Daiwa Capital Markets

Sector

Consumer Discretionary / Macau
10 October 2014

The 10-second briefing

2015 to be much worse than 2014

- Cutting 2015E GGR (new forecast: -7%); more junket closures to come and premium mass structurally affected by transit visas
- Expect significant negative operating leverage against rising costs in a market contraction; cutting 2015E sector EBITDA by 29%
- Revising down TPs and all but one rating; SJM (Outperform) and MGM (downgraded to Outperform) are our new top picks

Macau Gaming Sector

- Positive
- **Neutral** (from Positive)
- Negative

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What's new

The latest Macau gaming data point to the slowdown lasting longer than expected, with softness across all major operating segments. We cut our 2015E GGR forecast to -7% YoY (from +11%). In the face of 20% wage inflation and other rising fixed costs, negative operating leverage is likely. Today's "build it and they will come" mantra is unlikely to hold up in 2015. Operators with aggressive capacity expansion amid an expected overall market contraction are likely to be the most negatively affected. Our new 2015E sector EBITDA is 27% below consensus, and we expect further cuts to the market's forecasts.

What's the impact

VIP – big picture worsens. We continue to see weakening supply/demand amid a tight credit environment. Some small/mid-sized junkets are dipping below minimum rolling levels, and the big ones have difficulty maintaining minimum volumes. We believe a loosening of credit (and revenue growth) is unlikely in the near term due to the sharp rise in bad debts. Sustained anti-graft efforts into 2015 are also expected to depress VIP growth, and we forecast GGR for the segment to fall by 19% in 2015. Signals to watch for: 1) potential table rolling minimums/junket commission revisions, 2) VIP table reductions per junket, and 3) further junket consolidation, would give colour on what is in store for 2015.

Mass – worrisome trends. We cut 2015E mass GGR growth to 11% YoY (from 20%). For **premium mass**, we highlight 2 negative trends: 1) a fall in visit frequency, especially higher-betting clients, and 2) a 20% fall in average gaming spend per customer vs. 6 months ago. For **grind mass**, while overall visitors set monthly highs, mass revenue growth has gone from 36% YoY for 1H14 to 16% for 3Q14. Recent tourist growth and mix has been shifting to lower-spending tour groups. We think sustainably high tourist growth will thus be needed to drive gaming revenue as a higher proportion of this segment is priced out by current minimum bet levels. The divergence between mass revenue growth (falling) and tourist growth (rising) is a key factor in the cut to our GGR growth forecast.

2015E: negative operating leverage, sequential EBITDA decline. We expect wage inflation, increased capacity, declining table yield, pre-opening staff hiring, and increasing promotional/fixed costs to eat into margins. Most at risk, in our opinion, are operators with new property openings amid a potential market contraction in 2015, especially those with small bases. We now forecast a 1pp contraction in the sector's EBITDA margin for 2015 (30bps expansion previously), and cut our company-level EBITDA forecasts by 22-38% (the biggest cuts for operators with new openings in 2015).

What we recommend

We now prefer operators with more defensive cost profiles. Our top picks are **SJM** (last new Cotai property opening, limited negative operating leverage from satellite casino revenue sharing) and **MGM** (solid operating trend, small operating base, and second-to-last new property opening). We would steer clear of operators with earlier openings (**Galaxy**, **Melco**, and **Sands**), which will likely bear the brunt of the squeeze next year. The key risk to our sector call: a larger-than-expected swing in China's economic fundamentals.

How we differ

While the market seems to favour supply-side driven growth, our stock picks are based on cost defensiveness.

Key stock calls

	New	Prev.
SJM Holdings (880 HK)		
Rating	**Outperform**	Outperform
Target	**16.70**	21.00
Upside	▲ **9.3%**	
MGM China Holdings (2282 HK)		
Rating	**Outperform**	Buy
Target	**23.80**	32.10
Upside	▲ **5.8%**	

Source: Daiwa forecasts.

Sector stocks: key indicators

Company Name	Stock code	Share Price	Rating New	Rating Prev.	Target price (local curr.) New	Target price Prev.	Target price % chg	EPS (local curr.) FY1 New	FY1 Prev.	FY1 % chg	FY2 New	FY2 Prev.	FY2 % chg
Galaxy Entertainment Group	27 HK	47.15	Hold	Buy	45.00	74.00	(39.2%)	2.600	2.987	(13.0%)	2.131	3.721	(42.7%)
Melco Crown Entertainment	MPEL US	25.89	Underperform	Buy	23.00	34.00	(32.4%)	1.133	1.437	(21.2%)	0.555	1.729	(67.9%)
MGM China Holdings	2282 HK	22.50	Outperform	Buy	23.80	32.10	(25.9%)	1.477	1.626	(9.2%)	1.328	1.825	(27.2%)
Sands China	1928 HK	42.15	Hold	Buy	40.00	60.20	(33.6%)	0.276	0.360	(23.4%)	0.253	0.423	(40.1%)
SJM Holdings	880 HK	15.28	Outperform	Outperform	16.70	21.00	(20.5%)	1.238	1.388	(10.8%)	1.033	1.437	(28.2%)
Wynn Macau	1128 HK	25.45	Underperform	Outperform	22.60	33.00	(31.5%)	1.294	1.490	(13.1%)	0.841	1.598	(47.4%)

Source: Daiwa forecasts

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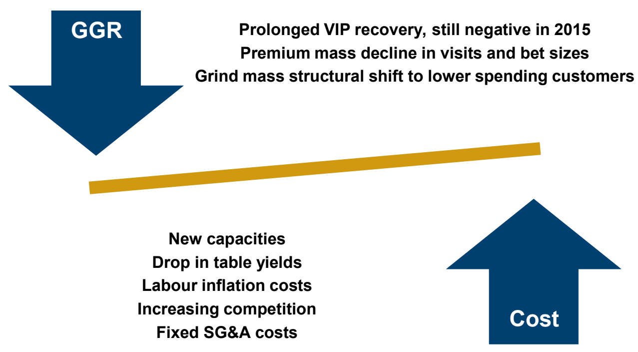
Macau Gaming Sector: 2015E operating deleverage



Source: Daiwa

Macau Gaming Sector: simplified analysis of 2015 forecasts

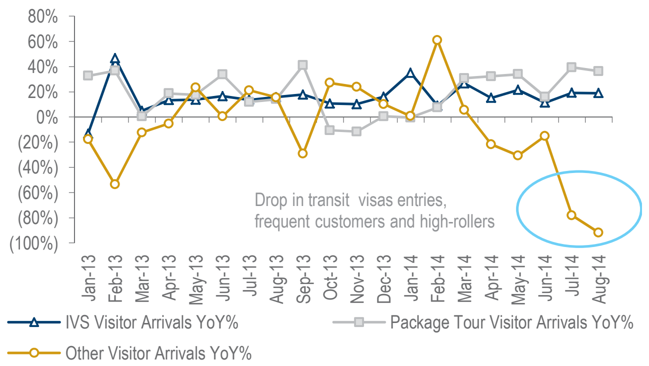
	2014 (rebased to 100)	2015E	YoY
GGR			
VIP	60.0	48.9	-19%
Mass	40.0	44.6	11%
Total	**100.0**	**93.5**	**-7%**
EBITDA			
VIP (10% margin)	6.0	4.9	-19%
Mass (35% margin)	14.0	15.6	11%
Total	**20.0**	**20.5**	**2%**
Cost Inflation			
Wage inflation*	8.5	11.5	35%
Advertising and promo **	3.0	3.7	25%
SG&A	22.0	22.7	3%
EBITDA (cost inflation adjusted)	**17.5**	**16.1**	**-8%**

Source: Daiwa

** 7-10% of GGR in 2014, 20% YoY increase + incremental hiring for new property in 2015*

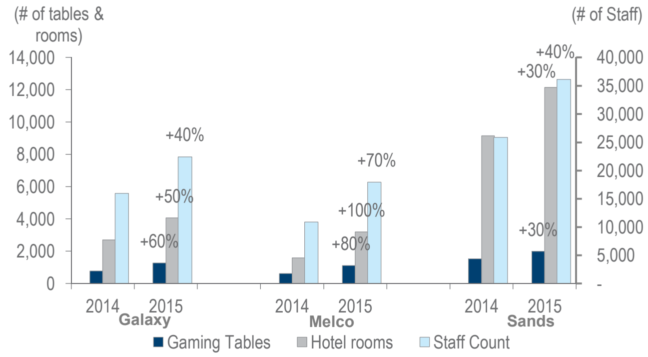
*** from 3% of GGR to 4% of GGR*

Macau: monthly tourist arrivals by segment



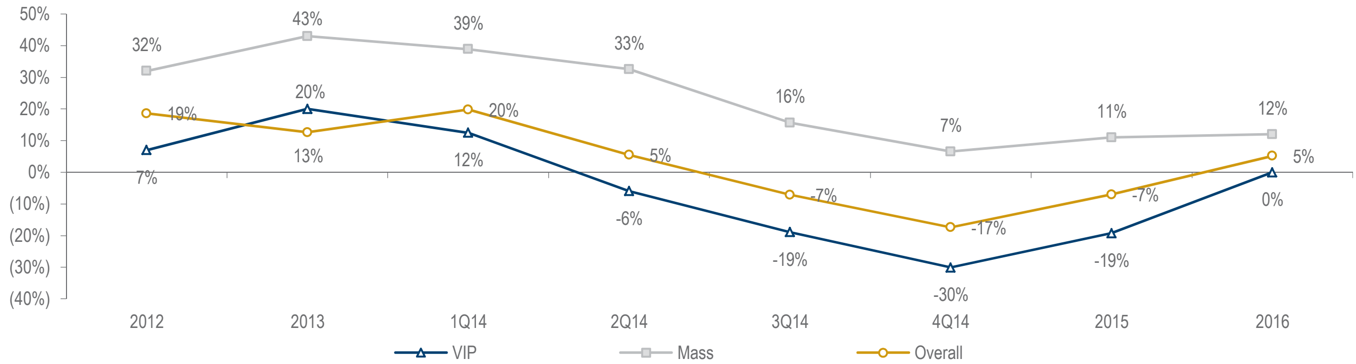
Source: DSEC

Galaxy, Melco, Sands: capacity increases by 2015E new openings



Source: Daiwa

Macau Gaming Sector: GGR growth trend



Source: Daiwa

Macau Gaming Sector: summary of earnings and rating changes

	Share price (Oct 8)	Recommendation			Target Price		Implied Upside	New EBITDA (HKDm)			Old EBITDA (HKDm)			EBITDA change		
Operator		**New**	**Old**	**Currency**	**New**	**Old**		**2H14E**	**2015E**	**2016E**	**2H14E**	**2015E**	**2016E**	**2H14E**	**2015E**	**2016E**
SJM	15.5	Outperform	Outperform	HKD	16.7	21	8%	3,778	7,484	6,490	4,527	9,616	10,714	-17%	-22%	-39%
MGM	22.5	Outperform	Buy	HKD	23.8	32.1	6%	3,152	6,249	6,558	4,225	8,026	9,372	-25%	-22%	-30%
Sands	42.2	Hold	Buy	HKD	40	60.2	-5%	11,197	23,547	25,748	14,264	31,832	40,027	-22%	-26%	-36%
Galaxy	47.2	Hold	Buy	HKD	45.0	74	-5%	6,346	11,357	14,259	7,747	18,308	22,374	-18%	-38%	-36%
Wynn	25.5	Underperform	Outperform	HKD	22.6	33	-11%	3,517	6,966	8,633	4,527	10,317	14,106	-22%	-32%	-39%
Melco	25.9	Underperform	Buy	USD	23.0	34	-11%	3,621	9,309	9,701	5,337	12,783	16,755	-32%	-27%	-42%

Source: Daiwa, Bloomberg

■ **Macau Gaming Sector: issues, concerns, and implications**

Issue	Key concerns	Implications
GGR/EBITDA revisions	1) 2014/15 GGR growth forecast: -1 and -7% YoY (from +6% and +11%, respectively) 2) 2014/15 VIP revenue forecast: -10% YoY and -19% YoY (from -2% and +6% YoY, respectively) 3) 2014/15 mass revenue forecast: +21% YoY and +11% YoY (from +25% and +20% YoY, respectively)	1) Cutting 2014/15E EBITDA by 22% and 29%, respectively 2) Forecast 1pp EBITDA margin contraction in 2015 (from 30bps expansion previously) 3) Our 2015E sector EBITDA is 27% below consensus; we expect further downward consensus revisions in coming months
VIP	1) Small/mid-sized junkets unable to meet table-betting volume minimums and larger junkets seeing difficulties in maintaining betting volumes; limited response casino operators can take to mitigate risk 2) A number of mid-sized junkets (eg, Heng Sheng) planning substantial room closures and consolidation of operations 3) Escalating bad debt, junkets unlikely to loosen credit provisions	1) More junket closures and consolidation to come 2) Potential downward revisions of: a) guaranteed monthly table VIP roll volumes, and b) junket commission structure, may give a sense of new norms for 2015 3) Current segment rolling volumes suggest a further 10-15% table allocation from VIP to mass in order to maintain junkets' guaranteed minimums
Mass	1) 20% decline in average betting activity among high rollers 2) Rated players unable and unlikely to maintain prior frequency of visits due to transit visa changes; anti-graft sentiment also having an impact 3) Despite YTD highs in visits, witnessing structural shift in tourist mix towards lower income segment which is not as conducive for GGR growth 4) Recent months' record-high tourist arrivals driven by tour groups, a higher proportion of whom are priced out by minimum bets	1) Mass table has already achieved critical mass, with table yields peaking in 1Q14E 2) Further table reallocations from VIP to mass unlikely to drive growth 3) Potential reallocation of gaming tables from VIP to mass further lower table yields and margin erosion
Anti-corruption	1) Our chief economist, Kevin Lai, expects to see a shift to a more entrenched and systematic fight against graft to be announced in the upcoming Fourth Plenum	1) Current sentiment extending into 2015 is already the best-case scenario 2) Further heightening of anti-corruption campaign in China a real possibility; may prompt a further sector de-rating
Labour Costs	1) SJM, Wynn, MGM: staff costs to increase by at least 20% YoY in 2015E driven by staff bonuses and wage inflation 2) Galaxy, Sands, Melco: aggressive staff hiring 3-6 months ahead of opening on top of existing staff cost increases; expect a 40-60% YoY wage costs hike	1) Operating deleveraging against negative GGR growth in 2015E 2) Downside risk still exists (15th-month bonus, further increase in wage hikes, etc.)
SG&A	1) A number of services (eg, hotel security, trash collection, casino cleaning) are outsourced and not categorized as staff costs 2) Operators with 3rd party managed hotels have limited room for cost adjustments	1) Staff costs hikes may lead to rises in the number of outsourced staff
Player Reinvestment Costs	1) Increasing competition (between operators and among new property openings) may further increase player reinvestment costs	1) Estimated player reinvestment cost to increase from 3% of GGR in 2014 to 4% in 2015 based on our forecasts; still lower compared to Las Vegas
Table Productivity	1) Slowing GGR growth, increased table counts (from new openings) and rising opex point to potentially lower table productivity in 2015	1) We forecast the sector net win per table to fall by 14% to HKD142k/day in 2015
Smoking Ban	1) Total ban on mass floor (including premium mass) effective October 6	1) Short-term disruption of gaming floor should affect business 2) Ban in premium mass areas is affecting frequent visitors and their gaming habits For our discussion on this, see our memo ***click here***
October/Golden Week numbers	1) Operators unable to price up hotel rooms 2) Sands imposed no special complimentary hotel room policy typical of peak seasons 3) Occupy Central movement in HK continued throughout Golden Week, likely affecting around 20% of Mainland visitors to Macau 4) Major renovations among peak-season properties may cause further disruptions	1) Lacklustre October; we now forecast negative GGR growth of 20-25% YoY For our discussion on October and Golden Week expectations please see our memo ***click here***

Source: Daiwa

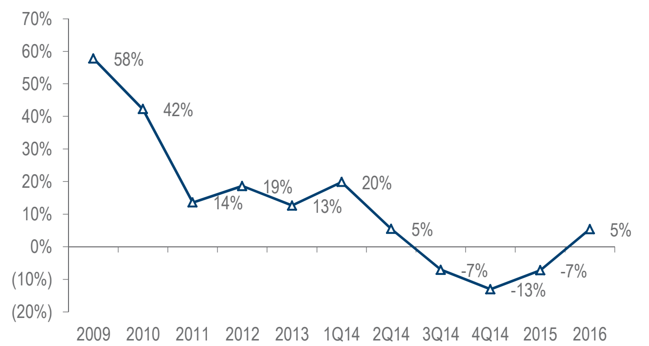
Revising down GGR growth forecasts

New GGR forecasts

Lowering 2014-15E GGR. We are revising down our GGR forecasts for 2014-15 in light of: 1) recent run rates, 2) much slower-than-expected recovery in VIP, 3) a structural shift in tourists and a structural decline in premium mass/high-rollers, 4) expected sustained anti-graft efforts and depressed sentiment in 2015, 5) negative operating leverage, and 6) new capacity.

We now forecast GGR to decline by 1% in 2014 and 7% in 2015. A VIP recovery may be more prolonged than previously expected, and as such, we now forecast VIP GGR to fall by 19% YoY in 2015. We also look for mass GGR growth to slow from 21% in 2014 to 11% in 2015.

■ Macau Gaming Sector: revised GGR growth forecasts



Source: DICJ, Daiwa

■ Macau Gaming Sector: Daiwa GGR growth forecast revisions

		New forecasts			Previous forecasts		
	2013	2014E	2015E	2016E	2014E	2015E	2016E
VIP	13%	-10%	-19%	0%	-2%	6%	8%
Mass	35%	21%	11%	12%	25%	20%	26%
Overall	19%	-1%	-7%	5%	6%	11%	16%

Source: DICJ, Daiwa forecasts

VIP: consolidation far from over

Recovery likely to be more prolonged than previously expected

Junkets unable to meet monthly table betting volume minimums. The average per table rolling volume minimum in Macau is set at HKD200-250m per month. This volume is usually negotiated (on a base-by-case basis) between junket operators and casino operators.

In recent months, a number of small and mid-sized junkets have been facing difficulties in maintaining betting volumes and have dipped below their respective contractual minimums in some months.

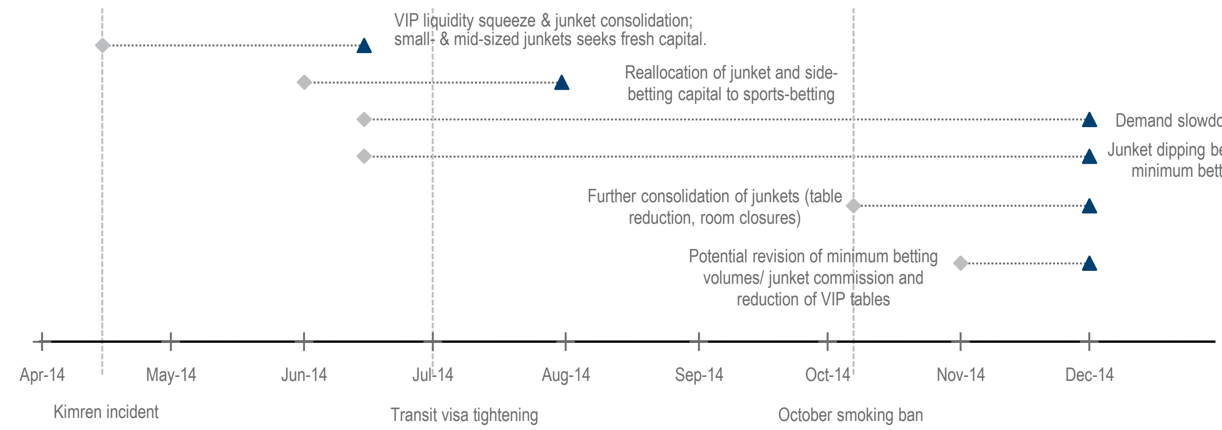
On the other hand, the larger junkets, with substantial table number commitments and a broader casino presence, have been able to maintain their average per table rolling volumes and continue to capture additional market share. However, they are struggling to maintain the necessary levels of table yields.

This is likely a combination of current demand weaknesses and continued liquidity constraints within the VIP system. Our checks indicate that while the VIP liquidity environment has improved since June, it continues to be tight for many of the small and mid-sized junkets.

Planning room closures and consolidation. Based on our checks, a number of junkets are planning to reorganise and consolidate their operations. This includes: 1) closing their own junket rooms, 2) lowering table counts within their own rooms, and 3) closing self-run junket rooms and setting up counters (sub-junket operations) in other junkets to share the burden of table minimums.

As an example, Heng Sheng, a mid-sized junket with around a 5% market share, has been experiencing a severe liquidity crunch and plans to consolidate its businesses. The junket plans to close at least 5 of its 11 junket rooms over the next few months, including those in Galaxy Macau, The Venetian, Sands Cotai Central, and Wynn Macau.

■ **Macau Gaming Sector: VIP timeline of events**



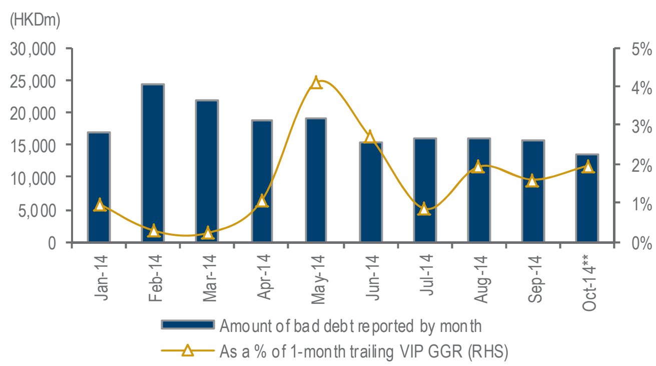
Source: Daiwa

Escalating bad debts worrisome; junkets unlikely to loosen credit provisions. We have tracked the number of instances and amount of bad debt posted on Beautiful World (www.99world.net), a website which regularly publishes bad-debt information on VIP players in Macau.

We analysed Macau's bad debts as a percentage of 1-month trailing VIP revenue (assuming an average collection period of between 2 and 4 weeks) YTD. We note that while VIP revenue has continued to decline on a YoY base over the past 4 months, the proportion of bad debt has seen a notable increase from pre-Kimren levels in April (when a junket agent absconded with HKD8bn). More of a concern is that bad debts (percentage of 1-month trailing VIP GGR) in October to-date have already exceeded the September level.

We believe this trend suggests: 1) the overall quality of players may be declining, and 2) gaming debts are increasingly difficult to collect. Junket operators will likely respond to this by tightening the provision of credit to customers, which would put downward pressure on the segment's fundamentals as a whole.

■ **Bad debt as percentage of 1-month trailing VIP GGR**



Source: Beautiful World, Daiwa
*Note: * Excludes the approximate HKD8bn relating to the Kimren incident in April 2014*
***bad debt up to October 10th, 2014*

What to watch for in 2015

Limited action could be taken by casinos in response. Historically when a junket underperforms, the typical strategy among the casino operators is to reduce their table allocation or remove these junkets from the casinos entirely. The tables might either be allocated to other better performing junkets or to the mass floor. However, this strategy may not be as practical in a market contraction since: 1) slowing VIP means less demand for additional tables by other junkets, and 2) mass table yield likely has already peaked in 1Q14 and further table allocation to the mass floor may not translate into tangible growth.

In our view, there are 3 strategies casino operators can take in response to this dog-eat-dog market contraction; however, we think all would be negative in terms of profitability: 1) Increase junket commissions to attract junkets, 2) potential table reduction at a per junket level, and 3) decrease the rolling minimum required for junkets.

Casino operators could use higher junket commissions and specials comps to attract business. Against declining segment GGR growth, we also expect casino operators to become increasingly aggressive in chasing market share, or the incremental gaming dollar above and beyond rolling minimums.

Casino operators have already begun to offer special incentives to attract junket businesses, including special hotel room deals and special junket commission incentives. We believe any sustained spending of these incremental costs would be margin-dilutive for the segment in the long run.

Potential table reduction or downward revisions to minimum monthly betting volumes in 2015. Due to the prolonged challenges expected to be faced by the junkets, in the coming months we may also see: 1) downward adjustments to guaranteed roll per table as negotiated between junket and casino operators, and/or 2) junkets lowering their total table counts as a means of lowering aggregate minimum bets. The magnitude of these adjustments could give a sense of the new norm we should be expecting for 2015.

We may see 10-15% gaming table reallocation to mass in order for the casinos to maintain guaranteed minimums at current run rates. Based on our forecasted VIP GGR for 2015, our analysis suggests that between 200 and 250 VIP tables (10-15% of existing total) need to be shifted to mass areas in order for the segment as whole to maintain current per table minimums.

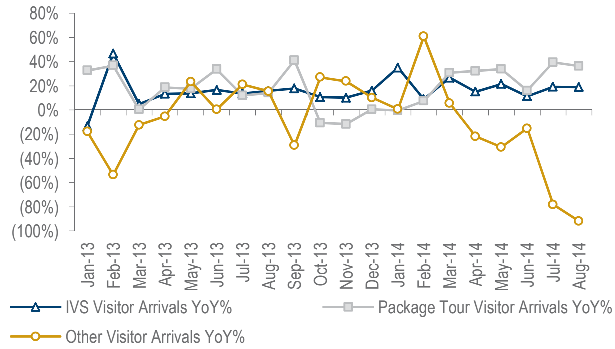
Mass: shift in tourist mix not conducive to GGR growth

Lacking fundamental drivers for a pick-up in growth

Despite record-high visits, the shift in the tourist mix is not conducive to GGR growth. Chinese tourists travelling to Macau reached 2.1m in August, marking another record-breaking month in Macau's history. However, 2 worrisome trends can be observed when examining the details of this number: 1) a substantial pick-up in growth in tour group arrivals (up 36% YoY in August vs. up 20% for 1H14), and 2) a clear decline in the "other" category (down 92% YoY for August after a decline of just 6% YoY for 1H14).

The "other" category is particularly important, as it includes travellers who visit Macau on transit visas and business visas, both of which are frequently used by higher-betting quality rated premium mass players.

■ Mainland Chinese visits by different means (YoY growth)



Source: The Statistics and Census Service of Macau (DSEC)

Premium mass looking lacklustre: frequency of visits and average betting activity both declined; trend unlikely to reverse in near term. Based on our conversations with premium mass hosts in some of the flagship properties, 2 worrisome trends were noted: 1) average per-player gaming activity has declined by around 20% when compared to 1Q14 levels, and 2) the frequency of visits among high rollers has seen a notable decline.

These trends likely have resulted from the recent restriction of transit visas and the overall depressed sentiment in China due to the anti-graft crackdown. As such, it is unlikely we will see a substantial improvement in frequency of visits by rated players in the near term.

Tour groups: priced out and require substantial visitor growth to drive gaming business. In our view, the strong growth of tour groups to Macau is not as conducive to driving GGR growth. According to local news flow, tourists joining tour groups spend HKD3,000-4,000 per trip, mainly on shopping, dining and sightseeing. These tourists are also more likely to spend money on shopping, since much of the time typically allocated on these tours is for shopping (rather than gaming), whereby tour guides have rebate incentives to encourage purchases. Against minimum bet sizes of HKD500-1,500 on the mass gaming floor, we believe a material portion of the tour groups are also effectively priced out from gaming.

Grind mass is likely the most structurally intact segment in Macau. During this year's Golden Week, Macau witnessed a 17% YoY increase in tourist arrivals. While hotel occupancy continues to be very high, we did witness an average 20-30% decline in average daily rates (ADR) for rooms versus prior peak seasons. In our view, a peak season room rate is a very good indicator of 1) relative demand and 2) the overall quality of customers travelling to Macau. The YoY decline in ADR during peak season is a strong indicator of the tourist mix shift to those with lower spending power.

A lower gaming budget per customer for tour groups means that there needs to be very high tourist growth in Macau in order for any meaningful mass GGR growth to be seen.

A good indicator of this is The Venetian, a well recognised not-to-be-missed property among Mainland tourists, which has been achieving record-high footfall in Macau. While property visits continue to rise, casino hosts have remarked that casino visits and overall gaming headcount have actually seen notable declines over the past 3 months. On the other hand, during Golden Week when The Venetian saw high foot traffic, its market share in GGR increased by 4pp from that for September.

Mass table productivity has already peaked; set to fall in 2015

Table yields likely already peaked in 1Q14. Mass table productivity has doubled over the past 3 years, likely peaking in 1Q14 with net wins of HKD101k/day. In 2Q14, we saw net wins declining to HKD100k/day, marking a 1% QoQ decline. In 3Q14, wins look set to decline by another 1% QoQ to HKD99k/day.

Table productivity to see 11% decline by 2016E. On an annual basis, we expect mass table yields to post growth of 10% YoY in 2014, largely driven by a relatively stronger 1H.

However, as we head into 2015-16, we look for table yields to drop by 11% to HKD86k/day by 2016, driven by: 1) the expected slowing mass market growth in 2015-16, 2) new gaming table capacity from new casino openings, and 3) likely table shifts from VIP to mass (see page 8).

Margin erosion expected. We look for a decline in table yields and increasing labour costs to drive margin erosion across the sector. We discuss this in detail in the next section.

China's macro environment also unlikely to help Macau

Entrenching anti-graft efforts; sentiment unlikely to abate in 2015

(by Kevin Lai, Daiwa Chief Economist)

Anti-graft efforts began to escalate in February 2014. China's 2-year anti-graft campaign began to escalate in February 2014, and culminated in the downfall of Zhou Yongkang in July 2014, the first member of the Politburo Standing Committee to be prosecuted for graft and potentially other crimes.

Overall anti-graft sentiment has led to reduced demand for any product or services associated with ostentatious displays of wealth. It has dealt a blow to many areas, including the Macau Gaming Sector which has contributed to the negative GGR growth witnessed since June 2014.

A shift to a systematic fight against anti-graft in 2015. In the upcoming Fourth Plenum later this month, we expect a shift to an entrenched and systematic fight against anti-graft from the ongoing "hitting tigers and flies" campaign. The legal and judicial reforms mean some of these impacts will be more permanent in nature; consequently, the prevailing anti-graft climate is unlikely to abate in 2015.

Changes target existing government and private sectors alike. The main reforms are centered on structural reforms of the government apparatus and SOEs. However, the contagion impact on private enterprises is also noted, which has resulted in a partial paralysis in many areas of economic growth, especially those previously facilitated through local government endorsement. This is expected to result in much lower opportunities for quick riches and fast wealth creation among private enterprises; and by extension, lower spillover growth to industries such as Macau gaming.

Negative operating leverage; EBITDA to fall in 2015

Increasing labour costs, SG&A, and player investment costs are expected to outpace revenue growth in 2015, resulting in significant margin compression and operating deleveraging.

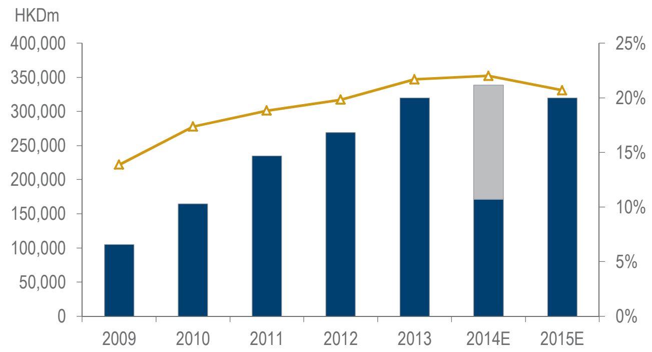
Margins should contract in 2H14

Macau enjoyed multiple years of margin expansion. Macau's average gaming sector EBITDA margin increased from 14% in 2009 to 22% in 1H14, due mainly to: 1) a favourable revenue mix from VIP to mass, and 2) increasing mass table productivity from growth of premium mass segment and rising minimum bets.

Margin contraction expected in 2H14. Against our expected negative GGR growth in 2H14 and 2015, we look for these prevailing trends, resulting in negative operating leverage:

1) 20% YoY increase in base wage inflation.
2) 40-60% YoY increase in staff costs for operators with new openings due to incremental hiring to fully staff new properties 3-6 months prior to their respective openings.
3) SG&A cost pressures, such as outsourced staff costs and fixed hotel operating expenses.
4) Increased player investment, promotion, and marketing costs.

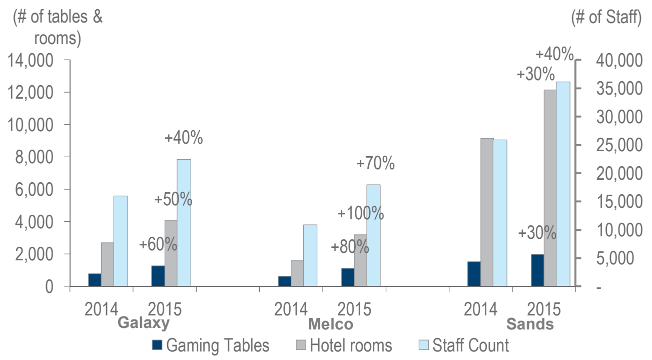
■ Macau Gaming Sector: EBITDA and EBITDA margins (2009-15E)



Source: Company, Daiwa

Operators with the biggest incremental new capacities should feel the most pain in 2015. In our view, opening mega-sized resorts atop a relatively smaller existing operating base in a contracting market is a dangerous proposition. Three of the six casino operators in Macau are slated for new property openings in 2015, including Galaxy (mid-2015), Melco (3Q15) and Sands (late 2015). Of the three, Melco stands to see the biggest increase in capacity (in both tables and hotel rooms).

■ Capacity increases following new openings in 2015



Source: Daiwa, company

Cutting 2014-16E EBITDA by 10-42%. Against slower GGR growth and expected deleveraging, we are reducing our 2014-16E EBITDA forecasts by 10-42%; our heaviest cuts are for operators with 2015 openings.

■ Macau Gaming Sector: Daiwa vs. consensus EBITDA forecasts

		Daiwa (HKDm)			Consensus (HKDm)			Variance		
Operator	Currency	2H14	2015E	2016E	2H14	2015E	2016E	2H14	2015E	2016E
SJM	HKD	3,778	7,484	6,490	4,532	9,654	9,921	-17%	-22%	-35%
MGM	HKD	3,152	6,249	6,558	3,555	7,653	9,089	-11%	-18%	-28%
Sands	USD	11,197	23,547	25,748	12,154	31,051	36,991	-8%	-24%	-30%
Galaxy	HKD	6,346	11,357	14,259	6,701	17,881	21,243	-5%	-36%	-33%
Wynn	HKD	3,517	6,966	8,633	4,791	9,709	13,330	-27%	-28%	-35%
Melco	USD	3,621	9,309	9,701	4,975	12,575	16,801	-27%	-26%	-42%

Source: Bloomberg, Daiwa

Sector cost pressures

No.1: staff costs pressure largely underestimated by consensus

Since the beginning of the year, casino operators have successively announced staff retention programmes including annual bonus payments ("14th month bonus") and different iterations of multi-year retention programmes (one-off cash bonuses in 2017, vested equity and stock option plans). Despite this, we have seen continued and escalating pushback by labour unions demanding higher wages and bonuses.

Wage inflation pressure unlikely to soften in 2015-16. We see wage inflation continuing to rise, driven by: 1) the structural supply shortage of trained and experienced staff in Macau, and 2) increasing demand for staff following the successive casino openings in 2015-17.

20% YoY increase in base staff costs. We forecast base staff costs to increase by 20% YoY for 2015, driven by: 1) 14th-month bonuses for all existing staff, 2) 8-10% YoY wage inflation, and 3) other staff benefits.

Operators with casino openings should see the highest wage inflation and negative operating leverage in 2015. We estimate that operators with new casino openings (Galaxy, Melco, Sands) will see staff costs increase by 40-60% YoY when they begin to fully staff the new properties 3-6 months ahead of each new casino's respective opening.

Among the 6 operators in Macau, 3 are planning to introduce new capacity (Galaxy: mid-2015, Melco: mid-2015, and Sands late 2015) and are most at risk of negative operating leverage and margin erosion. Wynn is also at risk since the operator would have to begin its hiring in 3Q14-4Q15 ahead of Wynn Palace's opening, scheduled for Lunar New Year 2016.

Of the 3 operators with new openings scheduled in 2015, Galaxy has the earliest casino opening, Melco has the lowest base, and Sands has the least productive table yields.

SJM faces the least risk. In our view, SJM faces the lowest risk from labour-cost increases. Our argument is premised upon:

1) 50% of SJM's revenue is derived from satellite casinos, of which it receives 3-5% of revenue; labour and other cost pressures for these casinos are borne by third parties.
2) Its new Cotai property opening is the last among peers (2017); as such, it should bear the least risk in incremental staff costs or rushed hiring.
3) Grand Lisboa has high table yields and faces a lower (relative to other operators) risk of negative operating leverage.

Macau's labour constraints poised to worsen. According to our forecasts, the total number of dealers required to operate all the gaming tables of new casinos opening in 2015-17 would be as high as 16,500.

The unemployment rate in Macau reported as of the end of 2Q14 was 1.7%, which implies that 10,608 Macanese are currently unemployed. Since only Macau residents are permitted to work as dealers and pit bosses, we expect the gap between the labour supply and demand of dealers to widen in Macau in the coming years.

■ **Macau Gaming: new capacities and labour cost increases**

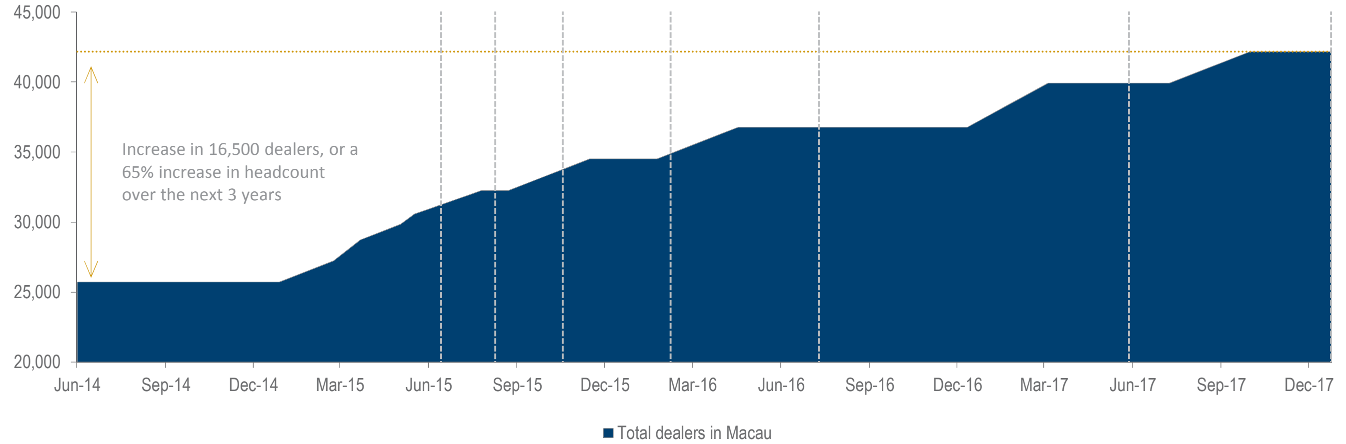
	Galaxy	Melco*	Sands	Wynn	MGM	SJM
Existing Capacity (June 2014)						
Staff Count	16,000	10,896	25,884	7,366	6,010	21,700
Hotel rooms	2,710	1,601	9,156	1,008	588	413
Gaming Tables	771	615	1,529	465	424	1,771
Staff cost reported (USDm)	319	211	526	185	123	374
New Capacities (est. new openings)	**Mid-2015**	**Mid-2015**	**Late-2015**	**Early-2016**	**Mid-2016**	**2,017**
Staff Count	+40%	+70%	+40%	+90%	+130%	+40%
Hotel rooms	+50%	+100%	+30%	+170%	+270%	+480%
Gaming Tables	+60%	+80%	+30%	+110%	+120%	+40%
Estimated labour cost increase 2015 (YoY%)	48%	66%	46%	39%*	20%	20%

** Staff count excludes City of Dreams Manila*

*** Increase from hiring for Wynn Palace in 3Q14-4Q15 prior to Wynn Palace's opening in Chinese New Year 2016*

Source: Daiwa

■ **Dealers in Macau (2H14-2017)**

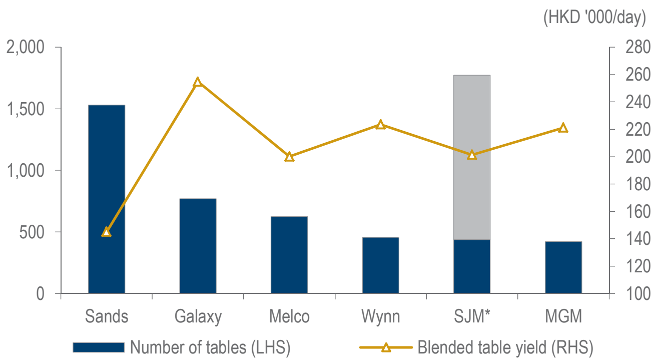


Source: DSEC, DICJ, Daiwa

Sands faces a longer-term structural risk to labour cost increases. Among its peers, we believe Sands faces the highest structural risk of labour-cost increases. Sands currently has: 1) the highest number of self-operated gaming tables among peers, and 2) the lowest per table yield in Macau.

In other words, the operator is incurring the highest commitment of resources (table and labour) to achieve the lowest operating leverage among peers. Its existing cost structure also reflects this, with Sands incurring the highest percentage of labour costs as a percentage of revenue.

■ **Macau Gaming: number of table and blended table yield per operator**



Source: Daiwa
**SJM table yield based on GLB [Grey = SJM excl. GLB]*

No.2: SG&A also at risk of increases and largely overlooked

Outsourced services are also at risk of cost hikes. We see a number of costs that are also at risk of hikes in 2015-16. A number of services, such as hotel security, trash collection, casino cleaning and some non-gaming staffing, has been outsourced to third-party companies and are not included in staffing costs. Currently, SG&A accounts for around 22% of the Macau Gaming Sector's revenue.

In our view, wage inflation for internal staff among casino operators in Macau's labour-constrained market is likely to increase the costs for these outsourced services, which would consequently be reflected in SG&A.

Rigid hotel operating cost structure, especially for operators with third-party managed hotels. Against rising costs and declining average daily rates for hotel rooms, we see very little cost maneuverability for casino operators, especially those with hotels that are managed by third parties (Sands, Galaxy, Melco). These 5-star hotel brands must maintain certain service levels, minimum staff experience and quality levels, and amenities that are unlikely to be compromised in the light of slower GGR growth or lower average daily rates. It is difficult to strip out the exact financial implication of this risk based on public information, but we do highlight this as a potential risk for further operating deleverage.

■ Macau Gaming Sector: hotels and room count

Casino Operator	Property	Hotel Brand	Room count
MGM	MGM Macau	Own brand	600
Galaxy	Galaxy Macau	Banyan Tree	250
		Hotel Okura	500
		Galaxy hotel	1,500
	StarWorld	StarWorld	500
Melco Crown	City of Dreams	Crown Towers	290
		Hard Rock	320
		Grand Hyatt	790
	Altira	Own brand	215
Wynn	Wynn Macau	Wynn	1,000
Sands China	Sands Macao	Own brand	290
	Venetian Macao	Own brand	3,000
	Plaza Macao	Four Seasons	360
	Sands Cotai Central	Conrad	600
		Sheraton	3,900
		Holiday Inn	1,200
SJM	Grand Lisboa	Own brand	430

Source: Daiwa

No.3: player investment costs to rise in the face of mounting competition

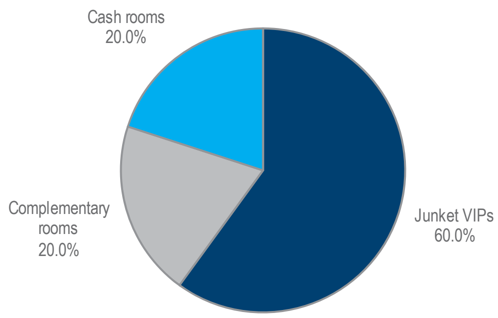
Over the past 2-3 years, each casino operator has been actively building out its customer database and expanding its business through attracting an increasing amount of repeat business from rated players (as opposed to grind mass market players who are more property and operator-agnostic).

Naturally, costs are expected to increase as the need to offer non-gaming complementary services to customers, such as hotel rooms, transportation, and other gaming/non-gaming incentives, rises. We already have seen a progressive increase in promotional allowances from 3.3% of GGR in 2012 to 3.6% by 1H14.

Going forward, all six operators increasing their hotel room supply amid slower growth will likely intensify both competition between casino operators and also against each operator's respective older properties.

Furthermore, with the expected VIP business shrinkage should come a decreasing allocation of hotel rooms to junkets, which would further increase hotel room supply even among existing properties. We estimate that approximately 60% of existing hotel rooms are currently allocated to junkets in Macau. We expect casino operators to be much more aggressive in terms of driving businesses, and by extension, increasing comp-ing activities (which is another way of describing an increase in player reinvestment costs). We forecast promotional costs to increase to around 4% of GGR in 2H15, which is still low compared to 6-7% in Las Vegas.

■ Macau Gaming Sector: average hotel room allocation by the 6 major casino operators



Source: Daiwa

Anecdotally, Sands has already been actively working on this strategy. The operator hired a new hotel management team in 1Q14 to facilitate this.

Earnings, stock pecking order and valuation

Investment thesis

Switching to defensive cost profiles

With the expected lacklustre top-line growth, rising costs, and margin erosion for the industry in 2015, we are shifting our stock preferences to those operators with more defensive cost profiles.

In our view, operators with earlier openings now bear the highest immediate risk of cost increases and the largest potential for negative operating leveraging.

Revised pecking order

Against an expected market contraction, EBITDA decline and margin erosion, we cut our target EV/EBITDA multiples ascribed to existing properties in our SOTP valuation from 7-15x to 7x-11x with the magnitude of cuts depending on the properties' business mix, Peninsula/Cotai exposure, and sensitivity to cost inflation. Our new stock picks are as follows:

■ Macau Gaming Sector: new pecking order

Order	Stock	Rating	Investment thesis
1 (5)	SJM	OP	1) Defensive revenue mix; 50% of group revenue from satellite casinos of which SJM takes 3-5% of revenue; opex incurred borne by third parties 2) Should see the least immediate labour-cost pressures, as it will have the last Cotai new property opening (Lisboa Palace in 2017) 3) Cash-rich and likely to be the only operator able to maintain its current dividend policy in this capex cycle (regular and special dividends) 4) Grand Lisboa has one of the highest VIP table yields as it has the highest mix of quality junkets among its peers 5) Cheap valuation; relatively limited downside risk, in our view
2 (2)	MGM	OP	1) Has the second-to-last new Cotai property opening in early 2016; less labour-cost hike pressure, especially if there are delays in the opening 2) Solid operator with a strong junket mix; mass table yield is also the highest in Macau 3) Small property and small operating base, nimble cost control that is much easier to manage than those of the mega-resorts amid the current market-share contraction
3 (3)	Sands	Hold	1) Cotai property opening in 2015 faces labour-cost pressure but less so than Galaxy and Melco, given Sands' lower incremental capacity increase from the existing higher base 2) Grind mass-centric and best retail offering is attracting tourist headcount, and by extension, gaming dollars 3) High risk of negative operating leveraging, as it has the lowest table yields among peers 4) Recent aggressive table shift to the mass market was largely unsuccessful; further table shifts to the mass market unlikely to create new demand
4 (1)	Galaxy	Hold	1) Earliest new property opening (mid-2015), and thus faces high cost pressures 2) Negative operating leverage from new opening, partially offset by strong VIP and market-leading table yields 3) Best junket management programme; we expect its VIP rolling to outperform peers but also likely to see higher-than-peers top-line pressures due to VIP-heavy business mix
5 (6)	Wynn	UP	1) Likely to see top-line pressure/market-share losses from the expected collapse of the high-end market 2) New Cotai property opening in 2016 (most expensive among peers); less immediate labour cost hike pressure 3) Preopening hiring will also affect the operator in 2015, hit in 3Q14-4Q15 ahead of the opening of Wynn Palace, slated to be at the time of the Lunar New Year in 2016 4) Most highly geared among peers after current capex cycle 5) Most expensive relative to peers
6 (4)	Melco	UP	1) Among the highest increase in table/hotel capacity with Studio City's scheduled opening in 3Q15 likely to be a big negative 2) Expect VIP rolling to underperform that of the industry in 2014-15 due to poor junket mix 3) The underperforming Altira may take time to adjust its segment mix

Source: Daiwa

■ Macau Gaming Sector: summary of earnings and rating changes

	Share Price	Recommendation			Target Price		Implied Upside	New EBITDA (HKDm)			Old EBITDA (HKDm)			EBITDA change		
Operator	(8 Oct.)	New	Old	Currency	New	Old		2H14E	2015E	2016E	2H14E	2015E	2016E	2H14E	2015E	2016E
SJM	15.5	Outperform	Outperform	HKD	16.7	21	8%	3,778	7,484	6,490	4,527	9,616	10,714	-17%	-22%	-39%
MGM	22.5	Outperform	Buy	HKD	23.8	32.1	6%	3,152	6,249	6,558	4,225	8,026	9,372	-25%	-22%	-30%
Sands	42.2	Hold	Buy	HKD	40	60.2	-5%	11,197	23,547	25,748	14,264	31,832	40,027	-22%	-26%	-36%
Galaxy	47.2	Hold	Buy	HKD	45.0	74	-5%	6,346	11,357	14,259	7,747	18,308	22,374	-18%	-38%	-36%
Wynn	25.5	Underperform	Outperform	HKD	22.6	33	-11%	3,517	6,966	8,633	4,527	10,317	14,106	-22%	-32%	-39%
Melco	25.9	Underperform	Buy	USD	23.0	34	-11%	3,621	9,309	9,701	5,337	12,783	16,755	-32%	-27%	-42%

Source: Daiwa, Bloomberg

■ **Dividend stress test**

Operator	SJM	MGM	Wynn	Sands (USD)	Galaxy	Melco (USD)
	Regular dividend policy operators				Special Dividends operators	
Total operating cash flow (2014-17E)	33,653	27,665	26,988	12,746	56,324	4,027
Total capital expenditures (2014-17E)	(30,000)	(20,310)	(45,336)	(3,054)	(58,639)	(2,151)
Net cash position (end-2013)	25,160	3,823	3,748	(281)	9,717	(8)
Dividend (Regular, 2014-17E)	(12,944)	(7,700)	(23,969)	(8,457)	-	-
Regular dividend payout ratio	50%	35%	100%	80%	-	-
Dividend (Special, 2014-17E)	(5,548)	(15,988)	-	(3,823)	(14,345)	(975)
Special dividend payout ratio	22%	73%	-	36%	29%	30%
Dividend (total regular and special, 2014-17E)	(18,492)	(23,688)	(23,969)	(12,280)	(14,345)	(975)
Total payout ratio	72%	108%	100%	116%	29%	30%
Net cash position (end-2017E, regular div only)	15,869	3,478	(38,569)	954	7,402	1,868
Net cash position (end-2017E, regular & special)	10,321	(12,510)	(38,569)	(2,869)	(6,943)	893
Can free cash flow support current dividend policy in its entirety over next three years?	YES	NO	NO	NO	NO	YES

Source: Daiwa

SJM is likely to be the only candidate to see firm dividend yield support over 2014-17. At current share-price levels, the sector is trading at a 3-7% dividend yield, or 2-5% if we exclude the special dividends.

We believe that the operators with regular dividend policies will see some share-price support (Sands, Wynn, MGM and SJM). That said: 1) investors typically do not buy Macau names for their dividend yields, and 2) operators by and large cannot maintain their current dividend payouts because this is likely to lead to cash burn.

We have performed a simple stress test on each operator's ability to maintain its respective dividend payout by examining each operator's total operating cash flow and capex budgets between 2014 and 2017 (above).

Of the operators with regular dividend policies, we do not believe they will be able to maintain their current payouts in their entirety (both regular and special dividends). The only exception to this is SJM, which is cash rich and has the latest new property opening in 2017 (and the slowest cash burn) among its peers.

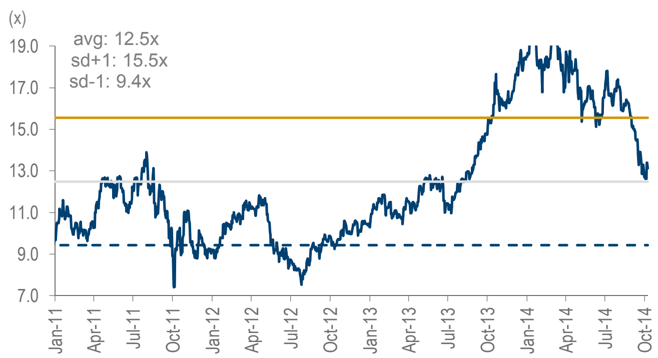
It should be pointed out that Galaxy does not have a regular dividend policy and does not have the necessary capital to maintain its current special dividend policy. However, this conclusion may change if the operator alters the capex plan for Galaxy Phases 3 and 4 (currently slated to open in 2016-18).

Valuation

Valuation looks unattractive; share prices likely have not factored in 2015E earnings fall. For 2015, the consensus still expects: 1) 16% YoY EBITDA growth for the sector, and 2) a 60bps EBITDA margin expansion to 23%. The sector is still trading near historical levels, at 2015E EV/EBITDA multiple of 15x and at 12-month forward PER of 22x.

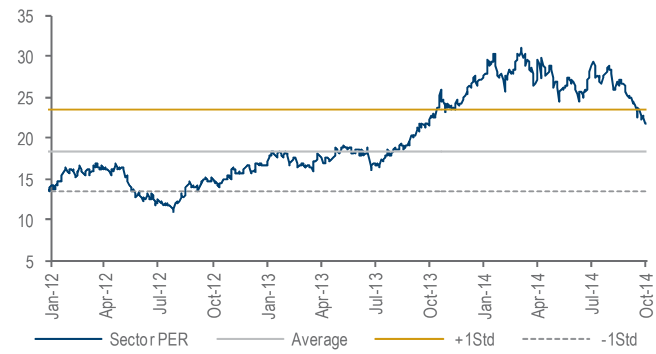
We argue that the sector may still see a further derating, given that it saw an earnings CAGR of 36% over the 2008-1H14 period, rather than the 8% YoY EBITDA decline that we expect for 2015. Our EBITDA forecast is also 26% below the consensus, as we expect higher increases in labour and promotional costs will lead to negative operating leverage and further cuts to consensus earnings in the coming months, which could drive a potential derating.

■ **Macau Gaming Sector: EV/EBITDA multiple**



Source: Bloomberg, Daiwa

■ **Macau Gaming Sector: weighted-average 12-month forward PER (x)**



Source: Bloomberg, Daiwa

Assessing the downside from here. The sector market cap has lost 38% since its peak in January 2014. However, it is still trading at 11x 2015 EV/EBITDA (based on the Bloomberg-consensus forecast), which is higher than the 2012 trough of 7.5x EV/EBITDA. If the sector reverts to this trough multiple (7.5x), this would imply 30% downside to the current market cap.

In our worst-case scenario, if we apply the 7.5x to our 2015 EBITDA forecast for the sector, which is 27% below the consensus, this would imply 49% downside to the current market cap. This would push the sector dividend yield to 11% (market-cap weight among the 4 operators with a regular dividend policy), which is an unlikely scenario.

That said, our analysis suggests that most operators with a regular dividend policy (other than SJM) are unlikely to maintain their current dividend policies in their entirety during the 2015-17 capex cycle amid this contracting market environment (see page 15). As such, any cut in the operators' special dividend policies could drive a derating.

Risks to our sector call. The main upside risk to our Neutral sector call would be if China's economic fundamentals were to improve unexpectedly. A secondary upside risk would be positive investor sentiment over the Hong Kong-Shanghai Stock Connect.

The main downside risk to our sector rating would be if the China government cracks down even further in terms of its anti-graft measures. Secondary risks would be if VIP GGR were to decline by more than we expect, and any further structural shifts in the tourist mix to Macau. Unexpected visa policy changes would also have a negative impact.

■ **Target multiples**

Operator	Share price (8 Oct)	Recommendation	Currency	TP	New implied 2015E multiples (x)		Prev. implied 2015E multiples (x)		Historical 1-yr fwd EV/EBITDA (x)			Historical 12m fwd PER(x)		
					EV/EBITDA	PER	EV/EBITDA	PER	Peak	Trough	Average	Peak	Trough	Average
SJM	15.5	Outperform	HKD	16.7	9.8	16.2	9.8	14.6	15.7	3.2	8.1	19.4	8.4	13.6
MGM	22.5	Outperform	HKD	23.8	13.5	17.9	14.2	17.6	17.2	6.0	10.3	21.4	6.4	12.9
Sands	42.2	Hold	HKD	40	12.9	20.3	15.5	18.2	17.2	9.1	12.7	34.3	12.0	20.4
Galaxy	47.2	Hold	HKD	45	14.8	21.1	16.4	19.9	23.0	2.3	9.2	46.8	8.5	19.3
Wynn	25.5	Underperform	HKD	22.6	19.1	26.9	17.9	20.7	17.4	7.5	11.7	24.1	10.4	16.9
Melco	25.9	Underperform	USD	23	13.6	15.8	13.4	7.5	42.5	5.4	11.3	28.4	11.3	19.6

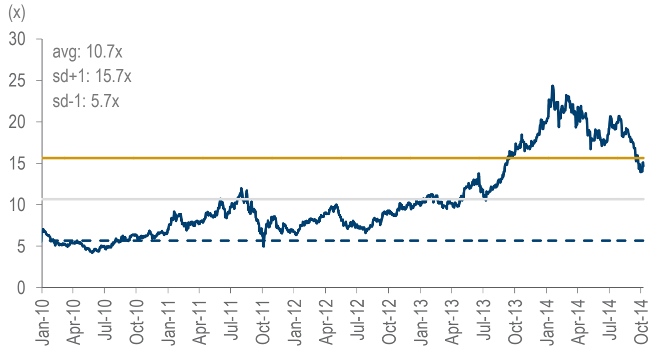
Source: Daiwa

■ Macau and global gaming sector: valuation summary

Company	Ticker	Share price (local cur.)	Market cap (USDbn)	Rating	EV/EBITDA (x)		EBITDA growth YoY (%)		PER (x)		2-yr EPS CAGR (%)	Div. yield (%)		FCF (%)	
					2014E	2015E	2014E	2015E	2014E	2015E	2013-15E	2014E	2015E	2014E	2015E
Macau															
Galaxy	27 HK	47.15	25.6	Hold	13.5	16.6	8.4	(16.7)	18.1	22.1	(5.5)	n.a.	n.a.	1.5	n.a.
Melco Crown	MPEL US	25.10	14.3	Underperform	12.6	12.9	(9.0)	1.9	22.2	45.2	(30.5)	n.a.	n.a.	n.a.	n.a.
MGM China	2282 HK	22.50	11.0	Outperform	12.6	13.8	4.9	(6.4)	15.2	16.9	(2.7)	2.3	2.1	0.3	n.a.
Sands China	1928 HK	42.15	43.6	Hold	13.9	14.8	9.4	(4.9)	19.7	21.5	(4.0)	4.1	3.7	3.8	2.6
SJM	880 HK	15.28	11.1	Outperform	7.5	9.0	(5.2)	(9.0)	12.3	14.8	(13.4)	5.9	4.9	4.9	n.a.
Wynn Macau	1128 HK	25.45	17.0	Underperform	16.9	20.7	(7.5)	(14.4)	19.7	30.3	(24.7)	4.1	2.6	n.a.	n.a.
Macau - market cap weighted avg					**13.4**	**15.2**	**3.1**	**(8.4)**	**18.6**	**24.5**	**(10.9)**	**4.1**	**3.4**	**2.2**	**0.9**
Asia															
Paradise Group (KR)	034230 KS	34,650.00	3.2	Outperform	17.3	12.0	11.5	38.9	22.6	18.2	26.9	1.0	1.0	3.7	4.5
Grand Korea Leisure (GKL)	114090 KS	41,550.00	2.6	Outperform	9.6	8.5	8.4	8.4	17.0	14.8	12.3	2.6	2.9	5.2	11.1
Kangwon Land	035250 KS	34,300.00	7.3	Outperform	10.0	8.1	34.8	19.6	17.6	15.1	27.6	2.9	3.4	2.3	5.8
Genting (Malaysia)	GENT MK	9.30	10.6	NR	7.0	6.3	7.3	7.8	18.1	16.1	5.3	0.8	0.8	5.4	7.1
Asia - market cap weighted avg						**9.6**	**7.8**	**16.5**	**15.7**	**18.4**	**15.9**	**15.9**	**1.7**	**1.9**	**4.2**
US															
Las Vegas Sands	LVS US	61.90	49.8	NR	11.1	10.3	19.2	5.6	17.0	15.5	17.3	3.2	3.5	5.9	6.5
Wynn Resorts	WYNN US	183.29	18.6	NR	13.3	12.9	5.4	4.6	22.2	20.9	7.2	2.7	3.1	(0.5)	1.1
MGM Resorts	MGM US	21.97	10.8	NR	11.1	10.2	17.6	7.2	36.1	32.9	66.8	0.0	0.0	3.8	(0.9)
Caesars Entertainment Corp	CZR US	11.25	1.6	NR	12.9	12.3	265.2	6.7	n.a.	n.a.	41.3	0.0	n.a.	n.a.	n.a.
US - market cap weighted avg						**11.6**	**11.0**	**20.7**	**5.6**	**20.4**	**18.8**	**22.1**	**2.6**	**2.9**	**4.0**
Australia															
Crown Resorts Ltd	CWN AU	13.55	8.6	NR	14.5	13.7	(2.8)	5.9	14.9	13.0	9.7	2.9	3.1	2.9	2.7
Echo Entertainment Group Ltd	EGP AU	3.31	2.4	NR	7.5	7.2	10.1	4.1	16.3	15.5	6.1	2.9	3.1	4.0	3.2
SKYCITY Entertainment Group Ltd	SKC AU	3.24	1.7	NR	9.1	8.8	16.9	10.4	16.0	14.6	8.3	5.5	5.6	n.a.	n.a.
Australia - market cap weighted avg						**12.4**	**11.8**	**2.2**	**6.2**	**15.3**	**13.6**	**8.8**	**3.2**	**3.4**	**2.7**

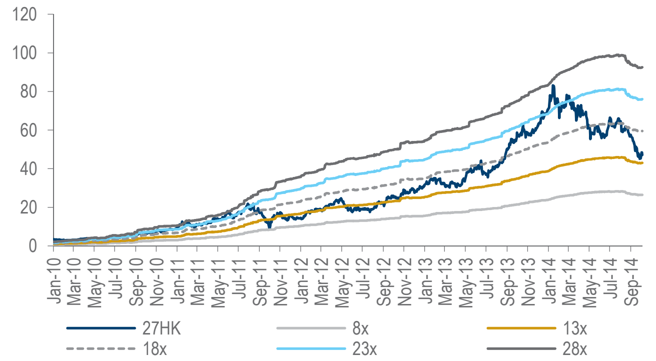
Source: Bloomberg (unrated companies), Daiwa forecasts (rated companies)
Note: based on share prices as of 9 October 2014 (US-listed based on 8 October 2014)

■ **Galaxy: EV/EBITDA**



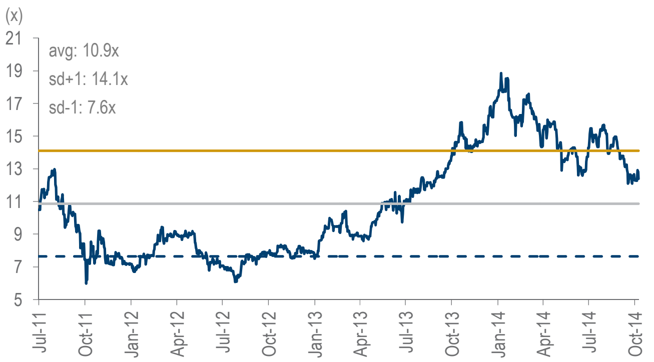
Source: Daiwa, Bloomberg

■ **Galaxy: 12-month forward rolling PER (x)**



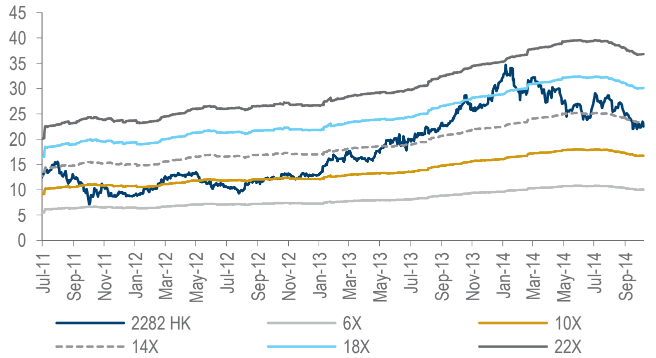
Source: Daiwa, Bloomberg

■ **MGM China: EV/EBITDA**



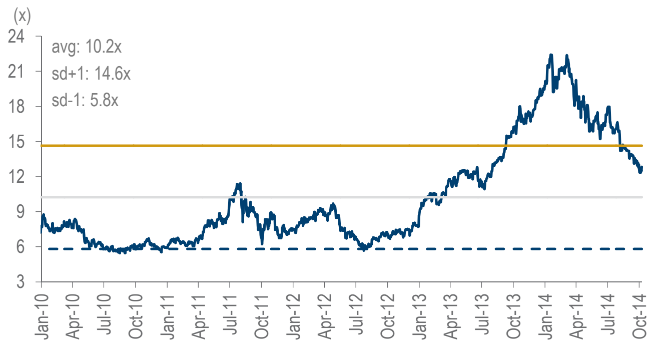
Source: Daiwa, Bloomberg

■ **MGM China: 12-month forward rolling PER (x)**



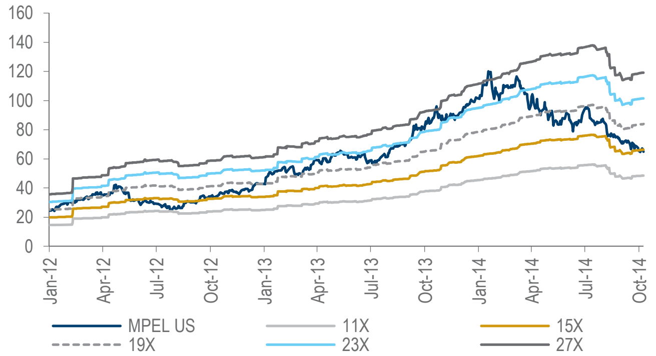
Source: Daiwa, Bloomberg

■ **Melco: EV/EBITDA**



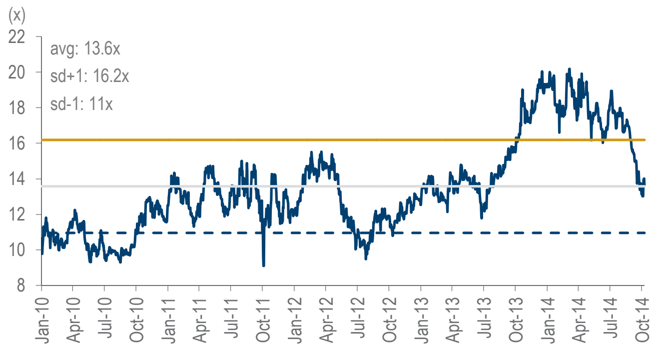
Source: Daiwa, Bloomberg

■ **Melco:12-month forward rolling PER (x)**



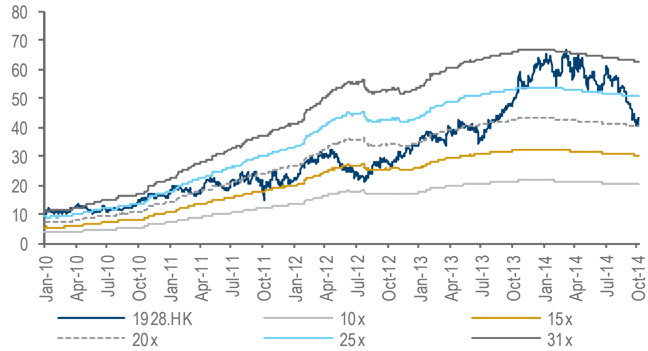
Source: Daiwa, Bloomberg

■ **Sands China: EV/EBITDA**



Source: Daiwa, Bloomberg

■ **Sands China: 12-month forward rolling PER (x)**

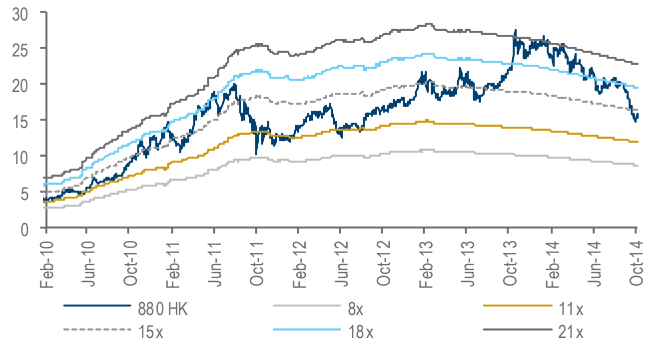


Source: Daiwa, Bloomberg

■ **SJM: EV/EBITDA**

Source: Daiwa, Bloomberg

■ **SJM: 12-month forward rolling PER (x)**

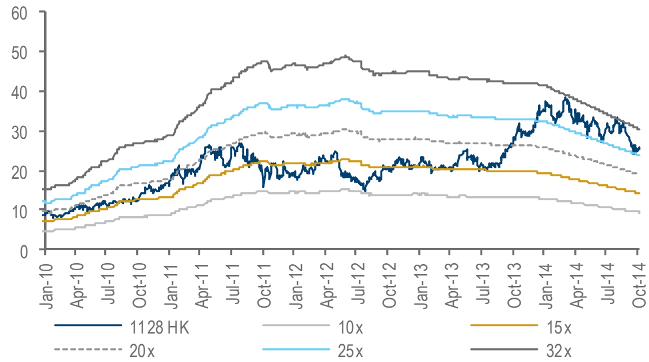


Source: Daiwa, Bloomberg

■ **Wynn: EV/EBITDA**

Source: Daiwa, Bloomberg

■ **Wynn: 12-month forward rolling PER (x)**



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"1": the security could outperform the local index by more than 15% over the next six months.
"2": the security is expected to outperform the local index by 5-15% over the next six months.
"3": the security is expected to perform within 5% of the local index (better or worse) over the next six months.
"4": the security is expected to underperform the local index by 5-15% over the next six months.
"5": the security could underperform the local index by more than 15% over the next six months.

Additional information may be available upon request.

Japan - additional notification items pursuant to Article 37 of the Financial Instruments and Exchange Law
(This Notification is only applicable where report is distributed by Daiwa Securities Co. Ltd.)

If you decide to enter into a business arrangement with us based on the information described in materials presented along with this document, we ask you to pay close attention to the following items.

- In addition to the purchase price of a financial instrument, we will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction.
- In some cases, we may also charge a maximum of ¥ 2 million (including tax) per year as a standing proxy fee for our deposit of your securities, if you are a non-resident of Japan.
- For derivative and margin transactions etc., we may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by us.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.
  *The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with us.

Corporate Name:	Daiwa Securities Co. Ltd.
	Financial instruments firm: chief of Kanto Local Finance Bureau (Kin-sho) No.108
Memberships:	Japan Securities Dealers Association, The Financial Futures Association of Japan
	Japan Securities Investment Advisers Association
	Type II Financial Instruments Firms Association