

Neptune Group Limited (70 HK)

25 July 2012



Blooming Junket Leader

Leveraging on prominent growth of Macau VIP gaming market and potential expansions, Neptune Group Limited (“NGL”) is well positioned to increase its earnings capacity and extend coverage into all casino operators in Macau.

Top junket in Macau

NGL entered into gaming promotion business through acquiring profit streams from licensed gaming promoters since 2007. Currently, NGL has a promotion networks from 51 VIP tables at The Venetian, Sands Macao and Galaxy StarWorld, which generated around HK\$14-15 billion of monthly rolling chip turnover in 2011.

Potential expansion

NGL is planning to acquire more profit streams from promotion operations to expand into other casino operators. We believe a larger coverage of casino network will help the company to increase earnings capacity and capture the overall performance of VIP gaming segment. We are positive on the story, given promising growth of the industry and undemanding valuation expected for the target operations.

Valuation

The current share price of HK\$0.163 implies a FY2013E P/E of approximately 2.0x, which is at a discount of 80% to comparable listed gaming players, which are trading at average of 10x. Being the only listed pure gaming promotion play with sizable network, NGL is attractive at current levels. We value the stock at a range of 7-9x FY13E P/E, implying a significant potential upside.

China/Hong Kong

Rating Buy

Price (24 Jul 12) HK\$ 0.163

Market Cap HK\$627M
US\$80.4M

Sector Gaming

Research Analyst

Elisa Chan
elisa.chan@ftfinancial.com.hk

Please refer to the important disclosure and analyst certification information at the end of this report.

Forecast Summary

(HKD '000, 30 th Jun)	<u>2011a*</u>	<u>2012e</u>	<u>2013e</u>
Revenue	414,787	428,313	1,374,478
Net profit (HK\$)	356,584	430,006	1,362,058
Attributable profit (HK\$)	193,265	275,128	494,753
Fully diluted EPS (HK cents)	5.03	7.15	8.93

Note: Company information assuming successful expansions into new casinos.

Source: FT Securities estimates

Assuming potential expansions are funded by issuance of new shares.

* Cruise ship leasing business excluded.

Business Overview

NGL's business is closely tied with gaming promotion industry in Macau. Its profit network covers casinos including Sands China (1928.HK)'s The Venetian and Sands Macao and Galaxy Entertainment (27.HK)'s StarWorld since 2007. NGL's network is currently one of the largest in Macau in terms of turnover, earnings, no. of VIP rooms and tables.

Promotion Network

NGL owns profit streams from a promotion network of 51 VIP tables at 3 casinos, among which 16 tables are located in The Venetian, 12 in Sands Macao and 23 in Galaxy StarWorld, generating around HK\$ 14-15 billion of monthly rolling chip turnover in 2011.

Revenue Model

Through its wholly-owned subsidiaries, NGL generates revenues by sharing commissions with licensed gaming promoters under the "Profit Agreements", where NGL is entitled to share generally 0.4% of rolling chip turnover generated at VIP rooms on pro rata basis of interest holding of corresponding profit agreement.

Figure 1: Current Profit Network

	Casino	Agreement	No of VIP Tables	Attr. Interest	Monthly Rolling Chip T/O (HK\$ m)		Revenue Sharing
					FY11A	FY12E	
				(%)			(%)
1	The Venetian	Hao Cai	12	85	3,400-3,500	3,800-3,900	0.4
2	The Venetian	Neptune Ouro	4	85	1,100-1,200	1,200-1,300	0.4
3	Sands	Hou Wan	12	30	3,500-3,600	3,400-3,500	0.35
4	StarWorld	Hoi Seng	6	20	1,300-1,400	1,000-1,100	0.4
5	StarWorld	Lucky Star	17	20	4,700-4,800	5,000-5,100	0.4
	Total		51		14,000-14,500	14,400-14,900	

Source: Company estimates

* Hou Wan interest has increased to 30% from 20% since Jan 2012. And prior to Jan 2012, the revenue sharing was at 0.4%.

^ New Star interest has increased to 20% from 10% since Jun 2012.

Seasoned Management

The company has a team of seasoned management with more than 25 years of experience in international gaming industry. Key management had taken executive roles previously at Vegas, Trump Taj Mahal and Caesars Palace at Atlantic City, overseeing operational, administrative and marketing activities throughout Asia, Middle East, Europe and Latin America.

Time for the leap

Potential expansions in the pipeline

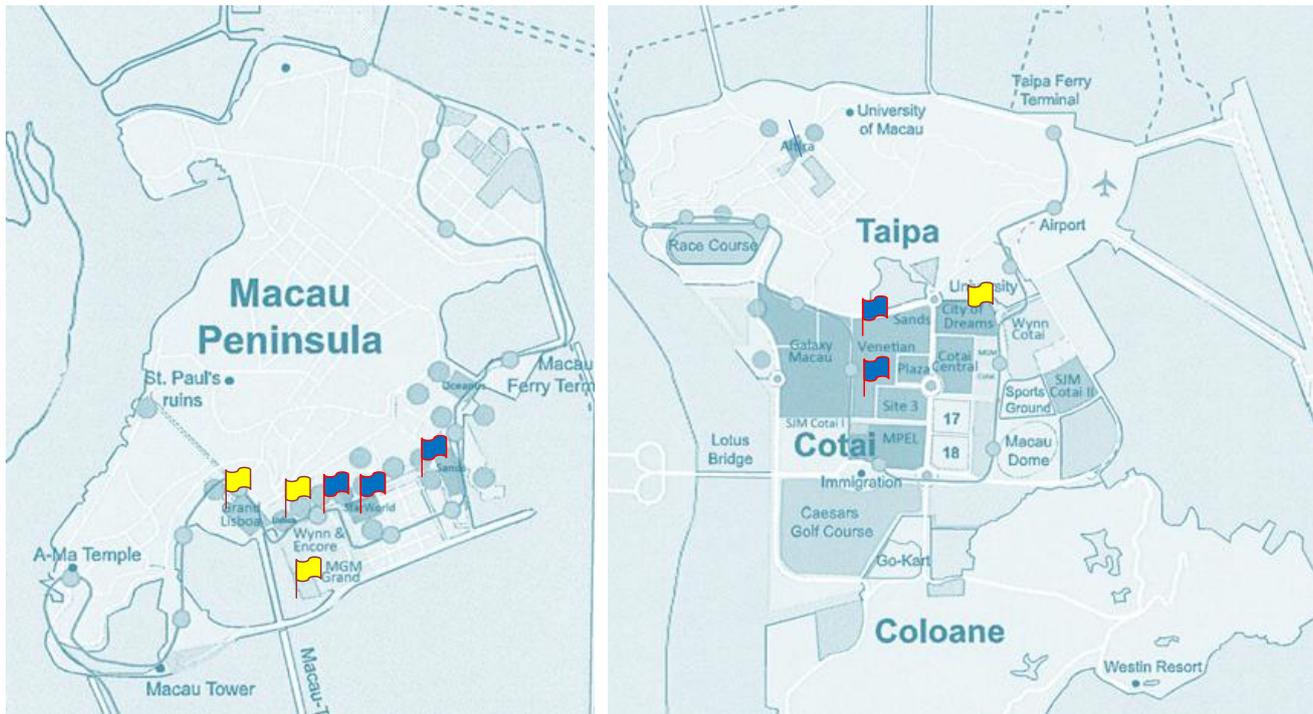
We expect that NGL will continue to acquire profit streams from gaming promotion operations to strengthen its position as a market leader in Macau gaming promotion industry. A larger coverage of casino network will help the company to increase earnings capacity and capture the overall performance of VIP gaming segment.

Target gaming promotion business

The existing promotion network covers only 2 casino operators, namely Sands China (1928.HK) and Galaxy Entertainment (27.HK). The company plans to further expand into promotion operations under other 4 casino operators, namely Wynn Macau (1128.HK), MGM China (2282.HK), SJM (880.HK) and Melco Crown Entertainment (6883.HK). If assuming NGL aims at total coverage of all 6 casino operators, the promotion network will be increased substantially from the current 50 to 150 VIP tables, and monthly rolling chip volume may increase from HK\$ 15 billion to HK\$ 45 billion.

Assuming that NGL acquires no less than 20-30% stakes in the profit stream from each junket operation, we estimate that NGL will need additional funding of approximately US\$ 60 million. The corresponding profit attributable to NGL from the potential expansion is expected to reach HK\$250 million in FY2013E (2-3Q contribution) and HK\$320 million in FY2014E (full-year contribution). Under such scenario, the total post-expansion net profit to NGL is expected to be approximately HK\$ 494 million in FY2013E and HK\$ 680 million in FY2014E, representing 80% and 38% yoy growth, respectively.

Figure 2: Existing & Potential Casino Network



-  Existing Casinos
- Sands Macao
 - The Venetian
 - Galaxy StarWorld

-  Potential Acquisition Targets
- Grand Lisboa (SJM)
 - Wynn & Encore (Wynn)
 - MGM Grand (MGM China)
 - City of Dreams (Melco Crown)

Source: Company estimates

Valuation

Leveraging on the potential coverage in new casinos in Macau, we believe NGL will be able to strengthen the leading position. The current share price of HK\$0.163 implies a FY2013E P/E of around 2.0x, which is at a discount of 80% to comparable listed gaming players' average of 10x. Being the only listed pure gaming promotion play with sizable network, NGL looks attractive at current level. We value the stock at a range of 7-9x FY13E P/E, implying a significant potential upside.

Figure 3: Gaming Players Valuation Metrics

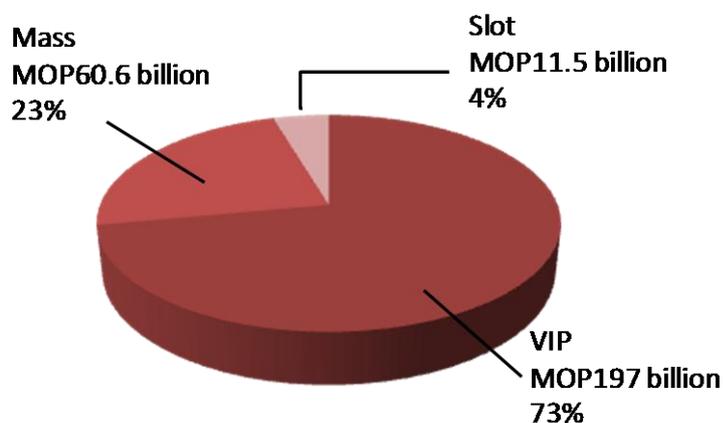
Company	Stock Code	Mkt Cap (HK\$m)	PER	PER	PER	EV/	EV/	EV/	EBITDA	EBITDA	EBITDA	Net	Net	Net
			(x)	(x)	(x)	EBITDA	EBITDA	EBITDA	Margin	Margin	Margin	Profit	Profit	Profit
			FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E
HK-listed Players														
SANDS CHINA LTD	1928 HK	178,736	21.0	15.7	11.1	15.7	11.4	8.6	31.3	29.9	31.1	23.2	21.4	23.9
WYNN MACAU LTD	1128 HK	78,747	13.6	11.8	10.3	11.2	9.6	8.5	23.7	26.7	26.9	20.1	22.4	22.9
GALAXY ENTERTAINMENT GROUP	127 HK	75,893	25.6	12.3	10.3	17.4	9.5	8.3	11.3	15.1	15.5	7.4	11.2	12.1
SJM HOLDINGS LTD	880 HK	78,095	14.7	12.2	10.9	9.5	8.0	7.1	8.6	9.3	9.4	7.0	7.8	8.1
MELCO CROWN ENTERTAINMENT	16883 HK	40,765	n/a	13.0	10.7	8.0	6.9	6.3	20.8	22.7	22.9	7.5	9.9	11.1
MGM CHINA HOLDINGS LTD	2282 HK	39,824	12.4	9.7	8.6	8.0	7.4	6.7	24.1	23.7	23.8	16.4	19.1	19.4
Simple Avg			17.5	12.4	10.3	11.6	8.8	7.6	20.0	19.2	19.4	42.7	83.0	115.3
Mkt Cap Weighted Avg			17.1	13.3	10.6	13.0	9.6	8.0	21.9	22.5	23.1	18.5	22.9	27.1
US-listed Players														
LAS VEGAS SANDS CORP	LVS US	245,025	22.5	14.5	12.6	12.2	9.6	8.6	33.9	34.6	33.9	20.0	18.4	18.7
WYNN RESORTS LTD	WYNN US	72,516	19.2	17.5	15.2	8.6	8.9	8.3	29.2	28.4	28.6	15.7	11.0	11.8
MELCO CROWN ENTERTAINME-AD	MP EL US	40,130	17.8	13.2	11.4	7.9	7.1	6.7	20.8	22.3	21.9	7.5	10.0	10.7
MGM RESORTS INTERNATIONAL	MGM US	35,653	1.5	n/a	n/a	15.5	10.5	9.4	16.4	20.2	21.5	41.2	n/a	n/a
Simple Avg			15.3	15.1	13.1	11.0	9.0	8.3	25.1	26.4	26.5	21.1	13.1	13.7
Mkt Cap Weighted Avg			19.5	15.0	13.0	11.4	9.3	8.4	30.1	30.9	30.6	19.9	16.0	16.4

Source: Bloomberg, 25th Jul, 2012

Junket Industry in Macau

Gaming promoters or junket operators contributes over 90% of VIP GGR, while VIP GGR has averaged 69.4% of Macau’s total GGR in the past 5 years.

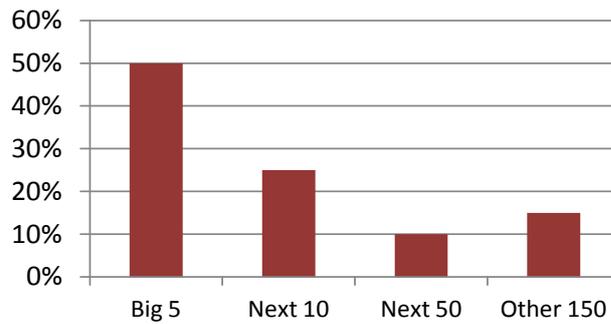
Figure 4: 2011 Macau Gross Gaming Revenue Compositions



Source: Company estimates

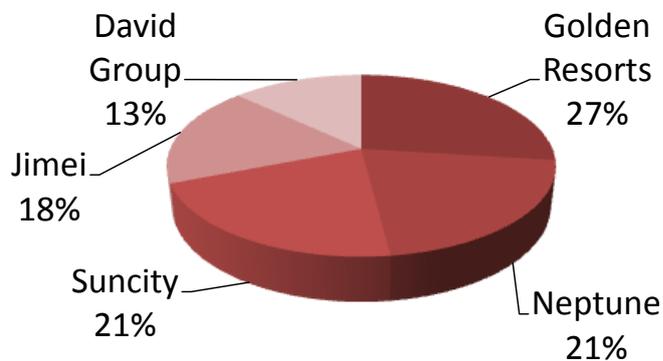
Macau’s Junket industry is highly fragmented with approx. 200 to 250 junket operators currently. However, junket market is dominated by large operators. The Big 5 junkets shares 50% of total market. The following 10 junkets collectively represent 25% of total market.

Figure 5: Market Share of Macau Junket operators



Source: Company estimates

Figure 6: Market share within Big 5 operators



Source: Company estimates, May 2011

Macau

Macau consists of the Macau Peninsula itself and the islands of Taipa and Coloane, which are now connected by landfill forming the Cotai Strip. It is situated 60 kilometres (37 mi) southwest of Hong Kong and 145 kilometres (90 mi) from Guangzhou. With growing tourist arrivals and average spending, gaming has gradually become the pillar of Macau’s economy, which is contributing 40.9% of total GDP in 2010 compared with 25.9% in 2000.

Figure 7: Macau Economic Snapshot

Snapshot of Macau	2000	2011
Area	25.4 km ²	29.7 km ²
Population	437,900	557,400
GDP	50 billion MOP	292 billion MOP
GDP per capita	119,911 MOP	531,723 MOP
Gaming as % of GDP	25.9%	40.9% <small>(2010)</small>
Gross Gaming Revenue	16 billion MOP	268 billion MOP
Tourist Arrivals	9.2 million	28 million
Unemployment Rate	6.8%	2.1%
Average Gaming Spending	1,739 MOP	9,571 MOP
No. of casinos	15	32

Source: DICJ, DSEC

Sustainable Visitor Growth

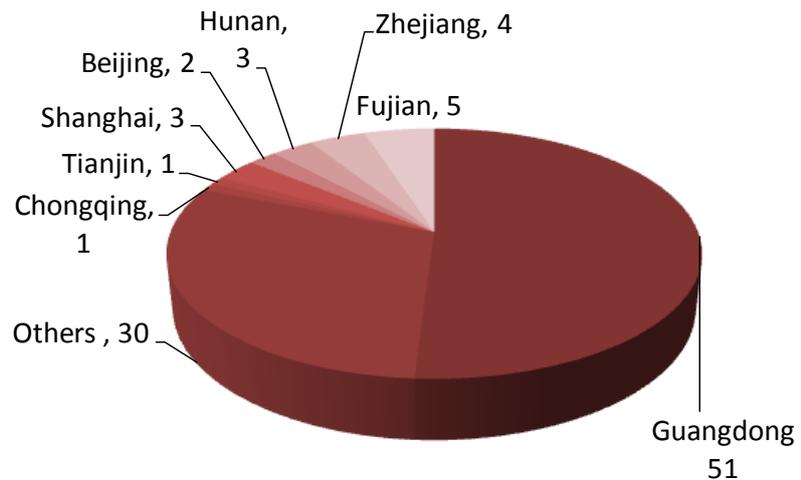
Visitors from China and Hong Kong made up 84.8% of total visitors in 2011. Among all the mainland Chinese visitors, about 51% are from Guangdong province.

Figure 8: 2011 Macau visitors by region

2011 Visitors by Region	Number of visitors	%
China Continental	16,162,747	57.7
Hong Kong	7,582,923	27.1
Taiwan, China	1,215,162	4.3
Korea	398,807	1.4
Japan	396,023	1.4
Malaysia	324,509	1.2
Singapore	280,602	1.0
Americas	310,608	1.1
Europe	251,748	0.9
Oceania	127,983	0.5
Africa and others	24,864	3.2
Total	28,002,279	100.0

Source: DSEC

Figure 9: 2H2011 Chinese visitors by province



Source: Company estimates

Infrastructure underway

Infrastructure projects have taken off to support the visitor growth from China/Hong Kong and other regions as well:

From China/Hong Kong:

Guangzhou–Zhuhai Intercity Railway

- The GZ Intercity Railway links Zhuhai to the provincial capital, Guangzhou with a 40 minutes ride on China Railway High-speed.
- The main line between the cities is 117km long with 18 stations.
- The railway has partly started operations since Jan 2011.
- An extension of the line toward Zhuhai-Macau cross-border terminal is expected to complete before 2015.

Expansion of Gongbei cross-border terminal

- The “Gongbei” terminal is the largest terminal from mainland China to Macau currently open from 7am to midnight.
- The terminal has a designed daily flow capacity of 150,000 passengers, but is running at actual average of 240,000.
- New terminal is under construction with designed capacity of 350,000~400,000 per day with half electronic checking channels.
- Expansion work is expected to complete in 2013.

Hong Kong-Zhuhai-Macau Bridge

- Construction formally began on 15 December 2009 and projected completion is in 2015-16.

Figure 10: Guangzhou-Zhuhai Intercity Railway Map



Source: www.lifeofguangzhou.com

- The bridge will shorten the distance from Hong Kong to Macau and Zhuhai from 60km to 30km, and reduce the journey time to within 30 minutes.

From the region

Macau International Airport

- Macau International Airport connects 28 destinations in the region including Tokyo, Seoul, Singapore, Taipei, Kuala Lumpur, Manila, Bangkok, Shanghai, Beijing and etc.
- The airport is located on Taipa Island and is 15 minutes away from the Macau Ferry Terminal, 20 minutes from the Barrier Gate and only 10 minutes away from the COTAI Frontier Post.

New Airlines and Runway

- The Macau government is spending 6 billion MOP to build the 3rd runway to raise capacity from 6 million to 25 million visitors per year.
- New airlines are joining the hub and new routes are opening very recently, to achieve total of 21 airlines and 31 destination.

Figure 11: New Destinations from Macau

Airline	Destination	Joining Date
Mandarin Airlines	Taichung	April 2012
Vietnam Airline	Danang	April 2012
Air Asia	Chiang Mai	July 2012
Air Busan	Busan	July 2012
Thai Smile Airlines	Bangkok	July 2012

Source: HK Wenweipo

Private jet service

According to the management, NGL is planning to introduce private jet liners to serve VIP customers starting from 1H2013. The fleet will consist of 3-5 jets, providing excellent experience all the way including:

- Access of designated parking lot and private air terminal
- No security lines
- Convenient, stress-free check-in handled by attentive staff
- Comfortable accommodations and champagne while you wait to board your flight
- Personal ground transportation directly to and from hotels
- Baggage handling directly to your room

Key Drivers

- Double digit growth of VIP segment of Macau gaming market supports strong organic growth for the existing gaming promotion operations;
- NGL has the market leading position and exclusive right to VIP rooms and facilities;
- Potential expansion will increase coverage of casinos;
- Potential coverage of all 6 casino operators will fully reflect overall performance of VIP gaming segment of Macau.

Risks

We have identified possible slowdown of Macau VIP market as the key concern pertinent to the company. Retaining competitive sub-junkets may also pose challenge to the operations.

Disclaimer

This report has been prepared by FT Securities Limited ("FT Securities") solely for the purpose of supplying information to the clients of FT Securities and/or its affiliates to whom it is distributed. This report is not, and should not be construed as, a solicitation or offer to buy or sell any securities or related financial products.

This report has been prepared by FT Securities solely from publicly available information. The information contained herein is believed to be reliable but has not been independently verified. FT Securities makes no guarantee, representation or warranty, and FT Securities and/or its affiliates, directors, employees or agents accepts no responsibility or liability whatsoever, as to the accuracy, completeness or appropriateness of such information or for any loss or damage arising from the use or further communication of this report or any part thereof. Information contained herein may not be current due to, among other things, changes in the financial markets or economic environment. Opinions reflected in this report are subject to change without notice.

This report does not constitute, and should not be used as, a substitute for, tax, legal or investment advice. This report has been prepared without regard to the individual financial circumstances, needs or objectives of the persons who receive it. The securities and investments related to the securities discussed in this report may not be suitable for all investors. Readers should independently evaluate particular investments and strategies, and seek the advice of a financial adviser before making any investment or entering into any transaction in relation to the securities mentioned in this report.

FT Securities has no legal responsibility to any investor who directly or indirectly receives this material. Investment decisions are to be made by and remain as the sole responsibility of the investor. Investment involves risks, the price of securities may go down as well as up, and under certain circumstances investors may sustain total loss of investment. Past performance should not be taken as an indication or guarantee of future performance. Unless otherwise attributed, forecasts of future performance represent analysts' estimates based on factors they consider relevant. Actual performance may vary. Consequently, no express or implied warranty can be made regarding future performance.

FT Securities and its affiliates, their directors, officers, employees or clients may have or have had interests or positions in the securities, derivatives of such securities or other securities issued by companies mentioned in this report for their own account or the accounts of others, or enter into transactions contrary to any recommendations contained herein, and may also perform or seek to perform broking and other investment or securities related services for the companies whose securities are mentioned in this report as well as other parties generally.

Restrictions on Distribution

This report is not directed to, or intended for distribution to or use by, any person who is a citizen or resident of, or entity located in, any locality, territory, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to or restricted by law or regulation. Persons or entities into whose possession this report comes should inform themselves about and observe such restrictions.

Analyst Certification

Each research analyst listed on the cover page of this report certifies that the view expressed in this research report accurately reflect the analyst's personal views about the subject security(ies) and company and that no part of his/her compensation was, is, or will be, directly or indirectly, related to any specific recommendation or view expressed in this research report.

As of the date of this report, the research analyst listed on the cover page of this report, or his/her associate(s), does not have any interest (including any direct or indirect ownership of securities, arrangement for financial accommodation or serving as an officer) in the company covered in this report, knows or has reason to know of any conflict of interest at the time of publication of this research report that could influence the research analyst's views in the report.

Stock Ratings

FT Securities' investment recommendations are based on Absolute Total Return, which is the sum of the expected price appreciation and dividend yield. Rating definitions are as described below:

STRONG BUY (>20% total return over the next three months)

BUY (>15% total return over the next 12 months)

HOLD (0-15% total return over the next 12 months)

SELL (negative total return over the next 12 months)

Company Disclosures

FT Securities has not been party to any agreement in the past 12 months for the provision of investment banking services to the company covered in this research report. FT Securities may expect to receive or intends to seek compensation relating to the provision of placing of securities services to this company in the next 3 months or in the future.

All Rights Reserved 2013. This document may not be altered, reproduced or redistributed, or passed on to any other party, in whole or in part, without the prior written consent of FT Securities Limited.