

SKYCITY

NEUTRAL

Investor Day — Consistent Hand

SKYCITY's (SKC) Investor Day provided considerable detail, largely reinforcing prior messages and priorities, and FY20 EBITDA guidance was retained (albeit with mix shifts). SKC offers a solid dividend yield, earnings growth potential post major projects (although we remain cautious on Adelaide returns); while near-term disruption and cost inflation are constraints. The NZICC fire also adds some uncertainty (which is unlikely to be resolved any time soon). NEUTRAL.

Recent trading — strength in NZ offsetting weakness in Adelaide

Prior FY20 guidance was reiterated for “some” growth in EBITDA on a base of NZ\$303m — broadly consistent with our current forecasts. However, recent trading shows a mix shift — with its NZ properties ahead of expectations, while Adelaide continues to disappoint (disruption and new initiatives not driving the anticipated market share improvement) and IB turnover is down -10% (not helped by a strong comparative and win rate above theoretical).

EBITDA and cash results will remain the best measures for comparison to expectations, peers, and history in the short to medium-term as NPAT is clouded by project accounting and now — for FY20, various decisions around accounting treatment (particularly ability to capitalise costs) relating to the NZICC fire. At this stage we have not made any change to our Auckland project capex timing or associated earnings given material uncertainty on the extent of the delay.

Other key take-outs

- **Challenging backdrop reiterated:** Economic conditions and cost inflation.
- **Adelaide — focus turning to execution:** The material transformation, scale and complexity of the project is evident. Attention now turns to execution on the earnings uplift required (project EBITDA of ~A\$50m; property EBITDA of ~A\$75m) to meet its return hurdles (ROIC target of 9%). While the opportunity has been well articulated and we can see various areas of upside potential, Adelaide has underwhelmed over history which adds caution. SKC has noted it will take time to deliver (“3–4 years to reach potential”). Timelines and EBITDA indications appear modestly slower relative to our expectations.
- **NZICC fire — still a lot of unknowns, key near-term issue is reduced carparking:** Material delay to completion is inevitable, but timing is unknown at this point. The key implications for earnings are (1) timing of hotel opening, (2) carparks (reduced capacity currently), (3) visitation / disruption. At this stage NZICC capex is unchanged and SKC appears confident in its insurance arrangements.
- **No new growth projects:** A number of options are being evaluated, however, any material projects appear unlikely near-term.
- **Balance sheet in good shape:** Headroom provides optionality.
- **Near-term margin pressure:** From new openings (Adelaide and Auckland projects) and establishing new businesses (online). This isn't new, albeit suggests margins will be under pressure longer than we anticipated.

Investment View

SKC has a casino monopoly and significant licence term in all its key markets. A slowing macro environment and cost inflation present near-term headwinds, while a solid dividend yield and share buyback provides share price support. NEUTRAL.

NZX Code	SKC
Share price	NZ\$3.85
Target price	NZ\$4.00
Risk rating	Medium
Issued shares	675.8m
Market cap	NZ\$2,602m
Average daily turnover	678.8k (NZ\$2,598k)

Share Price Performance



Financials: June	19A	20E	21E	22E
NPAT* (NZ\$m)	173.0	150.9	154.9	156.2
EPS* (NZc)	25.6	22.4	22.6	22.4
EPS growth* (%)	0.9	-12.5	0.8	-0.9
DPS (NZc)	20.0	20.0	20.0	20.0
Imputation (%)	100	100	100	100

Valuation (x)	19A	20E	21E	22E
EV/EBITDA	8.8	10.2	9.7	9.0
EV/EBIT	12.0	14.4	14.1	13.0
PE	15.0	17.2	17.1	17.2
Price / NTA	7.3	17.0	13.0	n/a
Cash dividend yield (%)	5.2	5.2	5.2	5.2
Gross dividend yield (%)	7.2	7.2	7.2	7.2

*Historic and forecast numbers based on underlying profits

Chelsea Leadbetter, CFA

chelsea.leadbetter@forsythbarr.co.nz

+64 4 495 5262

Investment summary

SKYCITY (SKC) is one of the largest gaming operations in Australasia. Earnings and valuation are driven by Auckland, which makes up ~70% of group EBITDA. SKC has two major growth projects underway in Auckland and Adelaide which are large, complex, and challenging, but directly relate to its core expertise. The macro backdrop is supportive in Auckland, albeit tailwinds are beginning to slow, and challenging in Adelaide. With SKC trading at a discount to the NZ market and broadly in line with its five-year average, our rating is NEUTRAL.

Business quality

- **Monopoly assets:** SKC has a casino monopoly in all its markets and significant term on its exclusive casino licences.
- **Increasingly capital intensive platform,** given a fairly mature industry and a need to continually diversify and refresh its offering to retain relevance and drive visitation.

Earnings and cashflow outlook

- **Consumer confidence:** Consumer activity levels in its key Auckland market are robust but are more challenging in Adelaide. There are some early indications the macro backdrop is weakening both domestically and internationally for SKC.
- **Project execution:** Two major capital projects are underway in Auckland and Adelaide. Achieving a satisfactory return on capital is the challenge given the substantial capital being spent. Adelaide in particular raises questions given perennial disappointment from the property through history.

Financial structure

- **Gearing:** SKC has committed to a BBB- credit rating and 'efficient capital allocation' is a key strategic priority. There are a number of moving parts influencing gearing with capex for its two capital projects, asset divestments (carparks, Darwin), a share buyback programme and future growth plans to build out destination precincts surrounding its casinos.
- **Solid yield and share buy-back:** SKC offers a solid dividend yield, which we view as sustainable (with upside risk after project completion). SKC also has a share buy-back programme in place for up to 5% of its shares.

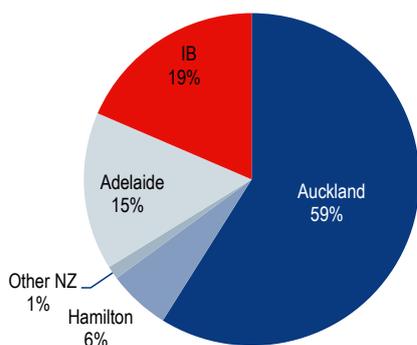
Risk factors

- **Gaming regulation:** Unexpected regulatory and taxation changes.
- **Mature local gaming market:** The local grind gaming market is not only mature but vulnerable to changing entertainment spending patterns.

Company description

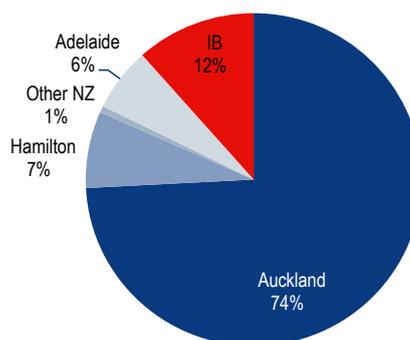
SKYCITY Entertainment Group is the major tourism and leisure company in NZ and one of the largest gaming operations in Australasia. Its key assets are major casino operations in Auckland, Adelaide, Hamilton and Darwin that also include hotel, resort, conference and International VIP gaming facilities. SKYCITY is undertaking a major redevelopment and expansion of the Adelaide Casino and has finalised an agreement with the NZ Government for the development of the NZ International Convention Centre in return for a range of regulatory concessions.

Figure 1. Revenue breakdown FY19 (cont. operations)



Source: Company reports, Forsyth Barr analysis

Figure 2. EBITDA breakdown FY19 (cont. operations)



Source: Company reports, Forsyth Barr analysis

Figure 3. Substantial Shareholders

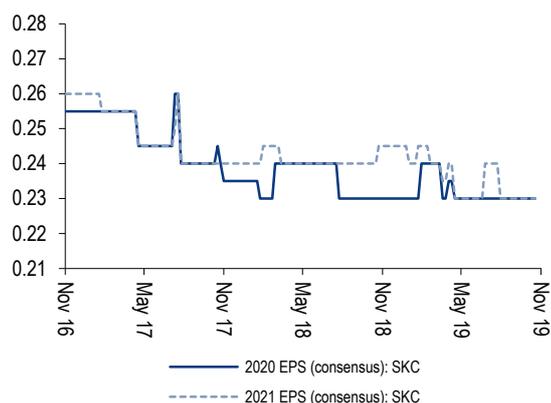
Shareholder	Latest Holding
Sumitomo Mitsui Trust Holdings	10.0%
Investor Mutual	8.4%
Lazard	7.5%
Commonwealth Bank of Australia	7.0%
BlackRock Investment Management	6.1%
The Vanguard Group	5.3%

Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

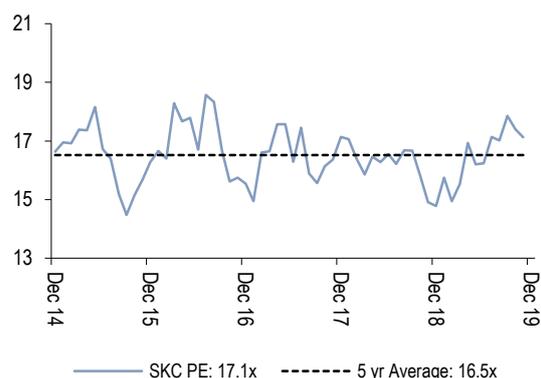
Figure 4. International Compco's

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash D/Yld
<i>(metrics re-weighted to reflect SKC's balance date - June)</i>										
			(m)	2020E	2021E	2020E	2021E	2020E	2021E	2021E
SKYCITY	SKC NZ	NZ\$3.85	NZ\$2,602	17.2x	17.1x	10.1x	9.3x	14.2x	13.6x	5.2%
Crown Resorts	CWN AT	A\$12.47	A\$8,444	23.3x	22.4x	10.8x	10.0x	16.6x	15.2x	4.8%
Tabcorp Holdings	TAH AT	A\$4.73	A\$9,580	23.5x	21.9x	11.8x	11.3x	16.6x	15.8x	4.9%
Star Entertainment Grp/The	SGR AT	A\$4.70	A\$4,311	17.7x	16.8x	9.0x	8.6x	13.7x	13.0x	4.9%
Genting Malaysia Bhd	GENM MK	RM3.27	RM18,487	14.4x	13.9x	7.8x	7.4x	13.6x	12.4x	4.0%
Kangwon Land Inc	035250 KS	KRW30200.00	KRW6,461,003	17.3x	14.9x	8.3x	7.9x	9.1x	8.6x	3.3%
Compco Average:				19.2x	18.0x	9.5x	9.1x	13.9x	13.0x	4.4%
EV = Current Market Cap + Actual Net Debt				SKC Relative:	-11%	-5%	+6%	+3%	+2%	+4%

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (SKC) companies fiscal year end

Figure 5. Consensus EPS Momentum


Source: Forsyth Barr analysis, Bloomberg

Figure 6. 12 Month Forward PE


Source: Forsyth Barr analysis

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