenue (HK$mn)	55,713	66,063	73,362	37,469	44,303	49,119	17,326	20,938	23,497
Market share (%)	32	32	31	29	30	28	41	40	38
New									
Revenue (HK$mn)	**56,984**	**72,644**	**83,324**	**38,683**	**50,093**	**57,506**	**17,382**	**21,728**	**25,071**
Market share (%)	**32**	**32**	**31**	**29**	**30**	**29**	**41**	**39**	**38**

Financial assumptions

	EPS (HK$)			EBITDA (HK$mn)			EBITDA margin (%)		
Old	0.61	0.77	0.90	4,589	5,449	6,068	8.2	8.2	8.2
New	**0.66**	**0.87**	**1.02**	**4,851**	**6,036**	**6,926**	**8.4**	**8.3**	**8.3**
Change	0.05	0.10	0.12	262.4	586.7	858.2	0.3	0.1	0.0
Change (%)	8.3	13.5	13.4	5.7	10.8	14.1	3.3	0.7	0.5

Note: Group gaming revenue includes revenue from slots, which is not broken down separately

Source: Nomura estimates

Financial statements

Income statement (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Revenue	28,211	34,408	57,468	73,138	83,821
Cost of goods sold					
Gross profit	**28,211**	**34,408**	**57,468**	**73,138**	**83,821**
SG&A	(27,398)	(33,245)	(53,919)	(68,465)	(78,456)
Employee share expense					
Operating profit	**814**	**1,163**	**3,548**	**4,673**	**5,364**
EBITDA	**1,600**	**2,318**	**4,851**	**6,036**	**6,926**
Depreciation	(769)	(1,109)	(1,289)	(1,350)	(1,549)
Amortisation	(18)	(46)	(13)	(13)	(12)
EBIT	**814**	**1,163**	**3,548**	**4,673**	**5,364**
Net interest expense	(75)	(147)	(71)	51	180
Associates & JCEs	5	(8)	-	-	-
Other income	2	4	0	0	0
Earnings before tax	**745**	**1,012**	**3,477**	**4,724**	**5,544**
Income tax	(17)	(18)	(20)	(20)	(20)
Net profit after tax	**729**	**995**	**3,457**	**4,704**	**5,524**
Minority interests	141	112	(20)	(20)	(20)
Other items					
Preferred dividends					
Normalised NPAT	**869**	**1,106**	**3,437**	**4,684**	**5,504**
Extraordinary items	(74)	(201)	(10)	(10)	(10)
Reported NPAT	**796**	**906**	**3,427**	**4,674**	**5,494**
Dividends	(3,800)	(450)	(1,713)	(2,337)	(2,747)
Transfer to reserves	**(3,004)**	**456**	**1,713**	**2,337**	**2,747**
Valuation and ratio analysis					
FD normalised P/E (x)	63.7	57.8	19.3	14.7	12.5
FD normalised P/E at price target (x)	77.1	70.0	23.4	17.8	15.1
Reported P/E (x)	69.6	70.6	19.4	14.7	12.5
Dividend yield (%)	5.9	0.7	2.5	3.4	4.0
Price/cashflow (x)	88.9	15.8	16.3	9.8	10.5
Price/book (x)	8.8	7.6	5.3	4.3	3.6
EV/EBITDA (x)	43.9	29.5	13.1	9.8	8.4
EV/EBIT (x)	86.1	59.1	17.9	12.7	10.9
Gross margin (%)	100.0	100.0	100.0	100.0	100.0
EBITDA margin (%)	5.7	6.7	8.4	8.3	8.3
EBIT margin (%)	2.9	3.4	6.2	6.4	6.4
Net margin (%)	2.8	2.6	6.0	6.4	6.6
Effective tax rate (%)	2.2	1.7	0.6	0.4	0.4
Dividend payout (%)	477.7	49.7	50.0	50.0	50.0
Capex to sales (%)	7.0	3.9	1.0	1.3	3.9
Capex to depreciation (x)	2.6	1.2	0.5	0.7	2.1
ROE (%)	11.7	11.5	31.9	32.2	31.3
ROA (pretax %)	6.7	8.4	25.1	34.1	37.1
Growth (%)					
Revenue	(12.5)	22.0	67.0	27.3	14.6
EBITDA	(19.6)	44.9	109.3	24.4	14.7
EBIT	(42.1)	42.9	205.1	31.7	14.8
Normalised EPS	(50.7)	10.1	199.4	31.5	17.5
Normalised FDEPS	(50.7)	10.1	199.4	31.5	17.5
Per share					
Reported EPS (HK$)	0.18	0.18	0.66	0.87	1.02
Norm EPS (HK$)	0.20	0.22	0.66	0.87	1.02
Fully diluted norm EPS (HK$)	0.20	0.22	0.66	0.87	1.02
Book value per share (HK$)	1.46	1.69	2.42	2.97	3.56
DPS (HK$)	0.76	0.09	0.32	0.43	0.51

Source: Nomura estimates

We expect 24% EBITDA growth in FY11F

Cashflow (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	1,600	2,318	4,851	6,036	6,926
Change in working capital	(1,542)	1,458	(668)	982	(489)
Other operating cashflow	564	286	(115)	8	137
Cashflow from operations	**623**	**4,063**	**4,068**	**7,026**	**6,574**
Capital expenditure	(1,978)	(1,344)	(600)	(950)	(3,250)
Free cashflow	**(1,355)**	**2,719**	**3,468**	**6,076**	**3,324**
Reduction in investments	(11)	(8)	(7)	(7)	(7)
Net acquisitions					
Reduction in other LT assets	(207)	80	(31)	(33)	(34)
Addition in other LT liabilities	265	184	40	42	45
Adjustments	(226)	(2,773)	(2)	(3)	(3)
Cashflow after investing acts	**(1,534)**	**201**	**3,468**	**6,076**	**3,324**
Cash dividends	(3,500)	(300)	(450)	(1,713)	(2,337)
Equity issue	3,850	-	-	-	-
Debt issue	936	(702)	(940)	(840)	(1,350)
Convertible debt issue					
Others	(442)	3,891	-	-	-
Cashflow from financial acts	**844**	**2,889**	**(1,390)**	**(2,553)**	**(3,687)**
Net cashflow	**(690)**	**3,090**	**2,078**	**3,522**	**(363)**
Beginning cash	6,538	5,847	8,937	11,015	14,537
Ending cash	5,847	8,937	11,015	14,537	14,174
Ending net debt	362	(1,878)	(6,500)	(10,878)	(11,880)

Source: Nomura estimates

SJM has the strongest balance sheet among the six operators

Balance sheet (HK$mn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	5,847	8,937	11,015	14,537	14,174
Marketable securities					
Accounts receivable	930	1,233	1,295	1,284	1,360
Inventories					
Other current assets	525	1,092	1,134	1,177	1,223
Total current assets	**7,302**	**11,263**	**13,443**	**16,998**	**16,757**
LT investments	127	135	142	149	156
Fixed assets	10,422	10,985	10,287	9,879	11,572
Goodwill	52	46	41	36	32
Other intangible assets					
Other LT assets	1,017	938	969	1,002	1,036
Total assets	**18,921**	**23,367**	**24,882**	**28,065**	**29,553**
Short-term debt	1,020	1,040	1,040	1,550	537
Accounts payable	4,583	6,895	6,343	7,358	6,990
Other current liabilities	69	85	72	72	72
Total current liabilities	**5,671**	**8,020**	**7,456**	**8,981**	**7,600**
Long-term debt	5,189	6,019	3,475	2,109	1,757
Convertible debt					
Other LT liabilities	624	807	848	890	935
Total liabilities	**11,484**	**14,847**	**11,778**	**11,980**	**10,291**
Minority interest	149	65	85	105	125
Preferred stock					
Common stock	5,000	5,000	5,374	5,374	5,374
Retained earnings					
Proposed dividends					
Other equity and reserves	2,287	3,455	7,646	10,607	13,763
Total shareholders' equity	**7,287**	**8,455**	**13,020**	**15,980**	**19,137**
Total equity & liabilities	**18,921**	**23,367**	**24,882**	**28,065**	**29,553**
Liquidity (x)					
Current ratio	1.29	1.40	1.80	1.89	2.20
Interest cover	10.8	7.9	49.7	na	na
Leverage					
Net debt/EBITDA (x)	0.23	net cash	net cash	net cash	net cash
Net debt/equity (%)	5.0	net cash	net cash	net cash	net cash
Activity (days)					
Days receivable	11.2	11.5	8.0	6.4	5.8
Days inventory	na	na	na	na	na
Days payable	na	na	na	na	na
Cash cycle	na	na	na	na	na

Source: Nomura estimates

Wynn Macau 1128 HK

GAMING, HOTELS & LEISURE | CHINA

Maintained

NEUTRAL

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Action

Wynn continues to differentiate itself via its premium brand, unique product and service plus management quality. But given its strong stock performance, a high expectation for growth may already be priced in. A potential revenue slowdown (which could be attributed to credit tightening) may have an unparalleled impact on it, especially when Wynn is perceived as the prime VIP play. Higher valuation may also cap stock performance in the short run. We up our PT to HK$23, on higher valuation multiple and earnings estimate but maintain our NEUTRAL rating.

Catalysts

Potential approval on the land concession and updated plans of their Cotai project, due to open in 2015, could be near-term catalysts.

Anchor themes

We favour stocks with resilient qualities in a downturn, as an expectation gap has introduced higher downside risk.

Closing price on 11 Mar	HK$21.00
Price target	HK$23.50
	(from HK$17.00)
Upside/downside	11.9%
Difference from consensus	3.3%
FY11F net profit (HK$mn)	5,890
Difference from consensus	4.2%

Source: Nomura

Nomura vs consensus

Our earnings estimates are almost in line with consensus.

Await better timing and valuation

① Another triumph amid strong competition

Once more, Wynn delivered solid strong market share and returns amid keen competition and the risk of a commission hike. Again, it differentiated itself by its superior brand, luxury positioning and prime location. It has proven that its product is indeed unique, which has allowed it to defend its business and profitability over time. Our initial concern on potential market share loss in 4Q10 was overdone.

② Stock performance could be capped

We continue to like Wynn but reckon that given its strong share price, strong growth expectation may already be priced in. Thus, any sign of a slowdown (be it seasonal or structural) may impact it more than others, especially when the market attributes the slowdown to credit tightening. Wynn is perceived as a VIP-play despite mass market / slots and non-gaming accounting for over 50% of its EBITDA and its premium mass enjoying solid growth. Also, rich valuation of 15x FY11F EBITDA, trading a premium to peers, could cap performance in the short run. We prefer Sands China (1928 HK, HK$17.02, BUY) — a laggard play with defensive mass earnings.

③ Outstanding 4Q10; expect solid 1Q11

For 4Q10, EBITDA was at US$297mn, 17% ahead of consensus, due to: 1) strong VIP volume and high win; 2) growth from premium mass market; and 3) margin expansion from better operating efficiency. We expect 1Q11 to remain strong on further growth in premium mass.

④ Valuation and risk

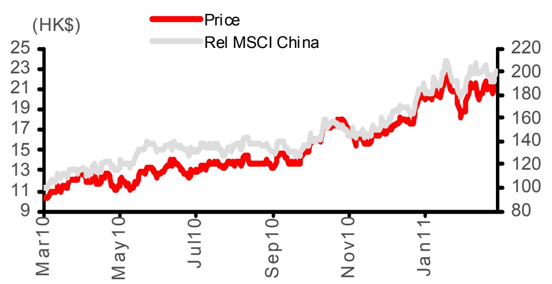
We use the same methodology but have increased our valuation multiple to reflect Wynn's superior earning/cash-generation ability. Upside: 1) market share coming in stronger than expected; 2) faster-than-expected progress on Cotai. Downside: 1) regulatory changes; 2) stronger-than-expected demand for the Cotai resort.

Key financials & valuations

31 Dec (HK$mn)	FY09F	FY10F	FY11F	FY12F
Revenue	14,077	22,364	27,511	30,471
Reported net profit	2,069	4,507	5,890	6,790
Normalised net profit	2,097	4,517	5,900	6,801
Normalised EPS (HK$)	0.40	0.87	1.14	1.31
Norm. EPS growth (%)	na	115.4	30.6	15.3
Norm. P/E (x)	51.9	24.1	18.5	16.0
EV/EBITDA (x)	34.8	19.0	14.9	13.2
Price/book (x)	28.9	25.1	12.9	8.2
Dividend yield (%)	0.0	0.0	0.0	0.0
ROE (%)	91.8	111.2	92.1	62.7
Net debt/equity (%)	73.9	68.8	28.3	8.4
Earnings revisions				
Previous norm. net profit		3,864	4,463	5,147
Change from previous (%)		16.9	32.2	32.1
Previous norm. EPS (HK$)		0.74	0.86	0.99

Source: Company, Nomura estimates

Share price relative to MSCI China



	1m	3m	6m
Absolute (HK$)	13.1	27.9	59.6
Absolute (US$)	13.2	27.6	59.1
Relative to Index	9.0	29.0	54.0
Market cap (US$mn)			13,981
Estimated free float (%)			25.0
52-week range (HK$)			22.25/10.10
3-mth avg daily turnover (US$mn)			18.13
Stock borrowability			Easy
Major shareholders (%)			
Wynn Resorts Limited			75.0

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

From 14.5x, we increase our valuation multiple to 16x, as we believe its earnings quality, future growth potential and optimally leveraged balance sheet deserve a premium compared to its peers. We have not changed our valuation methodology.

We added Wynn Cotai to our valuation in anticipation of land concession approval, which could come as early as year-end 2010. That piece is valued based on capex expected to be capitalised by end-2011.

Exhibit 28. NEW WM sum-of-the-parts valuation

Divisions	Valuation methodology	FY11F NAV (HK$mn)	Per share (HK$)
Gaming			
Wynn Macau	14.5x FY11F EBITDA	65,144	12.6
Wynn Cotai	Capitalised Capex on the project by end-2011	3,900	0.8
Hospitality			
Wynn Macau	14.5x FY11F EBITDA	22,247	4.3
Gross Asset Value		87,391	17.6
less net debt	FY11F year-end forecast	(3,079)	(0.6)
Target valuation by end-FY11F		**88,212**	**17.00**

Source: Nomura estimates

Exhibit 29. OLD WM sum-of-the-parts valuation

Divisions	Valuation methodology	FY11F NAV (HK$mn)	Per share (HK$)
Gaming			
Wynn Macau	16x FY11F EBITDA	92,906	17.9
Wynn Cotai	Capitalised capex on the project by end-2011	4,875	0.9
Hospitality			
Wynn Macau	16x FY11F EBITDA	26,514	5.1
Gross Asset Value		124,296	24.0
less net debt	FY11F year-end forecast	(2,394)	(0.5)
Target valuation by end-FY11F		**121,901**	**23.50**

Source: Nomura estimates

Investment risks

Potential upside includes: 1) stronger-than-expected market share, especially for VIP; 2) faster-than-expected progress on Wynn Cotai project. Potential downside risks to our call include: 1) any regulatory changes in China that could harm the gaming industry; 2) underperformance of the Wynn Encore casino; 3) a resumption of the commission war in the VIP business; and 4) demand in Cotai grows faster than expected.

Financial statement analysis

Earnings revisions

After factoring in our new market share and gaming revenue assumptions, we have increased our EBITDA forecasts for Wynn Macau. Here are two points worth noting:

- **Market share:** 4Q10 results surprised us on the upside, in particular in Wynn's ability to guard its business amid keener competition; therefore, we have adjusted Wynn's overall market share to reflect the company's ability to generate earnings.
- **Margin:** Margin was up to reflect robust growth from the premium mass market segment, which accounts for an increasing portion of earnings pulling up the margin.

Below we summarise the changes to our assumptions:

Exhibit 30. Wynn Macau: earnings estimate revisions

	Group gaming revenue			VIP segment			Mass segment		
	FY10	FY11F	FY12F	FY10	FY11F	FY12F	FY10	FY11F	FY12F
Operating assumptions									
Old									
Revenue (HK$mn)	25,816	30,037	34,009	20,012	23,043	26,314	4,154	5,197	5,719
Market share (%)	14.2	14.0	13.4	15.6	15.5	15.0	9.9	9.8	9.0
New									
Revenue (HK$mn)	**27,480**	**34,408**	**38,484**	**21,385**	**26,829**	**30,056**	**4,405**	**5,763**	**6,431**
Market share (%)	**14.7**	**14.4**	**13.6**	**16.1**	**15.8**	**15.0**	**10.3**	**10.2**	**9.5**
Financial assumptions									
	EPS (US$)			EBITDA (US$mn)			EBITDA margin (%)		
	FY10	FY11F	FY12F	FY10	FY11F	FY12F	FY10	FY11F	FY12F
Old	0.74	0.86	0.99	5,237	6,027	6,664	22.2	22.0	21.8
New	**0.87**	**1.14**	**1.31**	**5,890**	**7,464**	**8,318**	**23.2**	**23.6**	**23.6**
Change	0.13	0.28	0.32	653.5	1,436.8	1,653.2	1.0	1.5	1.8
Change (%)	17	32	32	12	24	25	4	7	8

Note: Group gaming revenue also includes revenue from slots, which is not broken down separately.

Source: Nomura estimates

Financial statements

Income statement (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09F**	**FY10F**	**FY11F**	**FY12F**
Revenue	14,711	14,077	22,364	27,511	30,471
Cost of goods sold					
Gross profit	**14,711**	**14,077**	**22,364**	**27,511**	**30,471**
SG&A	(12,269)	(11,587)	(17,469)	(21,342)	(23,476)
Employee share expense					
Operating profit	**2,442**	**2,490**	**4,894**	**6,169**	**6,995**
EBITDA	**3,138**	**3,209**	**5,890**	**7,464**	**8,318**
Depreciation	(697)	(718)	(996)	(1,295)	(1,323)
Amortisation					
EBIT	**2,442**	**2,490**	**4,894**	**6,169**	**6,995**
Net interest expense	(226)	(312)	(302)	(189)	(115)
Associates & JCEs					
Other income	(114)	(76)	(60)	(60)	(60)
Earnings before tax	**2,102**	**2,103**	**4,532**	**5,920**	**6,821**
Income tax	57	(6)	(15)	(20)	(20)
Net profit after tax	**2,159**	**2,097**	**4,517**	**5,900**	**6,801**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**2,159**	**2,097**	**4,517**	**5,900**	**6,801**
Extraordinary items	(120)	(29)	(10)	(10)	(10)
Reported NPAT	**2,040**	**2,069**	**4,507**	**5,890**	**6,790**
Dividends					
Transfer to reserves	**2,040**	**2,069**	**4,507**	**5,890**	**6,790**
Valuation and ratio analysis					
FD normalised P/E (x)	na	51.9	24.1	18.5	16.0
FD normalised P/E at price target (x)	na	58.1	27.0	20.7	17.9
Reported P/E (x)	na	52.7	24.2	18.5	16.0
Dividend yield (%)	-	-	-	-	-
Price/cashflow (x)	na	24.1	17.7	14.1	12.7
Price/book (x)	147.7	28.9	25.1	12.9	8.2
EV/EBITDA (x)	36.4	34.8	19.0	14.9	13.2
EV/EBIT (x)	46.8	44.9	22.9	18.0	15.7
Gross margin (%)	100.0	100.0	100.0	100.0	100.0
EBITDA margin (%)	21.3	22.8	26.3	27.1	27.3
EBIT margin (%)	16.6	17.7	21.9	22.4	23.0
Net margin (%)	13.9	14.7	20.2	21.4	22.3
Effective tax rate (%)	(2.7)	0.3	0.3	0.3	0.3
Dividend payout (%)	-	-	-	-	-
Capex to sales (%)	10.5	15.4	9.4	18.7	16.9
Capex to depreciation (x)	2.2	3.0	2.1	4.0	3.9
ROE (%)	52.9	91.8	111.2	92.1	62.7
ROA (pretax %)	29.3	26.2	44.8	45.9	40.4
Growth (%)					
Revenue	35.5	(4.3)	58.9	23.0	10.8
EBITDA	28.1	2.2	83.6	26.7	11.4
EBIT	24.3	2.0	96.5	26.0	13.4
Normalised EPS	na	na	115.4	30.6	15.3
Normalised FDEPS	na	na	115.4	30.6	15.3
Per share					
Reported EPS (HK$)	na	0.40	0.87	1.14	1.31
Norm EPS (HK$)	na	0.40	0.87	1.14	1.31
Fully diluted norm EPS (HK$)	na	0.40	0.87	1.14	1.31
Book value per share (HK$)	0.14	0.73	0.84	1.63	2.55
DPS (HK$)	-	-	-	-	-

Source: Nomura estimates

Cashflow (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09F**	**FY10F**	**FY11F**	**FY12F**
EBITDA	3,138	3,209	5,890	7,464	8,318
Change in working capital	(142)	1,219	338	318	349
Other operating cashflow	174	89	(72)	(77)	(76)
Cashflow from operations	**3,170**	**4,517**	**6,155**	**7,705**	**8,590**
Capital expenditure	(1,546)	(2,167)	(2,108)	(5,155)	(5,155)
Free cashflow	**1,624**	**2,351**	**4,048**	**2,550**	**3,435**
Reduction in investments	-	-	-	-	-
Net acquisitions					
Reduction in other LT assets	(1)	(29)	-	-	-
Addition in other LT liabilities	100	(11)	13	13	14
Adjustments	(73)	(12,752)	(7)	23	34
Cashflow after investing acts	**1,650**	**(10,441)**	**4,054**	**2,586**	**3,483**
Cash dividends	(8,320)	(1,009)	(3,943)	(1,770)	(2,040)
Equity issue		14,490	-	-	-
Debt issue	3,900	0	(620)	(3,527)	386
Convertible debt issue					
Others	(219)	(355)	(308)	(225)	(163)
Cashflow from financial acts	**(4,639)**	**13,126**	**(4,871)**	**(5,522)**	**(1,817)**
Net cashflow	**(2,989)**	**2,685**	**(818)**	**(2,936)**	**1,666**
Beginning cash	5,534	2,544	5,229	4,412	1,475
Ending cash	2,544	5,229	4,411	1,475	3,142
Ending net debt	5,429	2,788	2,985	2,394	1,114

Source: Nomura estimates

Balance sheet (HK$mn)					
As at 31 Dec	**FY08**	**FY09F**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	2,544	5,229	4,412	1,475	3,142
Marketable securities					
Accounts receivable	208	325	342	359	377
Inventories	199	203	207	211	215
Other current assets	166	161	164	167	171
Total current assets	**3,118**	**5,918**	**5,124**	**2,212**	**3,904**
LT investments					
Fixed assets	7,419	8,992	10,104	13,964	17,797
Goodwill	398	398	398	398	398
Other intangible assets					
Other LT assets	255	283	283	283	283
Total assets	**11,190**	**15,592**	**15,909**	**16,858**	**22,382**
Short-term debt					
Accounts payable	2,059	3,348	3,699	4,030	4,393
Other current liabilities	158	205	215	226	237
Total current liabilities	**2,218**	**3,553**	**3,914**	**4,256**	**4,631**
Long-term debt	7,973	8,017	7,396	3,870	4,255
Convertible debt					
Other LT liabilities	262	251	263	276	290
Total liabilities	**10,452**	**11,821**	**11,573**	**8,402**	**9,176**
Minority interest					
Preferred stock					
Common stock	-	5	5	5	5
Retained earnings	29	1,842	2,407	6,527	11,277
Proposed dividends					
Other equity and reserves	709	1,924	1,924	1,924	1,924
Total shareholders' equity	**738**	**3,771**	**4,336**	**8,455**	**13,206**
Total equity & liabilities	**11,190**	**15,592**	**15,909**	**16,858**	**22,382**
Liquidity (x)					
Current ratio	1.41	1.67	1.31	0.52	0.84
Interest cover	10.8	8.0	16.2	32.6	61.1
Leverage					
Net debt/EBITDA (x)	1.73	0.87	0.51	0.32	0.13
Net debt/equity (%)	736.1	73.9	68.8	28.3	8.4
Activity (days)					
Days receivable	6.8	6.9	5.4	4.6	4.4
Days inventory	na	na	na	na	na
Days payable	na	na	na	na	na
Cash cycle	na	na	na	na	na

Source: Nomura estimates

Melco Crown Entertainment MPEL US

GAMING, HOTELS & LEISURE | CHINA

Maintained

REDUCE

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Action

We remain cautious on MPEL, given: 1) the initiative to increase direct VIP business, which may bring credit risk; 2) the potential impact from the opening of Galaxy Macau on City of Dreams, which may pressure its mass market share; and 3) EBITDA, which remains VIP-driven, thus volatile. Trading at 11x FY11F EBITDA, the name is among the least expensive in the sector, but we consider a re-rating unlikely in the short term, given the strong YTD rally and the above-mentioned concerns. Still a REDUCE, on a revised PT of US$6.90.

Catalysts

Inexpensive valuation should provide support and further steady improvement in mass-market share would help the stock re-rate.

Anchor themes

We favour stocks with resilient qualities in a downturn, given that the expectation gap has introduced higher downside risk.

Closing price on 11 Mar	US$7.35
Price target	**US$6.90**
	(from US$5.70)
Upside/downside	-6.1%
Difference from consensus	-23.3%
FY11F net profit (US$mn)	17.51
Difference from consensus	-86.5%

Source: Nomura

Nomura vs consensus

Our estimates are well below market forecasts, likely due to our more prudent estimates on interest costs. Property EBITDA estimates are largely in line.

Short-term whirlwind

① We remain cautious

We remain cautious on MPEL, given: 1) increased direct VIP business (to 20% of total roll in 4Q10), which spells greater credit risk and risk of jeopardising operator-junket relations from chasing the same customers; 2) the potential negative impact from the opening of Galaxy Macau, especially on mass market business where target customers are similar (ie, those who pick Cotai over Peninsular Macau tend both not to be hard-core gamblers); and 3) VIP skewed EBITDA is likely to bring earnings volatility from win rates.

② Valuation support = limited downside

Trading at 11x FY11F EV/EBTIDA, the stock's valuation is among the least expensive in the industry, helping provide valuation support, especially amid strong industry growth, where the seasonally weaker month of February also delivered record gaming revenue of close to MOP20bn. However, within the Macau universe, we prefer Galaxy (with catalyst), Sands China (resilient earnings and cashflow) and SJM (cheapest valuation) over MPEL, where we see more negative than positive news flow in the pipeline.

③ 4Q10 results in line

MPEL reported flat q-q 4Q10 adjusted EBITDA of US$134mn, in line with street estimates. VIP turnover and mass-market drop grew by 12% q-q and 14% q-q, respectively. Management efforts continued to pay-off amid favourable supply-demand dynamics last year.

④ Valuation and investment risks

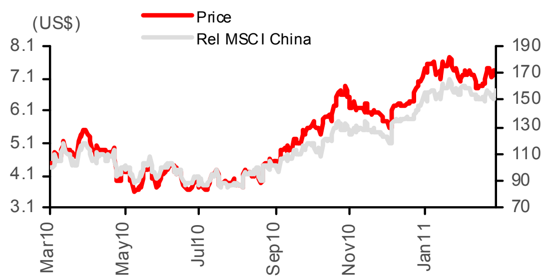
We continue to use SOTP valuation. Upside risks: 1) better-than-expected performance of the CoD; 2) further delays in other casino projects, which would limit competition. Downside risks: 1) stronger-than-expected impact from the Galaxy Macau opening; and 2) default risk from increased direct VIP business.

Key financials & valuations

31 Dec (US$mn)	FY09	FY10F	FY11F	FY12F
Revenue	1,333	2,642	2,919	3,061
Reported net profit	(301.4)	(11.1)	17.5	72.4
Normalised net profit	(293.0)	(7.6)	16.3	70.5
Normalised EPS (US$)	(0.200)	(0.005)	0.010	0.044
Norm. EPS growth (%)	na	na	na	332.4
Norm. P/E (x)	na	na	719.1	166.3
EV/EBITDA (x)	94.3	12.2	10.6	9.3
Price/book (x)	1.6	1.6	1.6	1.5
Dividend yield (%)	0.0	0.0	0.0	0.0
ROE (%)	(12.3)	(0.4)	0.7	2.8
Net debt/equity (%)	53.8	54.2	52.8	41.2
Earnings revisions				
Previous norm. net profit		(50.4)	(64.0)	(34.9)
Change from previous (%)		(84.9)	(125.5)	(301.8)
Previous norm. EPS (US$)		(0.032)	(0.040)	(0.022)

Source: Company, Nomura estimates

Share price relative to MSCI China



	1m	3m	6m
Absolute (US$)	2.4	27.4	62.3
Absolute (US$)	2.4	27.4	62.3
Relative to Index	(1.8)	28.5	56.9
Market cap (US$mn)			3,909
Estimated free float (%)			26.8
52-week range (US$)			7.76/3.56
3-mth avg daily turnover (US$mn)			43.41
Stock borrowability			Easy
Major shareholders (%)			
Melco Leisure & Entertainment Group Ltd			33.8
Crown Limited			33.8

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

Our revised 12-month price target of US$6.90 (up from US$5.70) is based on sum-of-the-parts (SOTP) valuation, including: 1) the CoD at 10x FY11F EBTIDA; 2) the Alitra at 10x FY11F EBITDA; 3) Mocha Clubs at 8x FY11F EBITDA; and 4) hotel rooms at 10x FY11 EBITDA. The multiple assumptions are below the industry average range of 12-14x because we think the company has poorer EBITDA quality than that of its competitors. EBITDA tends to mimics cashflow and with interest expenses remaining high due to a re-financing exercise earlier this year, the free cashflow for the company remains low, especially versus other operators'. This has lowered the company's EBITDA quality, thus we continue to keep lower multiples for our valuation.

The upward revision to our price target mainly reflects improved EBITDA forecasts, which come on our expectations of stronger overall sector growth and a successful business turnaround.

Exhibit 31. MPEL: New sum-of-the-parts valuation

Division	Valuation methodology	FY11F NAV (US$mn)	Per ADR (US$)
Gaming			
Altira	10x FY11F EBITDA	1,325	2.49
Mocha Clubs	8x FY11F EBITDA	221	0.42
City of Dream	10x FY11F EBITDA	3,155	5.93
Hospitality			
Altira & COD	10x FY11F EBITDA	843	1.58
Less: corporate expense	10x FY11F EBITDA	(661)	(1.24)
Gross Asset Value		4,882	9.18
less net (debt)/cash	FY11F year-end forecast	(1,212)	(2.28)
Target valuation end-FY11		**3,670**	**6.90**

Source: Nomura estimates

Exhibit 32. MPEL: Old sum-of-the-parts valuation

Division	Valuation methodology	FY11F NAV (US$mn)	Per ADR (US$)
Gaming			
Altira	10x FY11F EBITDA	1,068	2.01
Mocha Clubs	8x FY11F EBITDA	227	0.43
City of Dream	10x FY11F EBITDA	2,457	4.62
Hospitality			
Altira & COD	10x FY11F EBITDA	1,134	2.13
Less: corporate expense	10x FY11F EBITDA	(678)	(1.27)
Gross Asset Value		4,208	7.91
less net (debt)/cash	FY11E year-end forecast	(1,175)	(2.21)
Target valuation end-FY11		**3,033**	**5.70**

Source: Nomura estimates

Investment risks

Upside risks to our call include: 1) better-than-expected performance of the CoD; 2) strong VIP business growth; and 3) further delays in other casino projects in Macau, which would limit upcoming supply in 2011F.

Downside risks would include: 1) regulatory changes in China that could hinder growth; 2) stronger-than-expected impact from cooling measures in China's property market, which could drag VIP growth; 3) a resumed commission war on the VIP business; and 4) weaker-than-expected performance of the CoD and other lines of businesses.

Financial statement analysis

Earnings revisions

After factoring in our new market share and gaming revenue assumptions, we have increased our EBITDA forecasts for MPEL. Below we summarise the changes to our assumptions to reflect stronger overall sector growth and a successful turnaround of its businesses.

Although we have not seen much positive impact from the House of Dancing Water on mass market share at the City of Dreams (CoD), we revise up the mass market share for the CoD slightly in 2011F, to factor in the positive response we gathered from the show and the show's potential to increase traffic at the property this year.

Exhibit 33. Melco Crown: earnings revisions

Operating assumptions

	Group gaming revenue			VIP segment			Mass segment		
	FY10E	FY11F	FY12F	FY10F	FY11F	FY12F	FY10E	FY11F	FY12F
Old									
Revenue (US$mn)	3,257	3,519	3,672	2,664	2,859	2,924	483	556	643
Market share (%)	14	13	12	16	15	13	9	8	8
New									
Revenue (US$mn)	**3,338**	**4,012**	**4,222**	**2,717**	**3,287**	**3,468**	**509**	**614**	**643**
Market share (%)	**14**	**13**	**12**	**16**	**15**	**14**	**9**	**9**	**8**

Financial assumptions

	EPS (US$)			EBITDA (US$mn)			EBITDA margin* (%)		
Old	(0.03)	(0.04)	(0)	387	426	442	11	11	11
New	**(0.01)**	**0.01**	**0.05**	**430**	**494**	**535**	**12**	**12**	**12**
Change	0.03	0.05	0.07	43	67	93	1	0	1
Change (%)	(79)	(128)	(321)	11	16	21	9	3	6

Note: Group gaming revenue includes revenue from slots, which is not broken down separately; * for EBITDA margins, we use gross revenue, unlike NEMO figures which use net revenue

Source: Nomura estimates

Financial statements

Income statement (US$mn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Revenue	1,416	1,333	2,642	2,919	3,061
Cost of goods sold					
Gross profit	**1,416**	**1,333**	**2,642**	**2,919**	**3,061**
SG&A	(1,386)	(1,495)	(2,528)	(2,767)	(2,875)
Employee share expense					
Operating profit	**30**	**(162)**	**114**	**152**	**186**
EBITDA	**157**	**56**	**430**	**494**	**535**
Depreciation	(51)	(142)	(240)	(266)	(274)
Amortisation	(76)	(76)	(76)	(76)	(76)
EBIT	**30**	**(162)**	**114**	**152**	**186**
Net interest expense	(8)	(40)	(100)	(142)	(121)
Associates & JCEs					
Other income	(20)	(92)	(21)	1	0
Earnings before tax	**2**	**(293)**	**(8)**	**11**	**66**
Income tax	1	0	0	5	5
Net profit after tax	**4**	**(293)**	**(8)**	**16**	**71**
Minority interests	-	-	-	-	-
Other items					
Preferred dividends					
Normalised NPAT	**4**	**(293)**	**(8)**	**16**	**71**
Extraordinary items	(6)	(8)	(4)	1	2
Reported NPAT	**(2)**	**(301)**	**(11)**	**18**	**72**
Dividends					
Transfer to reserves	**(2)**	**(301)**	**(11)**	**18**	**72**
Valuation and ratio analysis					
FD normalised P/E (x)	2,727.6	na	na	719.1	166.3
FD normalised P/E at price target (x)	2,560.7	na	na	675.1	156.1
Reported P/E (x)	na	na	na	669.8	162.0
Dividend yield (%)	-	-	-	-	-
Price/cashflow (x)	na	na	78.0	80.3	36.2
Price/book (x)	1.34	1.56	1.56	1.55	1.51
EV/EBITDA (x)	29.1	94.3	12.2	10.6	9.3
EV/EBIT (x)	152.9	na	46.2	34.4	26.7
Gross margin (%)	100.0	100.0	100.0	100.0	100.0
EBITDA margin (%)	11.1	4.2	16.3	16.9	17.5
EBIT margin (%)	2.1	(12.1)	4.3	5.2	6.1
Net margin (%)	(0.2)	(22.6)	(0.4)	0.6	2.4
Effective tax rate (%)	(70.3)	na	na	(44.2)	(7.6)
Dividend payout (%)	na	na	na	-	-
Capex to sales (%)	74.3	69.1	8.5	4.3	2.1
Capex to depreciation (x)	20.5	6.5	0.9	0.5	0.2
ROE (%)	(0.1)	(12.3)	(0.4)	0.7	2.8
ROA (pretax %)	1.0	(4.0)	2.6	3.4	4.3
Growth (%)					
Revenue	295.0	(5.9)	98.2	10.5	4.9
EBITDA	na	(64.4)	670.6	14.9	8.4
EBIT	na	(643.0)	na	33.7	22.4
Normalised EPS	na	(7,518.0)	na	na	332.4
Normalised FDEPS	na	(7,518.0)	na	na	332.4
Per share					
Reported EPS (US$)	(0.00)	(0.21)	(0.01)	0.01	0.05
Norm EPS (US$)	0.00	(0.20)	(0.00)	0.01	0.04
Fully diluted norm EPS (US$)	0.00	(0.20)	(0.00)	0.01	0.04
Book value per share (US$)	1.82	1.57	1.57	1.58	1.62
DPS (US$)	-	-	-	-	-

Source: Nomura estimates

Gradual EBITDA improvement as CoD ramps up

Cashflow (US$mn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	157	56	430	494	535
Change in working capital	(60)	(168)	(155)	(218)	(103)
Other operating cashflow	(108)	0	(125)	(130)	(109)
Cashflow from operations	**(11)**	**(112)**	**150**	**146**	**324**
Capital expenditure	(1,052)	(920)	(225)	(125)	(65)
Free cashflow	**(1,063)**	**(1,033)**	**(75)**	**21**	**259**
Reduction in investments	-	-	-	-	-
Net acquisitions					
Reduction in other LT assets	(46)	32	37	5	5
Addition in other LT liabilities	18	(34)	34	5	5
Adjustments	(65)	(53)	(0)	(6)	(6)
Cashflow after investing acts	**(1,156)**	**(1,088)**	**(3)**	**25**	**263**
Cash dividends					
Equity issue	-	384	-		
Debt issue	904	270	6	(217)	(476)
Convertible debt issue					
Others					
Cashflow from financial acts	**904**	**653**	**6**	**(217)**	**(476)**
Net cashflow	**(251)**	**(434)**	**2**	**(192)**	**(213)**
Beginning cash	1,134	883	449	451	259
Ending cash	883	449	451	259	46
Ending net debt	645	1,350	1,353	1,328	1,066

Source: Nomura estimates

Placed additional equity in FY09 to buffer the CoD opening

Balance sheet (US$mn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	883	449	451	259	46
Marketable securities					
Accounts receivable	73	300	405	627	753
Inventories	2	7	7	7	7
Other current assets	18	20	20	20	20
Total current assets	**976**	**775**	**882**	**913**	**825**
LT investments					
Fixed assets	2,879	3,501	3,430	3,235	2,971
Goodwill	86	86	86	86	86
Other intangible assets	434	448	427	406	385
Other LT assets	123	91	54	49	44
Total assets	**4,498**	**4,900**	**4,880**	**4,689**	**4,311**
Short-term debt		45	267	526	386
Accounts payable	443	498	448	452	475
Other current liabilities	7	17	17	17	17
Total current liabilities	**450**	**559**	**732**	**995**	**878**
Long-term debt	1,528	1,754	1,538	1,062	726
Convertible debt					
Other LT liabilities	111	78	112	117	122
Total liabilities	**2,090**	**2,391**	**2,382**	**2,174**	**1,726**
Minority interest	-	-	-	-	-
Preferred stock					
Common stock	13	16	16	16	16
Retained earnings	(258)	(567)	(578)	(560)	(488)
Proposed dividends					
Other equity and reserves	2,654	3,060	3,060	3,059	3,058
Total shareholders' equity	**2,409**	**2,509**	**2,498**	**2,515**	**2,586**
Total equity & liabilities	**4,498**	**4,900**	**4,880**	**4,689**	**4,312**
Liquidity (x)					
Current ratio	2.17	1.39	1.21	0.92	0.94
Interest cover	4.0	(4.1)	1.1	1.1	1.5
Leverage					
Net debt/EBITDA (x)	4.12	24.22	3.15	2.69	1.99
Net debt/equity (%)	26.8	53.8	54.2	52.8	41.2
Activity (days)					
Days receivable	15.9	51.1	48.7	64.5	82.5
Days inventory	na	na	na	na	na
Days payable	na	na	na	na	na
Cash cycle	na	na	na	na	na

Source: Nomura estimates

Melco Int'l Dev. 200 HK

GAMING, HOTELS & LEISURE | CHINA

Maintained

REDUCE

NOMURA

NOMURA INTERNATIONAL (HK) LIMITED

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Action

We lift our valuation of Melco on our revised earnings forecasts and higher PT for major value driver MPEL. While the holding discount may have widened to more than 40%, we continue to prefer MPEL, since Melco has a complex corporate structure and is subject to 24% CB dilution risk. While we note valuation is not expensive, we consider a re-rating unlikely in the short term, given a strong YTD rally and concern arising from rising credit risk and the opening of Galaxy Macau on its major value driver MPEL. Thus REDUCE maintained; PT lifted to HK$4.83.

Catalysts

Improvement in mass market share by MPEL and continued turnaround in its business at the City of Dreams are potential catalysts.

Anchor themes

We favour stocks with resilient qualities in a downturn as the expectation gap has introduced higher downside risk.

Closing price on 11 Mar	HK$5.13
Price target	HK$4.83
	(from HK$4.34)
Upside/downside	-5.8%
Difference from consensus	-15.2%
FY11F net profit (HK$mn)	(12.22)
Difference from consensus	-162.1%

Source: Nomura

Nomura vs consensus

We expect Melco would still be marginally loss making in FY11F due to our lower-than-consensus assumption of MPEL's contributions.

Lack of re-rating catalysts

① Rely on MPEL to re-rate

Given Melco is a holding company where over 90% of EV comes from its holding in MPEL, our estimates for Melco benefit from upward revisions to our earnings forecasts and PT for MPEL (now US$6.9). In addition, other lines of businesses, valued based on market cap, have grown over time, further boosting our valuation for the stock. Still, after its strong YTD rally, we think any re-rating of Melco could face resistance, given new concerns stemming from MPEL's potential credit risk arising from its effort to step up direct VIP business, plus the potential impact of Galaxy Macau. Therefore, while we expect limited downside in the short run, we think it may be difficult for the stock to re-rate.

② Despite widening holding discount, still prefer MPEL

Despite the fact that the holding discount between Melco and MPEL has widened in recent months to over 40% versus 30% a year ago, we still prefer MPEL for direct exposure to Macau, because in the presence of derivative instruments and some frequent one-off items, Melco has a complex corporate structure. It is also subject to dilution risk from its convertible bonds.

③ In-line 4Q10 results

MPEL reported flat q-q 4Q10 adjusted EBITDA of US$134mn, in line with market estimates. VIP turnover and mass market drop grew by 12% and 14% q-q, respectively. Management efforts continued to pay off amid favourable supply/demand dynamics.

④ Valuation and investment risks

We keep our sum-of-the-parts valuation approach, where we use our new MPEL PT of US$6.9 and value the other business lines based on market cap. Upside risks: better-than-expected performance of CoD and strong VIP business growth.

Key financials & valuations

31 Dec (HK$mn)	FY09	FY10F	FY11F	FY12F
Revenue	710	743	779	816
Reported net profit	(1,450)	(88)	(12)	132
Normalised net profit	(1,134)	(88)	(12)	132
Normalised EPS (HK$)	(0.92)	(0.07)	(0.01)	0.11
Norm. EPS growth (%)	na	na	na	na
Norm. P/E (x)	na	na	na	48.0
EV/EBITDA (x)	-6.6	812.1	82.0	29.9
Price/book (x)	0.9	1.0	1.0	0.9
Dividend yield (%)	0.0	0.0	0.0	0.0
ROE (%)	(19.9)	(1.3)	(0.2)	2.0
Net debt/equity (%)	7.2	10.6	9.0	7.5
Earnings revisions				
Previous norm. net profit		(199.4)	(219.2)	(142.5)
Change from previous (%)		(56.0)	(94.4)	(192.3)
Previous norm. EPS (HK$)		(0.162)	(0.178)	(0.116)

Source: Company, Nomura estimates

Share price relative to MSCI China

	1m	3m	6m
Absolute (HK$)	0.8	10.6	57.4
Absolute (US$)	0.8	10.3	56.9
Relative to Index	(3.3)	11.7	51.8
Market cap (US$mn)			810
Estimated free float (%)			65.5
52-week range (HK$)			6.21/2.91
3-mth avg daily turnover (US$mn)			10.33
Stock borrowability			Hard
Major shareholders (%)			
Lawrence Ho			33.5

Source: Company, Nomura estimates

Valuation and investment risks

Valuation

We value Melco using a sum-of-the-parts approach (method unchanged), combining: 1) the value of MPEL using our revised target valuation of US$6.9/ADR; 2) the effective stake for listed non-MPEL subsidiaries/associates at market value; and 3) net debt (cash net of bank, shareholders' loans and CBs). We adjust our MPEL-Melco holding discount from 35% to 40% to reflect the expanding holding discount trend assigned by the market (more details below). Our new PT is HK$4.83.

Valuation method unchanged

Exhibit 34. Melco: NEW sum-of-the-parts valuation

Components	Valuation methodology	2011F NAV (HK$mn)	Per share (HK$)
Melco-Crown (MPEL US)	33.81% of MPEL value at US$6.9	9,678	7.87
Melco-Lot (8198 HK)	11.09% market value	7	0.01
Elixir Gaming Tech (EGT US)	39.8% market value	127	0.10
Melco China Resorts (MCG CN)	49.3% market value	92	0.08
Loans to associates		662	0.54
Total EV		10,567	8.60
Less: net (debt)/cash	Including CB and shareholders' loan	(587)	(0.48)
Net Asset Value		**9,980**	**8.12**
Holding discount	40%	(4,041)	(3.29)
Price target		**5,939**	**4.83**

Source: Nomura estimates

Exhibit 35. Melco: OLD sum-of-the-parts valuation

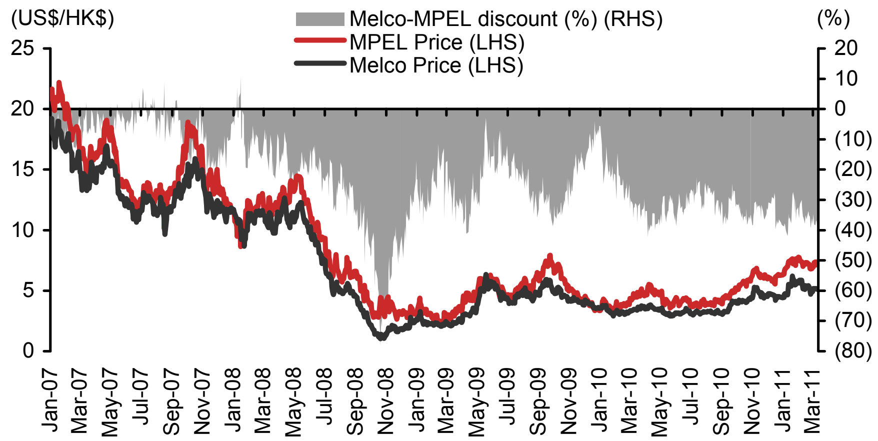
Components	Valuation methodology	2011F NAV (HK$mn)	Per share (HK$)
Melco-Crown (MPEL US)	33.81% of MPEL value at US$5.70	7,998	6.51
Melco-Lot (8198 HK)	11.09% market value	14	0.01
Elixir Gaming Tech (EGT US)	39.8% market value	88	0.07
Melco China Resorts (MCG CN)	49.3% market value	43	0.03
Loans to associates		662	0.54
Total EV		8,804	7.16
Less: net (debt)/cash	Including CB and shareholders' loan	(587)	(0.48)
Net Asset Value		**8,217**	**6.68**
Holding discount	35%	(2,876)	(2.34)
Price target		**5,341**	**4.34**

Source: Nomura estimates

We apply a Melco-MPEL discount since MPEL was spun off in December FY06. For simplicity, we ignore other non-MPEL assets and compare just the holding premium/discount for Melco's MPEL stake. The historical average has widened, as shown in the Exhibit below. We have adjusted our holding discount from 35% to 40% to reflect this trend.

MPEL-Melco holding discount has widened

Exhibit 36. MPEL and Melco's share price performance and holding discount



Source: Bloomberg, Nomura research

Investment risks

Upside risks to our call include better-than-expected performance of CoD, strong VIP business growth, and further delays to other casino projects in Macau, which could limit upcoming supply.

Downside risks include regulatory changes by the China government, the potential recommencement of a VIP commission war, and weaker-than-expected performance of CoD.

Financial statement analysis

Earnings revisions

Our EBITDA forecasts are unchanged, but we increase our net profit forecasts due to improved contributions / narrowed losses from MPEL, Melco's major holding. The difference is recognised under the line of "share of associate and JV net profit".

Exhibit 37. Melco: earnings revisions

	EPS (HK$)			EBITDA (HK$mn)			EBITDA margin (%)		
	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F	FY10F	FY11F	FY12F
Old	(0.16)	(0.18)	(0.12)	49	51	52	6.5	6.5	6.4
New	**(0.07)**	**(0.01)**	**0.11**	**49**	**51**	**52**	**6.5**	**6.5**	**6.4**
Change	0.09	0.17	0.22	0.0	0.0	0.0	0.0	0.0	0.0
Change (%)	56	94	192	0.0	0.0	0.0	0.0	0.0	0.0

Source: Nomura estimates

Financial statements

MPEL's earnings the main driver

Income statement (HK$mn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Revenue	691	710	743	779	816
Cost of goods sold					
Gross profit	**691**	**710**	**743**	**779**	**816**
SG&A	(612)	(658)	(695)	(728)	(764)
Employee share expense					
Operating profit	**79**	**52**	**49**	**51**	**52**
EBITDA	**79**	**52**	**49**	**51**	**52**
Depreciation					
Amortisation					
EBIT	**79**	**52**	**49**	**51**	**52**
Net interest expense	(107)	(99)	(99)	(99)	(99)
Associates & JCEs	(30)	(1,087)	(40)	34	176
Other income					
Earnings before tax	**(58)**	**(1,134)**	**(91)**	**(15)**	**129**
Income tax	(1)	(1)	-	-	-
Net profit after tax	**(59)**	**(1,135)**	**(91)**	**(15)**	**129**
Minority interests	4	1	3	3	3
Other items					
Preferred dividends					
Normalised NPAT	**(56)**	**(1,134)**	**(88)**	**(12)**	**132**
Extraordinary items	(2,301)	(316)	-	-	-
Reported NPAT	**(2,357)**	**(1,450)**	**(88)**	**(12)**	**132**
Dividends					
Transfer to reserves	**(2,357)**	**(1,450)**	**(88)**	**(12)**	**132**
Valuation and ratio analysis					
FD normalised P/E (x)	na	na	na	na	48.0
FD normalised P/E at price target (x)	na	na	na	na	45.2
Reported P/E (x)	na	na	na	na	48.0
Dividend yield (%)	-	-	-	-	-
Price/cashflow (x)	34.3	na	na	56.4	71.3
Price/book (x)	0.8	0.9	1.0	1.0	0.9
EV/EBITDA (x)	153.7	(6.6)	812.1	82.0	29.9
EV/EBIT (x)	153.7	(6.6)	812.1	82.0	29.9
Gross margin (%)	100.0	100.0	100.0	100.0	100.0
EBITDA margin (%)	11.4	7.3	6.5	6.5	6.4
EBIT margin (%)	11.4	7.3	6.5	6.5	6.4
Net margin (%)	(341.1)	(204.3)	(11.8)	(1.6)	16.1
Effective tax rate (%)	na	na	na	na	-
Dividend payout (%)	na	na	na	na	-
Capex to sales (%)	2.1	1.0	-	-	-
Capex to depreciation (x)	na	na	na	na	na
ROE (%)	(26.2)	(19.9)	(1.3)	(0.2)	2.0
ROA (pretax %)	0.4	(11.7)	0.1	1.1	2.9
Growth (%)					
Revenue	(32.0)	2.7	4.8	4.8	4.8
EBITDA	(41.7)	(34.6)	(6.1)	4.0	3.2
EBIT	(41.7)	(34.6)	(6.1)	4.0	3.2
Normalised EPS	na	na	na	na	na
Normalised FDEPS	na	na	na	na	na
Per share					
Reported EPS (HK$)	(1.92)	(1.18)	(0.07)	(0.01)	0.11
Norm EPS (HK$)	(0.05)	(0.92)	(0.07)	(0.01)	0.11
Fully diluted norm EPS (HK$)	(0.05)	(0.92)	(0.07)	(0.01)	0.11
Book value per share (HK$)	6.43	5.43	5.34	5.33	5.43
DPS (HK$)	-	-	-	-	-

Source: Nomura estimates

Cashflow (HK$mn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	79	52	49	51	52
Change in working capital	992	113	24	24	25
Other operating cashflow	(887)	(283)	(91)	37	11
Cashflow from operations	**184**	**(117)**	**(19)**	**112**	**88**
Capital expenditure	(14)	(7)	-	-	-
Free cashflow	**169**	**(125)**	**(19)**	**112**	**88**
Reduction in investments	1,340	929	40	(34)	(176)
Net acquisitions	(99)	351	-	-	-
Reduction in other LT assets	(157)	1,115	(169)	128	102
Addition in other LT liabilities	41	(205)	5	5	5
Adjustments	(1,363)	(1,237)	(72)	(100)	68
Cashflow after investing acts	**(68)**	**828**	**(215)**	**112**	**88**
Cash dividends					
Equity issue	-	-	-	-	-
Debt issue	233	(346)	(50)	(50)	(50)
Convertible debt issue					
Others	(69)	(26)	-	-	-
Cashflow from financial acts	**164**	**(372)**	**(50)**	**(50)**	**(50)**
Net cashflow	**96**	**456**	**(265)**	**62**	**38**
Beginning cash	309	405	861	596	658
Ending cash	405	861	596	658	696
Ending net debt	1,220	484	699	587	499

Source: Nomura estimates

Balance sheet (HK$mn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	405	861	596	658	696
Marketable securities					
Accounts receivable	131	35	35	35	35
Inventories					
Other current assets	353	169	160	152	145
Total current assets	**888**	**1,065**	**791**	**845**	**876**
LT investments	7,927	6,998	6,958	6,992	7,168
Fixed assets					
Goodwill					
Other intangible assets					
Other LT assets	1,591	475	644	516	414
Total assets	**10,406**	**8,538**	**8,394**	**8,353**	**8,457**
Short-term debt	346	166	116	66	16
Accounts payable					
Other current liabilities	480	313	329	346	363
Total current liabilities	**826**	**480**	**446**	**412**	**379**
Long-term debt	217	50	50	50	50
Convertible debt	1,062	1,128	1,128	1,128	1,128
Other LT liabilities	376	171	176	181	186
Total liabilities	**2,481**	**1,829**	**1,800**	**1,771**	**1,744**
Minority interest	26	27	27	27	27
Preferred stock					
Common stock	615	615	615	615	615
Retained earnings					
Proposed dividends					
Other equity and reserves	7,285	6,067	5,951	5,939	6,071
Total shareholders' equity	**7,900**	**6,682**	**6,567**	**6,554**	**6,686**
Total equity & liabilities	**10,406**	**8,538**	**8,394**	**8,353**	**8,457**
Liquidity (x)					
Current ratio	1.07	2.22	1.78	2.05	2.31
Interest cover	0.7	0.5	0.5	0.5	0.5
Leverage					
Net debt/EBITDA (x)	15.43	9.36	14.39	11.62	9.56
Net debt/equity (%)	15.4	7.2	10.6	9.0	7.5
Activity (days)					
Days receivable	215.4	42.5	17.1	16.3	15.6
Days inventory	na	na	na	na	na
Days payable	na	na	na	na	na
Cash cycle	na	na	na	na	na

Source: Nomura estimates

Convertible bonds — restructured in FY09

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