

Generous and stable payout policy

Key points:

- Net profit up 26.8% YoY
- Generous payout policy
- Stable despite slower economic growth
- Cost free sub-concession income
- Attractively valued

Payout policy remains generous. NagaCorp saw its interim net profit increase 26.8% YoY to US\$25.5m, on a 68.5% YoY increment in turnover to US\$109.1m. The company proposed an interim dividend of US\$15.3m, or US\$0.74 per share, representing a payout ratio of 60.2%. At end-Jun 2008, the group was in a net cash position of US\$46.7m.

Casino remains major revenue source. During the period, casino revenue surged 68.5% YoY to US\$108.9m, accounting for more than 99.0% of the group's total revenue. The public floor division and STG division accounted for 50.5% and 48.1%, respectively, of the group's gaming revenue.

Margin squeezed. The blended margin narrowed 10.6 pcp YoY to 41.5% in 1H FY12/08A as the gross margin of the public floor division shrunk to 23.8% from 52.2% in 1H FY12/07A due to higher marketing expenses (commissions to operator, freebies to customers).

The gross profit margin of the STG division widened 8.4 pcp YoY to 58.4% thanks to its fixed overriding management fee income generated from the sub-concession agreement with Poibos. We estimate this income was cost free and went directly to the bottom line.

STG division - focus on quality. Excluding the US\$12.6m fixed overriding management fee income, revenue of the STG division declined 10.6% YoY to US\$39.8m, mainly due to a 0.62pcp drop in the win rate to 3.25%, even though the rollings increased 9.1% YoY to US\$1.2b. Since the company decided to focus on the quality of STG players rather than quantity, the number of STG players decreased 15.0% YoY to 7,817.0, while the average check-in amount per STG player increased 27.6% YoY to a record level of US\$32,442.1. The higher average check-in amount per player boosted the rollings of the STG division, despite the drop in the number of players. The group managed to contain more marketing-related expenses as the number of STG players declined. The major cost component of the division was commissions to the junkets (1.6% of the rollings) and freebies for STG players (0.1% of the rollings).

STRONG BUY
(unchanged)

Asia Gaming

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Stock data

Price	HK\$1.80
Target price	HK\$2.84(+57.8%)
12 mth range	HK\$1.52-2.85
Market cap.	US\$478.4m
Daily t/o, 3 mth	US\$0.5m
Free float %	37.7%
Ticker	3918.HK/3918 HK

Financial summary

Year to Dec	06A	07A	08F	09F	10F
Turnover (US\$m)	85.4	140.8	160.1	195.3	217.1
Net Profit (US\$m)	32.6	50.2	55.9	77.5	73.7
EPS (US\$)	0.021	0.024	0.027	0.037	0.036
EPS Δ %	10.4	14.1	11.3	38.6	(4.8)
P/E (x)	10.9	9.5	8.6	6.2	6.5
P/B (x)	2.03	1.82	1.68	1.51	1.38
EV/EBITDA (x)	13.1	8.8	6.2	4.4	3.9
Yield (%)	7.5	6.3	7.0	9.7	9.2
ROE (%)	25.4	20.1	20.4	25.7	22.2
ROCE (%)	25.3	19.8	21.2	27.0	23.3
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Price Performance

	1 mth	3 mth	12 mth
Relative to HSI (%)	+4.8	-8.8	-13.1
Actual price changes (%)	-2.7	-22.1	-20.0

	08F	09F	10F
Consensus EPS (US\$)	0.030	0.038	0.041
Previous forecasts (US\$m)	70.2	93.4	109.9
Previous EPS (US\$)	0.034	0.045	0.053

Price Chart

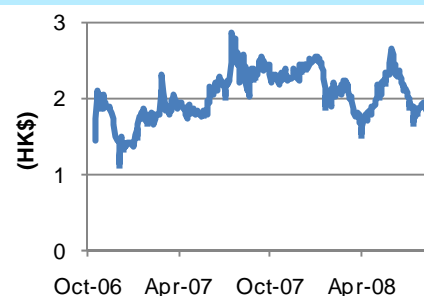


Table 1: STG division performance

	1H07	2H07	FY07	1H08
Excl. management fee income revenue (US\$m)	44.5	20.9	65.4	39.8
Check-ins amount (US\$m)	233.7	175.7	409.4	253.6
No. of players	9,192.0	8,840.0	18,032.0	7,817.0
Check-ins per player (US\$)	25,424.3	19,875.6	22,704.1	32,442.1
Win rate	3.9%	2.5%	3.3%	3.3%

Source: Company

Public floor- expansion in clientele. Thanks to the remarkable success of the Premium Players Program, a marketing campaign aimed at Cambodians with foreign passports, revenue generated from the public floor of NagaWorld surged 194.1% YoY to US\$55.0m. Since public floor division revenue depends on the win rate and buy-in amounts, the 10.5 pcp YoY drop in the win rate limited turnover growth during the period. As the public floor win rate of 17.0% is way below the historical range of 22.0-28.0%, we expect it to stabilize, or even rebound in 2H. We also expect NagaWorld to attract more public customers thanks to its well-developed entertainment facilities and continuous marketing efforts.

Table 2: Public floor division performance

	1H07	2H07	FY07	1H08
Revenue (US\$m)	18.7	56.7	75.4	55.0
Buy-ins amount (US\$m)	68.0	197.1	265.1	323.5
Win rate	27.5%	28.8%	27.7%	17.0%

Source: Company

Workforce expansion. Administrative expenses rose 30.3% YoY to US\$8.6m and other operating expenses 37.9% YoY to US\$10.6m, as the company increased its workforce to 2,424 employees at end-1H FY12/08A, from 1,564 in the year-earlier period, to cope with expansion.

Stable recurrent income. At end-2007, the company agreed to provide of 1,100.0m² gaming hall (about 7.2% of NagaWorld's gaming floor space) to Poibos, a Korea-based entertainment company listed on KOSDAQ. Under the agreement, NagaWorld will also provide gaming management services, manpower and equipment to Poibos, which will pay management fees over two periods: 1) US\$25.2m per annum from 2008 to 2013; 2) US\$31.2m per annum from 2013 to end-2017, generating a total income of US\$282.0m. Just as with Best Merit, other than the space provided and limited management services and equipment, the company's capital commitments are limited and most of the income will go straight to the bottom line. The two sub-concession agreements should generate stable recurrent income.

Attractive despite lower earnings estimates. We have cut our earnings forecasts by 20.4% to US\$55.9m for FY12/08F and 17.1% to US\$77.5m for FY12/09F due to assumption changes for the win-rate of STG and public floor divisions, the average check-in amount per STG player and the number of STG players. Trading at FY12/08F P/E of 8.6x and FY12/09F P/E of 6.2x and providing an attractive prospective FY12/08F dividend yield of 7.0%, the group's valuation remains very attractive, in our view, compared with the sector's average one-year forward P/E of 42.6x and two-year forward P/E of 25.0x. The company has been affected by the global economic slowdown but, unlike its peers in Macau who have to pour tremendous amounts of money into fixed assets to stay competitive, its future capital expenditure is countable and its casino is a growing cash cow. We expect the group to maintain its generous payout policy and the high dividend yield should provide some downside protection for the share price, especially in the current fluctuating market. We reiterate our target FY12/09F P/E multiple of 13.5x, but lower our target price to HK\$2.84 on our lower FY12/09F EPS projection. Our new target price still implies a potential upside of 57.8% and therefore we reiterate our STRONG BUY call.

Table 3: Peer group comparison

Company name	Ticker	Year End	Currency	Price	Market Cap	P/E (x)	
						1-yr forward	2-yr forward
Melco International Development	200 HK	Dec	HKD	5.0	779.3	23.8	12.0
Ameristar Casinos Inc	ASCA US	Dec	USD	16.0	912.6	14.2	12.8
Boyd Gaming Corp	BYD US	Dec	USD	11.9	1,043.8	11.3	11.4
Century Casinos Inc	CNTY US	Dec	USD	2.7	63.8	15.7	11.8
Las Vegas Sands Corp	LVS US	Dec	USD	40.3	14,335.9	87.9	34.7
MGM Mirage	MGM US	Dec	USD	33.3	9,189.1	21.2	18.5
Riviera Holdings Corp	RIV US	Dec	USD	11.2	140.2	6.9	0.0
Wynn Resorts Ltd	WYNN US	Dec	USD	95.6	9,922.2	27.9	31.6
Resorts World Bhd	RNB MK	Dec	MYR	2.5	4,410.5	11.5	10.8
Gold Reef Resorts Ltd	GDF SJ	Dec	ZAr	1,700.0	645.3	11.2	9.1
Sun International Ltd	SUI SJ	Jun	ZAr	8,800.0	1,206.9	12.6	10.1
Sky City Entertainment Group Ltd	SKC NZ	Jun	NZD	3.4	1,141.1	13.9	12.6
<i>Average</i>						42.6	25.0

Source: Bloomberg

Challenges ahead

Increase in competition. Currently, there are at least 213 casinos (legal) in the Asia Pacific Rim and East Asia alone has 121 casinos. With 28 casinos (4,375 gaming tables and 13,267 slot machines), Macau is the region's market leader, followed by the Philippines (19 casinos), Korea (17), Cambodia (14) and Malaysia (1). Many Asian countries are considering establishing casinos to attract tourists. Singapore's first casino complex, Marina Bay Sands should open in 2009 and another, Resorts World, in Sentosa, in 2010. The Thai government plans to legalize gambling and build five casinos in the tourist areas of Phuket, Pattaya, Khon Kaen, Hat Yai and Chiang Mai. Japan and Taiwan plan to legalize casino gambling as well. Nepal is expected to build six casinos, Myanmar four and Vietnam two in the short term. North Korea and Laos are probably going to build casinos too.

Economic slowdown in Asia. The Asia Development Bank (ADB) expects the region's average GDP growth to drop to 7.6% in 2008 and 7.8% in 2009, from 8.7% in 2007, and the average inflation rate to reach 5.1% in 2008 from 4.3% in 2007. This economic growth slowdown and rising inflation will inevitably erode the region's spending power and undermine tourism.

P & L (US\$m)	06A	07A	08F	09F	10F	Cash Flow (US\$m)	06A	07A	08F	09F	10F
Year to Dec						Year to Dec					
Turnover	85.4	140.8	160.1	195.3	217.1	EBIT	32.6	49.5	58.2	81.4	77.5
% chg	32.9	64.8	13.7	22.0	11.1	Depre./amort.	3.9	4.9	18.5	28.3	45.3
Gross profit	50.9	78.1	110.8	146.1	163.7	Net int. paid	(1.6)	(2.5)	(1.4)	(2.0)	(2.5)
						Tax paid	(4.3)	(1.7)	-	(1.7)	(3.7)
EBITDA	36.5	54.4	76.6	109.7	122.8	Dividends received	-	-	-	-	-
Depre./amort.	(3.9)	(4.9)	(18.5)	(28.3)	(45.3)	Gross cashflow	30.6	50.2	75.2	106.0	116.6
EBIT	32.6	49.5	58.2	81.4	77.5	Chgs. in working cap.	(124.6)	(11.9)	5.4	(3.1)	(1.3)
Net int. income/(exp.)	1.6	2.5	1.4	2.0	2.5	Operating cashflow	(94.0)	38.4	80.6	102.9	115.3
Exceptionals	-	-	-	-	-	Capex	(13.1)	(39.4)	(15.3)	(23.8)	(40.2)
Associates	-	-	-	-	-	Free cashflow	(107.1)	(1.0)	65.3	79.1	75.1
Jointly-controlled entit.	-	-	-	-	-	Dividends paid	(3.7)	(24.0)	(31.6)	(48.0)	(45.0)
Pre-tax profit	34.1	51.9	59.5	83.4	80.0	Net distribution to MI	-	-	-	-	-
Tax	(1.5)	(1.7)	(3.7)	(5.9)	(6.3)	Investments	-	-	-	-	-
Minority interests	-	-	-	-	-	Disposals	0.0	0.0	-	-	-
Net profit	32.6	50.2	55.9	77.5	73.7	New shares	199.9	-	-	-	-
% chg	30.8	53.9	11.3	38.6	(4.8)	Others	(11.5)	2.9	2.8	4.0	5.1
Dividends	(28.0)	(30.0)	(33.4)	(46.5)	(44.2)	Net cashflow	77.6	(22.1)	36.5	35.1	35.2
Retained earnings	4.6	20.2	22.5	31.0	29.5	Net (debt)/cash - Beg.	0.7	78.3	56.2	92.7	127.8
						Net (debt)/cash - End.	78.3	56.2	92.7	127.8	162.9
EPS (US\$) - Basic	0.021	0.024	0.027	0.037	0.036	Interim Results (US\$m)	06A	07A	08A		
EPS (US\$) - F.D.	0.021	0.024	0.027	0.037	0.036	Six months to Jun					
DPS (US\$)	0.017	0.014	0.016	0.022	0.021	Turnover	41.9	64.7	109.1		
No. sh.s o/s (m) - W.A.	1,541.0	2,075.0	2,075.0	2,075.0	2,075.0	% chg		54.4	68.5		
No. sh.s o/s (m) - Y.E.	2,075.0	2,075.0	2,075.0	2,075.0	2,075.0	Profit from operations	18.3	19.5	26.1		
No. sh.s o/s (m) - F.D.	1,541.0	2,075.0	2,075.0	2,075.0	2,075.0	Interest income	-	1.5	0.4		
						Associates	-	-	-		
Margins (%)						Jointly-controlled entit.	-	-	-		
Gross	59.6	55.5	69.2	74.8	75.4	Pre-tax profit	18.3	20.9	26.4		
EBITDA	42.7	38.6	47.9	56.2	56.5	Tax	(0.8)	(0.9)	(1.0)		
EBIT	38.1	35.1	36.3	41.7	35.7	Minority interests	-	-	-		
Pre-tax	40.0	36.9	37.2	42.7	36.8	Net profit	17.5	20.1	25.5		
Net	38.2	35.7	34.9	39.6	34.0	% chg		14.7	26.9		
						EPS (US\$) - Basic	0.013	0.010	0.012		
						DPS (US\$)	-	0.007	0.007		
Balance Sheet (US\$m)	06A	07A	08F	09F	10F	Shareholding Structure				Shares o/s (m)	%
Year to Dec											
Fixed assets	46.9	91.5	92.0	91.0	89.5	Tan Sri Dr Chen Lip Keong				1292.7	62.3
Intangible assets	101.7	98.1	94.6	91.0	87.5	Other shareholders				782.3	37.7
Other LT assets	0.7	0.7	0.7	0.6	0.6	Total				2,075.0	100.0
Cash	78.3	56.2	92.7	127.8	162.9	Background					
Accounts receivable	12.1	33.5	25.4	31.0	34.4	NagaCorp Ltd. is engaged principally in the management and operation of the only licensed casino in Phnom Penh, the capital city of Cambodia.					
Other receivables	-	3.0	-	-	-	The rights to operate the casino are valid for a period of 70 years from January 1995 and are exclusive within a 200km radius of Phnom Penh (except Cambodia-Vietnam border area, Bokor, Kirirom Mountains and Sihanoukville) until the end of 2035. NagaCorp Ltd operates and manages a casino and hotel complex known as NagaWorld in Phnom Penh.					
Inventories	0.0	0.1	0.0	0.1	0.1	Key Ratios	06A	07A	08F	09F	10F
Due from related co.s	-	-	-	-	-	Net gearing (%)	Cash	Cash	Cash	Cash	Cash
Other current assets	8.3	-	-	-	-	Net ROE (%)	25.4	20.1	20.4	25.7	22.2
Total assets	248.0	283.1	305.3	341.5	375.0	EBIT ROCE (%)	25.3	19.8	21.2	27.0	23.3
Accounts payable	(10.0)	(18.4)	(15.7)	(18.2)	(20.4)	Dividend payout (%)	85.8	59.8	59.8	60.0	60.0
Other payable	-	-	-	-	-	Effective tax rate (%)	4.5	3.3	6.1	7.1	7.9
Tax payable	(0.0)	-	(1.7)	(3.7)	(5.9)	Net interest coverage (x)	na	na	na	na	na
Due to related co.s	-	-	-	-	-	A/R turnover (days)	46.1	59.1	67.1	52.7	55.0
ST debts	(0.0)	(0.0)	-	-	-	A/P turnover (days)	286.3	36.8	38.9	31.7	32.5
Other current liab.	(2.1)	(2.1)	(2.1)	(2.1)	(2.1)	Stock turnover (days)	0.2	0.2	0.4	0.4	0.4
LT debts	0.0	-	-	-	-						
Other LT liabilities	-	-	-	-	-						
Total liabilities	(12.1)	(20.5)	(19.5)	(24.0)	(28.5)						
Share capital	25.9	25.9	25.9	25.9	25.9						
Reserves	210.0	236.6	259.9	291.5	320.6						
Shareholders' funds	235.9	262.6	285.8	317.5	346.5						
Minority interest	-	-	-	-	-						
Total	235.9	262.6	285.8	317.5	346.5						
Capital employed	235.9	262.6	285.8	317.5	346.5						
Net (debt)/cash	78.3	56.2	92.7	127.8	162.9						

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