

# China / Hong Kong Equity Radar

# Galaxy Entertainment

Version 1 | Bloomberg: 27 HK Equity | Reuters: 0027.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

30 Sep 2019

**BUY** (Initiating coverage)

Last Traded Price ( 27 Sep 2019): HK\$48.30 (HSI : 25,955)

Price Target 12-mth: HK\$62.48 (29.4% upside)

**Analyst**

Mavis HUI+852 36684188, mavis\_hui@db.com

## Price Relative



## Forecasts and Valuation

FY Dec (HK\$m)	2018A	2019F	2020F	2021F
Turnover	55,211	56,198	58,236	64,225
EBITDA	16,681	17,223	17,876	19,910
Pre-tax Profit	13,614	14,126	14,411	16,526
Net Profit	13,507	13,891	14,171	16,251
Net Profit Gth (Pre-ex) (%)	28.6	2.8	2.0	14.7
EPS (HK\$)	3.13	3.21	3.27	3.75
EPS Gth (%)	27.8	2.5	2.0	14.7
Diluted EPS (HK\$)	3.11	3.20	3.26	3.74
DPS (HK\$)	0.91	0.94	0.95	1.09
BV Per Share (HK\$)	14.40	16.71	19.03	21.69
PE (X)	15.4	15.1	14.8	12.9
P/Cash Flow (X)	15.1	13.9	12.1	10.4
P/Free CF (X)	19.3	17.5	14.8	12.7
EV/EBITDA (X)	12.2	12.0	11.2	9.6
Net Div Yield (%)	1.9	1.9	2.0	2.3
P/Book Value (X)	3.4	2.9	2.5	2.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	21.7	19.2	17.2	17.3
Earnings Rev (%)		New	New	New
Consensus EPS (HK\$)		3.09	3.23	3.74
Other Broker Recs:		B:22	S:1	H:5

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

## Good prospects despite near-term volatility

- 2019 should be unexciting along with slower macro conditions. Recent demonstrations in HK have also affected visitation, including the PRC visitors who normally go to Macau via HK.
- Medium-term prospects could stay positive, supported by China's rising per capita income and the increasing demand for leisure & entertainment. Galaxy's ongoing expansion of its integrated resorts to include more MICE facilities & new hotel rooms should also beef up operating capacity and performance.
- Initiate coverage with a BUY on 12-month horizon; TP HK\$62.48

**Good efforts on the mass segment.** Macau gaming operators increasingly focus on the (premium) mass segment to enhance profitability and minimize impacts from volatile VIP earnings. Operators like Galaxy that still has land to add MICE facilities ahead could better complement existing operations. Aside from more offerings, plans for new hotel complexes would mean better capacity to grow, as hotel accommodation has been the bottle neck for developing (premium) mass segment during the high seasons. Its latest refurbishment of Galaxy Macau and StarWorld Macau also improves resort attractiveness.

**Visitation issues could gradually resolve.** A slowdown in arrival numbers to Macau amid the HK unrest and lingering Sino-US trade tension, and costs of renovation and expansion of its integrated resorts could all result in decelerating earnings momentum in near-term. Nevertheless, its overall enhancement programme should attract more visitors in medium-term. Further shifts towards the mass segment should also improve its revenue-mix, profitability and business sustainability.

### Valuation:

Our 12-month TP of HK\$62.48 is based on DCF valuation (8.3% WACC, 0.5% perpetual growth), which implies ~16.6x FY21 PE.

### Key Risks to Our View:

Weaker economic growth in China; intensifying competition; slower gaming revenue growth; unfavourable gov't regulations.

### At A Glance

Issued Capital (m shrs)	4,333
Mkt Cap (HK\$m/US\$m)	209,264 / 26,691
Major Shareholders (%)	
City Lion Profits Corp.	22.5
Lui (Che Woo)	14.3
Capital Research Global Investors	9.5
Free Float (%)	53.7
3m Avg. Daily Val. (US\$m)	62.56
GLCS Industry: Consumer Discretionary / Consumer Services	
Bloomberg ESG Disclosure Score (2017)^	36
- Environmental / Social / Governance	35 / 23 / 52

^ refer to back page for more information



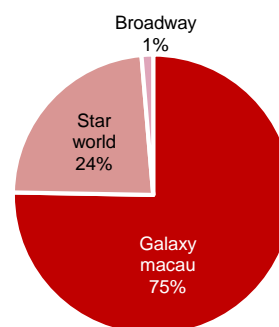
### Growth Prospects

**Good track record.** Galaxy's revenue had grown at a CAGR of 9.5% during FY15-18, and was able to increase its adjusted EBITDA margin to 30.5% in FY18 from 22.7% in FY15. However, growth is expected to slowdown in 2019 due to a slump in visitations from Hong Kong during 2H19. Operations could improve gradually ahead especially by 2H20 on a lower base.

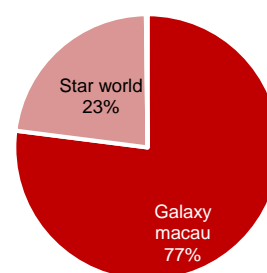
**Medium-term prospects remain intact.** The Macau casino industry is mainly influenced by footfall from Hong Kong and Mainland China. Chinese GDP per capita income is poised to grow in the coming years leading to higher consumer spending. Nevertheless, the current unrest in Hong Kong and a slower Chinese economy have direct impacts on overall gross gaming revenue (GGR). According to the Gaming Inspection and Coordination Bureau, in both July and August 2019, the GGR of Macau declined y-o-y by 3.5% and 8.6%, respectively. We believe once consumer sentiment improves and the Hong Kong demonstrations subside, the gaming industry is expected to steer ahead. Additionally, a revival in the economy, favourable government policies including potential visa relaxation for Mainland visitors to Macau, and more infrastructural developments such as the HK-Zhuhai-Macau Bridge and extended coverage of the high-speed rail to boost visitor arrivals would all support business outlook of the company.

**Big plans ahead.** Galaxy's property enhancement programme is progressing as planned, with the refurbishment of both Galaxy Macau and Starworld Macau budgeted at c.HK\$1.5 bn. Besides, the development of Phases 3 & 4 in Cotai, Macau will include ~4500 new hotel rooms, multi-purpose arena (e.g. MICE), retail and casinos. The company also currently explores into opening world-class integrated gaming resorts in Japan together with potential partners. Other projects in the pipeline could include a lifestyle resort in Hengqin that should benefit from the extension of Guangzhou-Zhuhai Intercity railway lines.

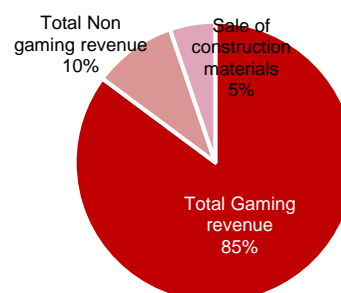
### Revenue breakdown – Property (2018)



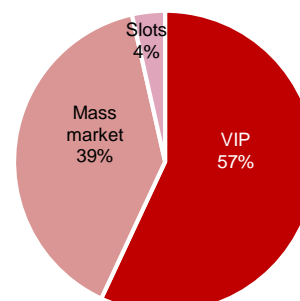
### Adjusted EBITDA breakdown – Property (2018)



### Revenue breakdown – by type (2018)



### Gross Gaming Revenue breakdown – by type (2018)



Source: Company, DBS HK

## Galaxy Entertainment

### Balance Sheet:

Galaxy has a strong balance sheet, with net cash position of >HK\$4bn as of Jun 2019. The company is also in a good liquidity position, with current ratio of 0.8x in FY18 and operating cash inflows of well over HK\$10bn per year.

### Share Price Drivers:

Barring the near-term impacts of Chinese economic slowdown along with Sino-US trade war and the Hong Kong unrest, Galaxy is expected to perform well in the coming years. Ongoing development plans in Asia are expected to support the company's market share in the region. The current enhancement programme of Galaxy Macau and StarWorld Macau, as well as further expansion in Cotai, Macau should all be key catalysts to drive growth.

### Key Risks:

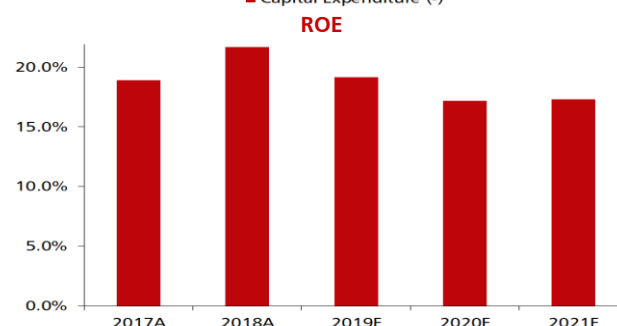
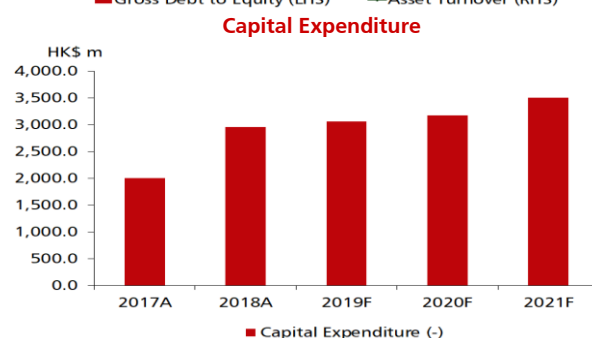
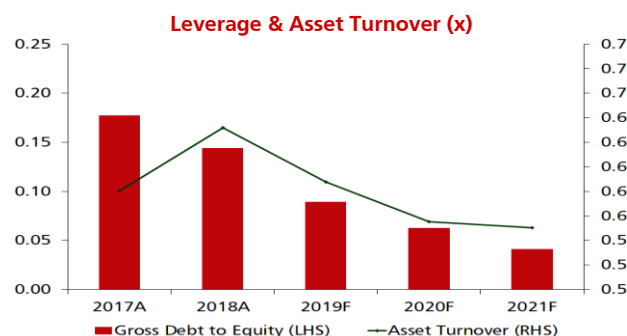
Ongoing trade conflicts between China and the US may affect China's economic growth in the short-term. Demonstrations in Hong Kong have also led to a slowdown in tourism resulting in lower visitor numbers to Macau. All these could impact consumer sentiment and result in lesser footfall in Macau from Mainland China and Hong Kong. The Macau gaming industry is regulated by The Gaming Inspection and Coordination Bureau; any regulatory changes may impact Galaxy's revenue growth and profitability. Rising competition amongst casino operators could also affect the company's margins.

### Environment, Social, Governance:

Galaxy has improved its overall ESG score from 12.8 in 2012 to 36.0 in 2017, signifying the company's effort to meet environmental compliance. In July 2019, Galaxy voluntarily joined Non-Mandatory Central Provident Fund (CPF) scheme to improve its existing employee pension scheme. It is also involved in numerous activities promoting responsible gaming in Macau along with Social Welfare Bureau of the Macau. Through Galaxy Entertainment Group Foundation which was established in 2015, the company has also been participating in philanthropic activities.

### Company Background

Galaxy Entertainment Group ("Galaxy") is one of the leading resorts, hospitality and gaming companies in Macau. The company is amongst the original concessionaries in Macau with services across integrated resorts, retail, dining, hotel and gaming facilities. Galaxy operates three resorts - Galaxy Macau, StarWorld Macau and Broadway Macau. Specifically, Galaxy Macau comprises five top hotels with ~3,600 rooms and hosts approximately 200 luxury and retail brands, while Starworld Macau provides over 500 guestrooms and suites and Broadway Macau offers ~320 rooms and suites and a ~3000 seat Broadway theatre.



Source: Company, DBS HK

## Segmental Breakdown (HK\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
<b>Revenues (HK\$ m)</b>					
Star world	14,180	17,049	16,687	16,998	18,541
Galaxy macau	44,570	52,759	52,424	54,871	61,007
Broadway	514	595	661	697	743
Commissions & Incentives	(10,623)	(15,192)	(12,974)	(14,330)	(16,066)
<b>Net Revenue</b>	<b>48,641</b>	<b>55,211</b>	<b>56,198</b>	<b>58,236</b>	<b>64,225</b>
<b>Adjusted EBITDA (HK\$ m)</b>					
Star world	3,000	3,810	3,871	3,944	4,357
Galaxy macau	11,100	12,871	13,263	13,882	15,496
Broadway	10	32	44	50	57
Others	117	111	112	111	111
<b>Total</b>	<b>14,217</b>	<b>16,824</b>	<b>17,290</b>	<b>17,987</b>	<b>20,021</b>
<b>Adjusted EBITDA Margins (%)</b>					
Star world	21.2	22.3	23.2	23.2	23.5
Galaxy macau	24.9	24.4	25.3	25.3	25.4
<b>Total</b>	<b>29.2</b>	<b>30.5</b>	<b>30.8</b>	<b>30.9</b>	<b>31.2</b>

Source: Company, DBS HK

## Income Statement (HK\$ m)

FY Dec	2017A	2018A	2019F	2020F	2021F
Revenue	48,640	55,211	56,198	58,236	64,225
Cost of Goods Sold	(23,261)	(26,819)	(27,130)	(27,939)	(30,619)
<b>Gross Profit</b>	<b>25,379</b>	<b>28,392</b>	<b>29,068</b>	<b>30,297</b>	<b>33,606</b>
Other Opng (Exp)/Inc	(14,931)	(15,027)	(15,213)	(16,208)	(17,426)
<b>Operating Profit</b>	<b>10,448</b>	<b>13,365</b>	<b>13,855</b>	<b>14,090</b>	<b>16,179</b>
Other Non Opng (Exp)/Inc	244	388	450	450	450
Associates & JV Inc	0	0	0	0	0
Net Interest (Exp)/Inc	(64)	(139)	(179)	(129)	(103)
Dividend Income	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>10,628</b>	<b>13,614</b>	<b>14,126</b>	<b>14,411</b>	<b>16,526</b>
Tax	(113)	(43)	(148)	(151)	(174)
Minority Interest	(11)	(63)	(87)	(88)	(101)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>10,504</b>	<b>13,507</b>	<b>13,891</b>	<b>14,171</b>	<b>16,251</b>

## Growth

Revenue Gth (%)	17.1	13.5	1.8	3.6	10.3
EBITDA Gth (%)	39.5	20.9	3.2	3.8	11.4
Opg Profit Gth (%)	65.3	27.9	3.7	1.7	14.8
Net Profit Gth (%)	67.2	28.6	2.8	2.0	14.7

## Margins &amp; Ratio

Gross Margins (%)	52.2	51.4	51.7	52.0	52.3
Opg Profit Margin (%)	21.5	24.2	24.7	24.2	25.2
Net Profit Margin (%)	21.6	24.5	24.7	24.3	25.3
ROAE (%)	18.9	21.7	19.2	17.2	17.3
ROA (%)	12.5	15.5	14.5	13.5	13.9
ROCE (%)	15.7	18.5	17.0	15.7	16.2
Div Payout Ratio (%)	24.3	29.3	29.2	29.2	29.2
Net Interest Cover (x)	163.5	96.3	77.4	109.3	156.7

Source: Company, DBS HK

**Balance Sheet (HK\$ m)**

FY Dec	2017A	2018A	2019F	2020F	2021F
Net Fixed Assets	36,815	36,280	35,976	35,363	35,132
Invt in Associates & JVs	1,521	1,633	1,633	1,633	1,633
Other LT Assets	25,378	31,157	42,750	47,250	51,750
Cash & ST Invt	17,600	14,505	10,057	15,372	22,707
Inventory	171	190	192	198	217
Debtors	1,962	1,860	1,894	1,962	2,164
Other Current Assets	368	1,758	3,117	3,117	3,117
<b>Total Assets</b>	<b>83,815</b>	<b>87,384</b>	<b>95,618</b>	<b>104,896</b>	<b>116,721</b>
ST Debt	9,685	8,804	6,505	5,205	3,905
Creditors	17,237	14,828	14,999	15,447	16,929
Other Current Liab	113	107	144	144	144
LT Debt	259	251	18	18	18
Other LT Liabilities	504	563	908	912	943
Shareholder's Equity	55,482	62,280	72,406	82,444	93,955
Minority Interests	534	551	638	726	827
<b>Total Cap. &amp; Liab.</b>	<b>83,815</b>	<b>87,384</b>	<b>95,618</b>	<b>104,896</b>	<b>116,721</b>
Non-Cash Wkg. Capital	(14,850)	(11,127)	(9,941)	(10,314)	(11,575)
Net Cash/(Debt)	7,656	5,450	3,533	10,149	18,784
Debtors Turn (avg days)	14.7	12.3	12.3	12.3	12.3
Creditors Turn (avg days)	316.0	230.3	230.4	233.4	229.8
Inventory Turn (avg days)	3.1	2.9	2.9	3.0	2.9
Asset Turnover (x)	0.6	0.6	0.6	0.6	0.6
Current Ratio (x)	0.7	0.8	0.7	1.0	1.3
Quick Ratio (x)	0.7	0.7	0.6	0.8	1.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	20.1	32.7	46.9	60.8	89.2

Source: Company, DBS HK

**Cash Flow Statement (HK\$ m)**

FY Dec	2017A	2018A	2019F	2020F	2021F
Pre-Tax Profit	10,628	13,614	14,126	14,411	16,526
Dep. & Amort.	3,349	3,316	3,367	3,786	3,731
Tax Paid	(113)	(43)	(148)	(151)	(174)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	5,066	(1,769)	(1,225)	373	1,261
Other Operating CF	(411)	(1,334)	(1,113)	(1,090)	(1,326)
<b>Net Operating CF</b>	<b>18,520</b>	<b>13,784</b>	<b>15,007</b>	<b>17,328</b>	<b>20,019</b>
Capital Exp.(net)	(1,999)	(2,958)	(3,063)	(3,174)	(3,500)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	92	256	0	0	0
Other Investing CF	(9,210)	(8,536)	(10,480)	(3,410)	(3,174)
<b>Net Investing CF</b>	<b>(11,117)</b>	<b>(11,238)</b>	<b>(13,543)</b>	<b>(6,584)</b>	<b>(6,674)</b>
Div Paid	(2,548)	(3,956)	(4,052)	(4,133)	(4,740)
Chg in Gross Debt	3,715	(864)	(2,532)	(1,300)	(1,300)
Capital Issues	330	358	287	0	0
Other Financing CF	(16)	0	384	4	31
<b>Net Financing CF</b>	<b>1,480</b>	<b>(4,462)</b>	<b>(5,913)</b>	<b>(5,429)</b>	<b>(6,009)</b>
Currency Adjustments	0	0	0	0	0
Chg in Cash	8,884	(1,916)	(4,448)	5,316	7,335
Opg CFPS (HK\$)	3.14	3.60	3.75	3.92	4.33
Free CFPS (HK\$)	3.86	2.51	2.76	3.27	3.81

Source: Company, DBS HK

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*\*Share price appreciation + dividends*

Completed Date: 30 Sep 2019 10:29:38 (HKT)  
Dissemination Date: 30 Sep 2019 15:19:33 (HKT)

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**DBS Bank (Hong Kong) Limited**13<sup>th</sup> Floor One Island East, 18 Westlands Road, Quarry Bay, Hong Kong

Tel: (852) 3668-4181, Fax: (852) 2521-1812

**DBS Regional Research Offices**

**HONG KONG**

**DBS Bank (Hong Kong) Ltd**  
**Contact: Carol Wu**  
 13th Floor One Island East,  
 18 Westlands Road,  
 Quarry Bay, Hong Kong  
 Tel: 852 3668 4181  
 Fax: 852 2521 1812  
 e-mail: dbsvhk@dbs.com

**MALAYSIA**

**AllianceDBS Research Sdn Bhd**  
**Contact: Wong Ming Tek (128540 U)**  
 19th Floor, Menara Multi-Purpose,  
 Capital Square,  
 8 Jalan Munshi Abdullah 50100  
 Kuala Lumpur, Malaysia.  
 Tel.: 603 2604 3333  
 Fax: 603 2604 3921  
 e-mail: general@alliancedbs.com

**SINGAPORE**

**DBS Bank Ltd**  
**Contact: Janice Chua**  
 12 Marina Boulevard,  
 Marina Bay Financial Centre Tower 3  
 Singapore 018982  
 Tel: 65 6878 8888  
 Fax: 65 65353 418  
 e-mail: equityresearch@dbs.com  
 Company Regn. No. 196800306E

**INDONESIA**

**PT DBS Vickers Sekuritas (Indonesia)**  
**Contact: Maynard Priajaya Arif**  
 DBS Bank Tower  
 Ciputra World 1, 32/F  
 Jl. Prof. Dr. Satrio Kav. 3-5  
 Jakarta 12940, Indonesia  
 Tel: 62 21 3003 4900  
 Fax: 6221 3003 4943  
 e-mail: indonesiaesearch@dbs.com

**THAILAND**

**DBS Vickers Securities (Thailand) Co Ltd**  
**Contact: Chanpen Sirithanarattanukul**  
 989 Siam Piwat Tower Building,  
 9th, 14th-15th Floor  
 Rama 1 Road, Pathumwan,  
 Bangkok Thailand 10330  
 Tel. 66 2 857 7831  
 Fax: 66 2 658 1269  
 e-mail: research@th.dbs.com  
 Company Regn. No 0105539127012  
 Securities and Exchange Commission, Thailand