

Asia Pacific Gaming

Takeaways from conference call with Suncity. Low GGR visibility near term.

Asia Leisure [Explore >](#)

On Feb 10, we hosted a conference call with management of Suncity Group, which runs the largest junket operations in Asia under its private entity. Its listed arm (1393.HK; Not covered) constructs and/or operates a number of casino projects in Vietnam, Russia, Philippines and Cambodia either by controlling other companies (e.g., 24.7% equity stake in Summit Ascent) or forming JVs (e.g., Suntrust in Philippines). Upon the completion of these projects scheduled by 2025, it will have over 800 tables, 4,500 hotel rooms and 2,500 slots across its asset portfolio.

As expected, most of the investor questions focused on the impact of coronavirus, about which management sounds cautious and does not expect any recovery until 2H20 given (1) various travel restrictions in place which they believe are unlikely to be lifted anytime soon; (2) gaming spending as a form of entertainment tends to be more discretionary in nature and only performs well when macro outlook improves. There remain a lot of uncertainties in the manufacturing and property industries, where most of the VIP or premium mass players earn their wealth from. Overall, the company is hopeful that its rolling volume would not fall more than -20% yoy for the full year of 2020 (vs. its previous guidance of flat volume trend) helped by pent-up demand recovery from 3Q20 onward, but acknowledges that visibility remains low.

Our current FY20E GGR growth forecast of -9% yoy assumes 30-35% GGR decline till end of 2Q20, followed by 15% recovery in 2H20. Should the government decide to extend the current 15-day casino suspension for longer (which Suncity believes depends on the number of new confirmed cases in coming days), it may present further downside risk to our and consensus estimates. As discussed in our prior report, we estimate every week of casino suspension would lower our EBITDA estimates by another 2-3%. After the 2% recovery last week, the sector is now trading at 11x EV/EBITDA in FY21E, vs. mid-cycle of 13x. Valuation does not look demanding, but given a lack of visibility and the above-mentioned earnings risk, we expect share prices to remain volatile near term. For long-term investors looking for

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exposure, we prefer Buy-rated SJM (on CL), Sands China and Galaxy.

Q1: How has the outbreak of coronavirus impacted Suncity's rolling volume so far?

The group's Macau rolling volume dropped 25% yoy in Jan. Comparing it with -10% to -15% yoy decline in the first half of the month, this implies a -30% to -35% yoy decline in the second half of the month, consistent with what we discussed in our [Feb 2 report](#) for the IVS suspension from Jan 24 and the typical pre-CNY weakness. Its business has been further affected after casino operators suspended their operations since Feb 5, and there are little signs that the lost volume in Macau has been diverted to other regional markets (e.g. Philippines, Vietnam, etc) where local governments have imposed various travel restrictions against Chinese travelers. The company also said that the near-term business disruptions in mainland China, particularly in property-related sector and SMEs, have not only hurt gaming demand by VIP players, but also premium mass market players in general. Overall, the group targets no more than 20% yoy rolling volume decline for FY20, vs. its earlier guidance of flattish volume target.

Q2: How has the current situation affected the debt collection cycle and liquidity for Suncity?

As an industry norm, Suncity typically does not collect debts from its players during CNY period, and usually starts to do so post holiday. But given the disruption, it has delayed its collection by 1-2 more weeks. They are not particularly concerned over their ability to collect credit from players and reaffirm that the group has ample liquidity to weather any further disruption in their junket operations. For example, opex related to staff costs mostly commission-based only amounts to HK\$3mn per day, well covered by the cash on hand.

Q3: Based on past experience, what is the expectation on the pace of recovery as the situation stabilizes? Does Suncity expect to see any pent-up demand afterwards?

Suncity sees gaming as a discretionary form of entertainment and does not expect any sharp recovery until 3Q20 onward since its players, many of whom are business owners in China, will likely focus more on addressing their own business operations near term (e.g. managing labour supply) due to disruptions from the viral outbreak. They also believe it may take time for players to start feeling comfortable traveling to Macau again even if casinos resume normal operations after the 15-day suspension. While the actual economic impact from the viral outbreak remains uncertain, they believe the magnitude of recovery would hinge on China's economic outlook especially in the manufacturing and property related industries where the majority of its players are exposed to. Having missed the peak season for gaming (i.e. Chinese New Year), it would be difficult for the junket and casino operators to make up for the lost volume entirely even if there is any pent-up demand as the situation stabilizes.

Q4: Could the 15-day casino suspension be further extended?

While Macau has not reported any new confirmed coronavirus cases since Feb 4,

should there be new cases confirmed in Macau then a further suspension of casino operations could be possible. Suncity also thinks that a potential resumption of IVS (suspended since Jan 28) would be an important driver for its rolling volume given the majority of the VIP and mass market players rely on IVS to travel to Macau, which has no longer been issued since Jan 28 following the suspension of group tours in Jan 24. As highlighted in our [Feb 5 report](#), IVS/group tour represents 47%/23% of total Chinese visitation in FY19.

Q5: How has the current situation affected project construction progress in Macau and across the region?

In terms of Suncity's on-going development projects across Asia, the company mentions that the travel restrictions have affected their construction for the Vietnam Hoiana IR (US\$1bn budget) to a certain extent since some of their construction workers come from mainland China. Despite this, they still target to launch the project by end-1Q20, targeting to replace PRC workers with local subcontractors for the construction. In the Philippines, they target to break ground for Westside City IR project in Mar 2020 and partial opening by May 2022. While Suncity does not have development projects in Macau, they would not be surprised if the construction works for new projects there (e.g. SCC renovation, GM Phase 3 and 4, Lisboa Palace, etc) would be affected as well. This said, they believe casino operators will likely try to stick with their opening by speeding up the construction process at a later point as the situation normalizes.

Q6: What are the latest updates and trends for individual operators in Macau?

When asked about VIP volume trends by individual properties/operators in Macau, Suncity sounds positive on SJM's upcoming project, Lisboa Palace (expected to launch in 3Q20), as they believe the property's design and F&B offerings will be well-received by Chinese players. Its hotel brands (i.e. Palazzo Versace, Karl Lagerfeld) are more unique and should be able to draw more visitation. As an example, after the opening of Morpheus in May 2018, CoD's rolling volume contribution to Suncity in Macau increased from 15% to 28% at the expense of galaxy, Wynn Palace and other adjacent properties. Wynn also lost some VIP market share for less attractive junket commission rates and cash rebates to agents/players. While it is still early, Suncity also commented that the opening of GM Phase 3 and 4 may help galaxy to gain back some lost market share later on, and they remain cautious on the volume outlook at MGM Cotai which continues to struggle to meaningfully drive up VIP demand even after the opening of Mansion villas.

Q7: What is Suncity's positioning across different markets? Which markets does Suncity find more attractive?

Suncity approaches each regional market with different strategies in accordance with the nature of the market. For example, following their launch of Hoiana IR Phase 1 in Vietnam, it will focus on attracting more foreign visitors to the property and actively promotes it to the group's existing VIP customers during the first year of launch. They still believe their original target of US\$12bn VIP rolling volume per annum at Hoiana could be achievable assuming no delays in the opening schedule, although results will

also hinge on whether the coronavirus situation and travel restrictions will stabilize/relax following the launch. In Manila, it targets similar GGR mix at its Westcity project as other existing properties in Entertainment City (43% VIP, 57% mass/slot by our estimate in FY19) not only by marketing the property to its own VIP players on database but also working to attract more mass market players esp. by local slot gamblers. In Vladivostok, the redevelopment for phase 1 and expansion for phase 2 should better position Tigre de Cristal IR to capture additional Korean, Japanese VIP players due to its geographic proximity while also benefiting from the significantly lower gaming tax rate (i.e. maximum of US\$1,900 fixed monthly tax per table).

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