

SKYCITY

Another Count of the Cash

CHELSEA LEADBETTER CFA

 chelsea.leadbetter@forsythbarr.co.nz
 +64 4 495 5262

OUTPERFORM

The backdrop and restrictions for re-opening is becoming clearer for SKYCITY's (SKC) New Zealand properties, however, the demand recovery path remains highly uncertain. SKC has managed costs and cash well during closure, and better than we had initially anticipated. This will remain a key near-term area of focus to match what we expect to be a slow demand recovery, particularly while substantial restrictions are in place (i.e. NZ's Alert Level 2). There is no shortage of challenges for SKC to navigate in the months ahead and we expect to see some battle scars, however, its asset base and long-term monopoly casino licences continue to provide comfort of value above current market pricing.

NZX Code	SKC	Financials: Jun/	19A	20E	21E	22E	Valuation (x)	19A	20E	21E	22E
Share price	NZ\$2.55	NPAT* (NZ\$m)	173.0	53.3	58.1	132.2	EV/EBITDA	6.2	12.2	10.8	7.4
Target price	NZ\$3.30	EPS* (NZc)	25.6	7.9	8.5	18.9	EV/EBIT	8.4	23.9	21.0	11.5
Risk rating	Medium	EPS growth* (%)	0.9	-69.1	7.1	n/a	PE	10.0	32.2	30.1	13.5
Issued shares	667.2m	DPS (NZc)	20.0	10.0	5.0	15.0	Price / NTA	4.8	11.4	8.2	4.7
Market cap	NZ\$1,701m	Imputation (%)	100	100	100	100	Cash div yld (%)	7.8	3.9	2.0	5.9
Avg daily turnover	851.8k (NZ\$2,807k)	*Based on normalised profits					Gross div yld (%)	10.9	5.4	2.7	8.2

NZ Alert Levels – restrictions and re-opening path clearer, demand profile still the key unknown

Our base case assumes NZ moves to Alert Level 2 on 19 May (hence, property closure duration of eight weeks), with a step down to Alert Level 1 in early September – the latter is likely to be the most meaningful change for SKC. The re-opening path for Adelaide looks likely to be later, albeit is more challenging to predict. While NZ's Alert Level system (and signalled re-opening plans from SKC) provide a guide to what restrictions will be in place, it doesn't help us to assess customer response. We don't believe the demand profile is likely to follow the same stepped path, with a gradual improvement more likely. While we expect some level of pent up demand on re-opening, there is also likely to be a high level of consumer caution, particularly initially. We make small adjustments to our near-term EBITDA forecasts (-2-3%; shorter closure duration offset by greater disruption as it progressively re-opens).

Cash well managed to date; more clarity wanted on liquidity/funding plans

Cash opex has been well managed during the closure period, helped by deeper permanent cuts than we anticipated, while total cash burn is broadly as expected (-NZ\$30-40m/month). SKC confirmed liquidity available of ~NZ\$400m and indicated it does not expect to require any waivers for its 30 June 2020 debt covenants. We concur. However, the temporary EBITDA shock looks highly likely to create a challenge for covenants at 31 December 2020. Potential implications range from waiver to repayment, and will depend on discussions with each of its funding groups. SKC has liquidity to cover some repayment, however, not all. SKC may look to increase existing banking facilities and there is also a reasonable risk additional equity will be necessary to support the balance sheet.

Risk/reward still positively skewed

Despite a recent recovery, SKC's market capitalisation has still declined by ~NZ\$1bn since the COVID-19 outbreak took hold in China, substantially larger than our various scenarios of the risk/cashflow impact. SKC's share price has largely tracked global casino peers through 2020, despite its greater reliance on domestic/local visitation (vs tourists), and more recently, the potential for a shorter duration of disruption in NZ from the virus (vs other countries). Recent sector transactions/M&A interest also provide a reminder of the attraction of the assets (property and casino licences) which is difficult to replicate, particularly at current prices.

SKYCITY Entertainment Group Ltd (SKC)

Priced as at 01 May 2020 (NZ\$)						2.55											
12-month target price (NZ\$)*						3.30	Spot valuations (NZ\$)										
Expected share price return						29.4%	1. DCF					3.17					
Net dividend yield						2.1%	2. Sum of the parts (current)					3.16					
Estimated 12-month return						31.5%	3. Sum of the parts (w project upside)					3.65					
Key WACC assumptions						DCF valuation summary (NZ\$m)											
Risk free rate						2.00%	Total firm value					2,548					
Equity beta						0.99	(Net debt)/cash					(368)					
WACC						8.1%	Less: Capitalised operating leases					0					
Terminal growth						1.5%	Value of equity					2,180					
Profit and Loss Account (NZ\$m)						Valuation Ratios											
Sales revenue	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E		
Normalised EBITDA	998.6	1,011.6	660.8	728.1	964.9	6.1	6.2	12.2	10.8	7.4	8.5	8.4	23.9	21.0	11.5		
Depreciation and amortisation	(94.4)	(89.9)	(91.4)	(105.7)	(113.2)	10.0	10.0	32.2	30.1	13.5	5.2	4.8	11.4	8.2	4.7		
Normalised EBIT	243.8	252.8	94.5	112.4	205.6	Free cash flow yield (%)	-0.4	-6.2	-10.4	-0.4	2.0	2.0	3.9	2.0	5.9		
Net interest	(12.5)	(10.2)	(19.4)	(31.6)	(22.0)	Net dividend yield (%)	7.8	7.8	3.9	2.0	5.9	10.9	10.9	5.4	2.7		
Associate income	0	0	0	0	0	Gross dividend yield (%)	10.9	10.9	5.4	2.7	8.2	Capital Structure					
Tax	(61.5)	(69.6)	(21.8)	(22.6)	(51.4)	Interest cover EBIT (x)	19.5	24.8	4.9	3.6	9.4	27.1	33.6	9.6	6.9	14.5	
Minority interests	0	0	0	0	0	Interest cover EBITDA (x)	27.1	33.6	9.6	6.9	14.5	27.2	30.3	42.8	41.8	40.6	
Normalised NPAT	169.8	173.0	53.3	58.1	132.2	Net debt/ND+E (%)	27.2	30.3	42.8	41.8	40.6	1.3	1.5	3.8	3.2	2.4	
Abnormals/other	(0.3)	(28.4)	253.1	0	0	Net debt/EBITDA (x)	1.3	1.5	3.8	3.2	2.4	Key Ratios					
Reported NPAT	169.5	144.6	306.4	58.1	132.2	Return on assets (%)	9.6	9.9	3.8	4.4	7.8	11.9	15.0	5.7	5.9	11.6	
Normalised EPS (cps)	25.4	25.6	7.9	8.5	18.9	Return on equity (%)	14.7	15.0	5.7	5.9	11.6	33.9	33.9	28.1	30.0	33.0	
DPS (cps)	20.0	20.0	10.0	5.0	15.0	Return on funds employed (%)	11.9	11.1	4.1	4.9	8.2	24.4	25.0	14.3	15.4	21.3	
Growth Rates						Operating Performance											
Revenue (%)	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	Total revenue (incl gaming GST)						
EBITDA (%)	6.9	1.3	-34.7	10.2	32.5	Auckland	584.6	606.6	474.2	510.3	644.4	60.7	61.8	51.9	57.6	66.5	
EBIT (%)	5.6	1.3	-45.8	17.3	46.1	Hamilton	60.7	61.8	51.9	57.6	66.5	13.0	13.2	11.2	12.6	14.7	
Normalised NPAT (%)	8.2	3.7	-62.6	19.0	82.9	Other NZ	13.0	13.2	11.2	12.6	14.7	149.0	148.7	117.6	147.2	193.7	
Normalised EPS (%)	10.5	1.9	-69.2	9.0	>100	Adelaide (A\$)	149.0	148.7	117.6	147.2	193.7	110.8	83.3	0	0	0	
Ordinary DPS (%)	8.5	0.9	-69.1	7.1	>100	Darwin (A\$)	110.8	83.3	0	0	0	160.3	190.5	67.5	65.3	129.1	
Cash Flow (NZ\$m)						Operating Performance											
EBITDA	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	Revenue (incl gaming GST)						
Working capital change	338.2	342.7	185.9	218.1	318.8	Capex to sales (%)	26.1	31.6	44.7	20.2	20.7	1,101.0	1,119.0	728.0	800.5	1,060.6	
Interest & tax paid	72.8	19.1	(4.9)	(12.9)	10.6	Capex to depreciation (%)	318	418	381	162	204	EBITDA breakdown					
Other	(157.4)	(147.2)	(63.2)	(64.8)	(95.9)	Imputation (%)	100	100	100	100	100	Auckland	260.7	267.9	209.0	220.0	282.1
Operating cash flow	253.6	214.5	117.7	140.5	233.5	Pay-out ratio (%)	79	78	126	59	79	Hamilton	26.9	26.9	15.6	20.4	28.4
Capital expenditure	(261.0)	(320.1)	(295.2)	(147.2)	(200.0)	Operating Performance						Other NZ	2.1	2.3	0.1	1.3	3.2
(Acquisitions)/divestments	(47.3)	224.9	129.0	0	0	Total revenue (incl gaming GST)						Adelaide (A\$)	22.5	21.0	11.5	25.1	39.3
Other	0	0	0	0	0	Total revenue (incl gaming GST)						Darwin (A\$)	25.1	19.0	0	0	0
Funding available/(required)	(54.7)	119.3	(48.5)	(6.7)	33.5	Operating Performance						IB	32.6	41.7	(10.6)	(11.8)	11.3
Dividends paid	(85.1)	(127.1)	(127.1)	0	(104.8)	Total revenue (incl gaming GST)						Corporate costs	(33.0)	(34.7)	(34.2)	(32.0)	(40.0)
Equity raised/(returned)	0	(37.3)	(20.0)	0	0	Total revenue (incl gaming GST)						Other	(2.8)	(4.0)	(6.0)	(6.2)	(8.0)
(Increase)/decrease in net debt	(139.8)	(45.0)	(195.6)	(6.7)	(71.3)	Total revenue (incl gaming GST)						Total EBITDA	338.2	342.7	185.9	218.1	318.8
Balance Sheet (NZ\$m)						Operating Performance											
Working capital	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	Revenue (incl gaming GST)						
Fixed assets	(161.7)	(172.4)	(167.5)	(154.6)	(165.2)	Auckland	584.6	606.6	474.2	510.3	644.4	0.92	0.94	0.95	0.95	0.94	
Intangibles	1,498.6	1,436.3	1,525.0	1,581.1	1,683.3	Hamilton	60.7	61.8	51.9	57.6	66.5	Capitalised interest					
Right of use asset	831.8	798.4	784.5	769.9	754.6	Other NZ	13.0	13.2	11.2	12.6	14.7	22.9	30.3	22.1	10.5	22.5	
Other assets	0	0	0	0	0	Adelaide (A\$)	149.0	148.7	117.6	147.2	193.7	Capitalised interest					
Total funds employed	2,275.9	2,282.3	2,257.1	2,311.5	2,387.7	Darwin (A\$)	110.8	83.3	0	0	0	Capitalised interest					
Net debt/(cash)	433.0	504.3	699.8	706.6	777.9	IB	32.6	41.7	(10.6)	(11.8)	11.3	Capitalised interest					
Lease liability	0	0	0	0	0	Corporate costs	(33.0)	(34.7)	(34.2)	(32.0)	(40.0)	Capitalised interest					
Other liabilities	684.8	622.0	621.8	621.8	472.4	Other	(2.8)	(4.0)	(6.0)	(6.2)	(8.0)	Capitalised interest					
Shareholder's funds	1,158.0	1,156.0	935.4	983.0	1,137.4	Total EBITDA	338.2	342.7	185.9	218.1	318.8	Capitalised interest					
Minority interests	0	0	0	0	0	NZDAUD	0.92	0.94	0.95	0.95	0.94	Capitalised interest					
Total funding sources	2,275.9	2,282.3	2,257.1	2,311.5	2,387.7	Capitalised interest	22.9	30.3	22.1	10.5	22.5	Capitalised interest					

* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend

Digging Into Alert Levels and Another Cash Check

SKC provided a market update with some insight into plans as NZ's COVID-19 related restrictions are eased. Customer response as the casino progressively re-opens remains the key unknown. Key take-outs from SKC's release and our view:

- **Operating plans:** NZ's move to Alert Level 3 on 28 April saw construction recommence (albeit with restrictions). When NZ progresses to Alert Level 2 this will see a staged re-opening for SKC's properties, in accordance with demand, although operations will remain materially restricted by social distancing requirements. The move from Level 2 to Level 1, whenever that may be, will likely see the largest change for SKC in our view.
- **Cash burn:** SKC disclosed operating cash burn is currently -NZ\$12m/month while closed which is slightly better than we forecast (helped by recent restructuring), although higher capex (NZICC and other small capex projects restarting) means total cash burn during casino closure appears broadly consistent with our prior expectations (-NZ\$30-40m/month).
- **Funding:** SKC reaffirmed current liquidity available of ~NZ\$400m (cash and undrawn debt facilities) and indicated it does not expect to require any waivers for its 30 June 2020 debt covenants. We concur. However, the temporary EBITDA shock looks highly likely to create a challenge for debt covenants at 31 December 2020 – we expect it to look to seek a temporary waiver from various debt funders, while there is also reasonable risk additional funding support is required.

Recapping our view; OUTPERFORM

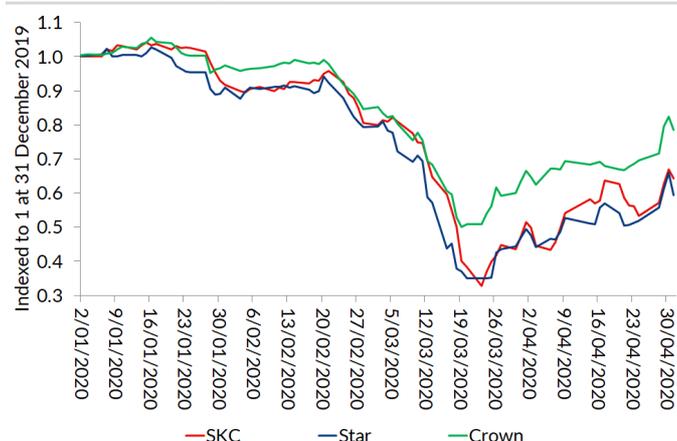
Fundamentally SKC is a strong business, with material property assets (~NZ\$2bn) and long-term monopoly casino licences. However, like the majority of businesses it has been caught out by extraordinary circumstances. Forecasting earnings is near impossible in the near-term, however, when we are out the other side of COVID-19 we expect gaming spend to recover which will improve EBITDA, gearing, and enable reinstatement of what was an attractive dividend. Despite a recent recovery, SKC's market capitalisation has still fallen by ~NZ\$1bn since the COVID-19 outbreak took hold in China. While we acknowledge material near-term risks, this is substantially larger than our various scenarios of the risk/cashflow impact. We expect the key near-term causality for investors to be a temporary dividend suspension (we assume in 2H20 and 1H21). There is also a possibility the board decides to raise equity to shore up the balance sheet through this period of heightened uncertainty.

SKC versus peers

Near-term valuation comparisons for the casino sector will be distorted for some time, particularly due to country differences (including virus trajectory and government responses). Since COVID-19, SKC's share price has largely tracked global casino peers despite its greater reliance on domestic/local players and more recently the potential for a shorter duration of disruption from the virus (due to NZ's more aggressive initial restrictions). Its Australian competitors appear to show a larger risk discount being applied for Star's weaker balance sheet versus Crown. Accordingly, we expect any resolution of funding/balance sheet questions will be helpful for SKC. We note heading into COVID-19, SKC had slightly better credit metrics (net debt/EBITDA of 2.1x vs Star at 2.6x) and lower future capex commitments versus Star.

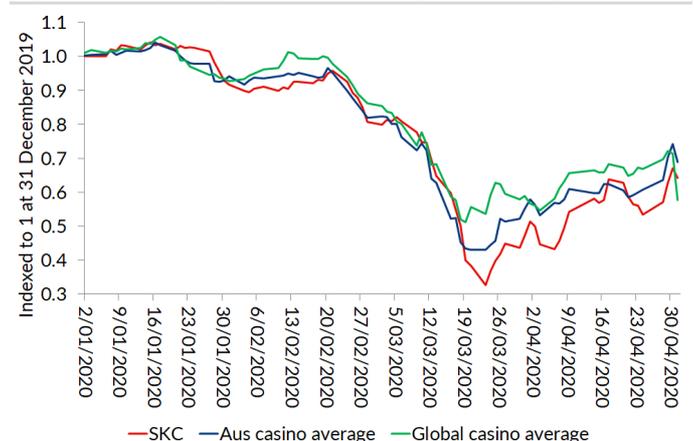
Recent signalling from private equity (buying a 9.99% stake in Crown) and Las Vegas Sands (flagging M&A ambitions to take advantage of existing market discounts, with Asia the primary target) also provides another reminder of the attraction of the assets (property and casino licences) which is difficult to replicate.

Figure 1. SKC share price move versus Star and Crown



Source: Forsyth Barr analysis, Bloomberg

Figure 2. SKC share price move versus global casino peers



Source: Forsyth Barr analysis, Bloomberg

Moving down the Alert Levels in NZ

SKC has provided some insight into the company's plans at Alert Level 3 and Alert Level 2 which appear logical and demand driven. Customer response when the casino progressively re-opens remains the key unknown which is challenging to pre-empt. We expect the move from Alert Level 2 to Alert Level 1 to be the most meaningful for SKC. While the Alert Level system provides a guide to what restrictions will be in place, we don't believe the demand profile during each Alert Level will be stable from beginning to end. We expect the trend is likely to be one of gradual improvement rather than dictated by Alert Level step changes.

Supply picture

The table below outlines the current guidance from the Government for each Alert Level and our expectations across SKC's key NZ operations. There is scope for changes and refinements from the Government. The re-opening path or timeframe is much less clear in Australia for its Adelaide casino. Alert Level specifics for SKC's NZ properties are:

- **Level 3:** SKC has recommenced some small capex projects in Auckland (no doubt taking advantage of no/limited visitation) and the NZICC/Horizon Hotel project has recommenced (albeit with restrictions).
- **Level 2:** Most facilities will be re-opened, with significant restrictions. At the key Auckland property, premium facilities will be prioritised (unsurprisingly), the main casino floor will see a staged re-opening, while most surrounding amenities will be back open (including both hotels, most dining, carparking).
- **Level 1:** All facilities back open, with no restrictions. The key exception is its IB segment, with borders likely still closed.

Figure 3. Restrictions at each Alert Level for SKC's NZ operations

Level	Key restrictions of relevance	Premium gaming rooms	Main gaming floor	IB / VIP	Hotels	Food & beverage	Carparks & Other	Construction
4	Full lockdown. In household 'bubble', essential work only	Closed	Closed	Closed	Closed	Closed	Closed	No
3	Small relaxation in lockdown, with slightly extended 'bubble'.	Closed	Closed	Closed	Closed	Closed	Closed	Yes - with restrictions.
2	1m distancing; avoid non-essential travel; indoor gathering restricted to 100pax and attendees recorded	Open; lower capacity likely due to restrictions	Open progressively, highly restricted; split into "zones"	Closed	Open	Mostly open; strict table spacing & social distancing.	Open	Yes
1	No restrictions on domestic travel, gatherings or distancing requirements	Open	Open	Highly unlikely	Open	Open	Open	Yes

Source: Forsyth Barr analysis, COVID-19.govt.nz

Demand picture

This is more difficult to forecast as New Zealand progresses down the Alert Levels, with no precedent to use as a guide. It will be some time before we have better clarity, particularly given we expect the trend to be one of gradual improvement rather than dictated by Alert Level step changes. While we expect some level of pent up demand on re-opening, there is also likely to be a high level of consumer caution. Behaviour changed rapidly as the virus and response escalated in New Zealand, however, we expect the unwind and relaxing of consumer caution may take longer.

Key considerations:

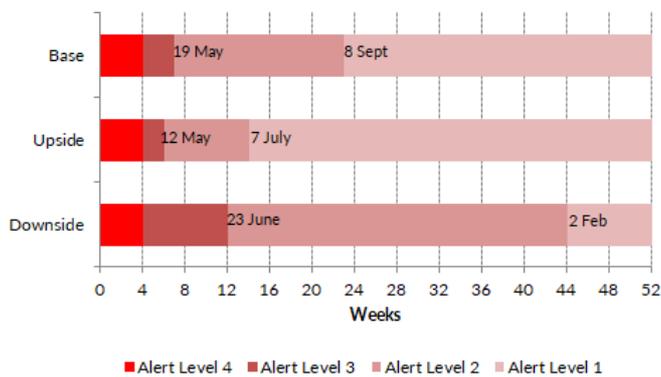
- **Government restrictions, virus progression and messaging:** Important to consumers' confidence to leave their bubble.
- **SKC's health and safety measures:** May play a part in willingness to visit SKC's facilities. Communication to customers will be key.
- **Consumer behaviour:** This is a key unknown. There is likely to be pent up demand but also substantial caution in willingness to visit entertainment destinations. We expect hospitality and large scale entertainment offerings are likely to be near 'last on the list' in terms of the recovery. Early data and anecdotes from China support this view.
- **Travel behaviours:** As domestic travel restrictions ease we expect there will be pent up demand for leisure travel, with limited options for destinations. Meanwhile, we expect less business travel and international borders to be closed for some time. SKC's key exposure to tourists is its IB/VIP segment (~10% of group EBITDA), with some exposure through its hotels (which make up ~9% of group EBITDA) and low exposure on the main gaming floor. While borders are closed we expect a pivot in focus to target domestic travellers looking for leisure options, however, this is unlikely to offset lost earnings from offshore high roller guests. If a trans-Tasman bubble was permitted between NZ and Australia, this would open up the inter-state slot market where SKC has historically under-indexed.

- **Consumer confidence:** With rising unemployment and other household pressures, consumers ability to spend will feature. Data through history across multiple geographies suggests gaming spend has been somewhat resilient through the cycle, with no obvious boom or bust cycles, albeit not recession proof or immune to a slowdown. During the GFC spending declines in casino and gaming spend across various markets were broadly within the -5% to -10% range.

Alert Level progression timing

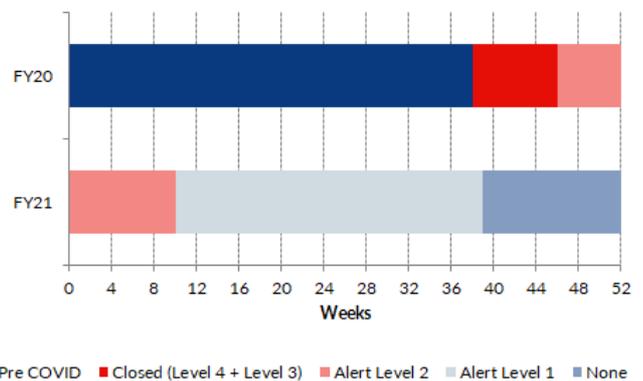
Indications are that the COVID-19 situation is coming under control in NZ, however, the progression to lower Alert Levels is likely to be a difficult balancing act between public health, political and economic decisions. Assuming NZ's transmission rate (reproductive rate or R_0) remains below one for the remainder of Alert Level 3 then we expect a relatively quick progression to Alert Level 2 – our base case assumes three weeks at Level 3 (to 18 May inclusive). When the move might be from Alert Level 2 to 1 (and 0) is less certain and will likely be driven by (1) how long it takes for a period of zero transmission, or (2) a robust contact tracing approach.

Figure 4. Our scenarios of Alert Level progression timing



Source: Forsyth Barr analysis

Figure 5. Our base case mapped to SKC's financial years



Source: Forsyth Barr analysis

Revisiting funding and the balance sheet

While the Alert Level setting and SKC's re-opening plans are becoming clearer, the demand recovery path is not. Hence, there remain a multitude of feasible scenarios for SKC's near-term EBITDA results and therefore gearing profile. The key issue is not the level of debt, but the short-term hit to earnings. This looks highly likely to create a challenge for debt covenants at 31 December 2020. Potential implications range from waiver, to repayment, and will depend on discussions with each of its funding groups. SKC has reasonable headroom to cover some repayment and current cash burn, but not all. We believe SKC may look to increase existing banking facilities, but there is also a reasonable risk additional equity will be necessary to support the balance sheet.

Figure 6. Estimated debt breakdown

NZ\$m	Debt	Liquidity available
Cash & undrawn facilities		400
Bank debt	30	
Lease liabilities	98	
Bond	125	
USPP (maturing in Mar 2021)	105	
Remaining USPP	215	
Total	573	400

Source: Forsyth Barr analysis, 1H20 company disclosures

Covenants and what happens if there is a breach

We understand both SKC's NZ bond and USPP have a net debt (adjusting for both cash in bank and cash held at its venues) to EBITDA covenant of 3.75x. These are assessed on 30 June and 31 December for the period of 12 months ending on that date.

- **30 June 2020 (2H20):** SKC indicated it does not expect to require any waivers for its 30 June 2020 debt covenants. We concur that a breach is highly unlikely.
- **31 December 2020 (1H21):** A key challenge for SKC, with rolling 12m EBITDA at that point including a meaningful period of closure (c. eight weeks) and highly disrupted period post re-opening (consumer behaviour and social distancing restrictions). A breach appears highly likely in our view.

- **30 June 2021 (2H21):** It is hard to be definitive this far out given the multitude of moving parts, however our range of scenarios suggest there is some risk of a breach.

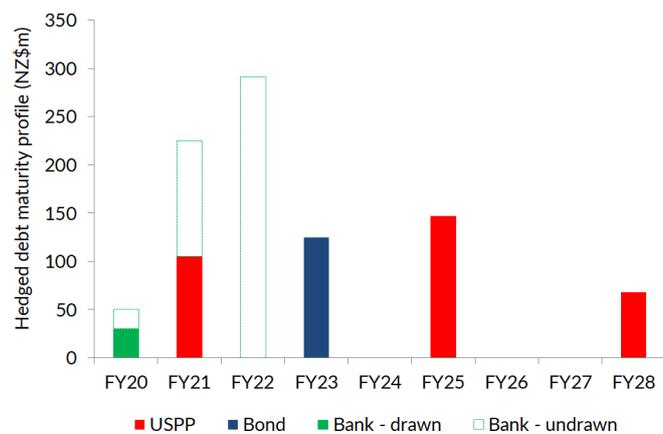
It is unclear how any potential covenant breach would play out, as it will depend on SKC's discussions with respective parties and what they want to see from SKC (particularly to provide support that is temporary). Given the main issue facing SKC is a short-term hit to earnings, we expect the banks will be accommodating of a short-term breach in covenants, particularly given its extensive asset base (with tangible value) and typically-strong cash flow generation. This view has been supported by a number of recent examples and feedback. Prima facie, SKC's bond (NZ\$125m) would require repaying. The USPP participants are harder to read. We have seen examples of both tough and relatively benign responses to covenant breaches.

Liquidity position

In its market release, SKC reaffirmed current liquidity available of ~NZ\$400m (cash and undrawn debt facilities). SKC has an NZ \$105m USPP note maturing in March 2021. After scheduled re-financing, liquidity available is c. ~NZ\$295m, assuming existing undrawn debt facilities remain available. This would provide sufficient cover for repayment of the bond (NZ\$125m) and casino closure cash burn of up to five months versus our closure scenarios of 2-3 months. However, there isn't sufficient liquidity to also cover repayment of all the remaining USPP debt (~NZ\$215m), with a gap of c. NZ\$115-150m.

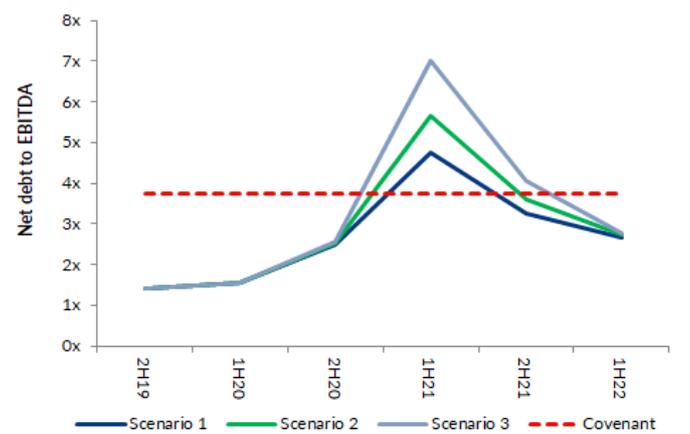
Liquidity appears tight should USPP debt require repaying, but also in 2021 (capex project timing dependent). It appears SKC is likely to need additional liquidity, be it through additional bank facilities or raising new funding (debt, convertible, equity). Based on industry feedback and examples from Star and Crown, it appears likely that Australasian banks will be supportive and we expect other potential funders would also be. SKC has indicated it is progressing a funding plan which "will be finalised once the trading performance of its New Zealand properties has been assessed following the expected re-openings by the end of May 2020". There is a reasonable risk the board decides to raise equity to shore up the balance sheet through this period of heightened uncertainty.

Figure 7. Hedged debt maturity profile (at 1H20 result)



Source: Forsyth Barr analysis, Company presentation

Figure 8. Illustrative gearing scenarios



Source: Forsyth Barr analysis

Earnings revisions

We make small downgrades to our near-term EBITDA expectations, with a slightly shorter closure period offset by higher assumed disruption during the 'recovery period'. Our longer-term forecasts are broadly unchanged. We lift our near-term capex assumptions to reflect some additional projects being undertaken during Alert Level 3, while take a more conservative view on the level of dividend payment. There is no change to our view of nil dividend in 2H20 and 1H21.

Figure 9. Earnings revisions (NZ\$m)

NZ\$m	FY19A				FY20E				FY21E				FY22E			
	Actual	Old	New	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg	Old	New	% chg
Total revenue excl gaming GST	1,011.6	660.8	660.8	0%	745.0	728.1	-2%	977.6	964.9	-1%						
Normalised EBITDA	342.7	188.9	185.9	-2%	225.7	218.1	-3%	329.8	318.8	-3%						
Normalised profit	173.0	55.6	53.3	-4%	61.0	58.1	-5%	141.0	132.2	-6%						
Normalised EPS (cps)	25.6	8.3	7.9	-4%	9.0	8.5	-5%	20.2	18.9	-6%						
Dividend per share (cps)	20.0	10.0	10.0	0%	10.0	5.0	-50%	20.0	15.0	-25%						

Source: Forsyth Barr analysis

Investment Summary

SKYCITY (SKC) is one of the largest gaming operators in Australasia. Earnings and valuation are driven by Auckland, which makes up ~70% of group EBITDA. The company is facing unprecedented challenges from temporary closure of its properties and disruption from the COVID-19 crisis. Whilst there is a high degree of uncertainty in the current environment, SKC has a strong asset base and we expect it to come through the crisis and gaming spend levels to recover. Valuation levels are attractive, more than compensating for the risks. **OUTPERFORM.**

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

- **Earnings outlook:** SKC is facing a period of depressed earnings near-term, given enforced property closures and disruption from COVID-19. We do expect gaming spend to recover, although this will likely take time and is contingent on the virus trajectory and government policies around restrictions.
- **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.

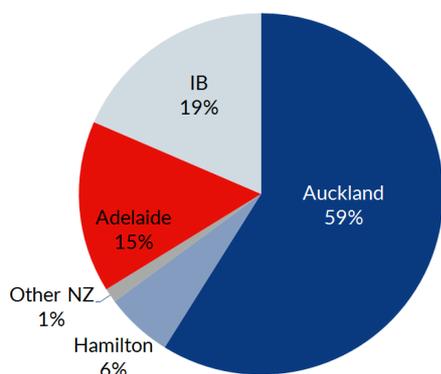
Financial structure

- **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), COVID-19 'social distancing' policies and future growth plans to build out destination precincts surrounding its casinos.
- **Yield:** SKC has historically offered a solid yield. The COVID-19 crisis has forced the Board to reconsider its dividend policy. We expect to see a temporary dividend suspension, for c. 12 months, during the period of heightened uncertainty.

Risk factors

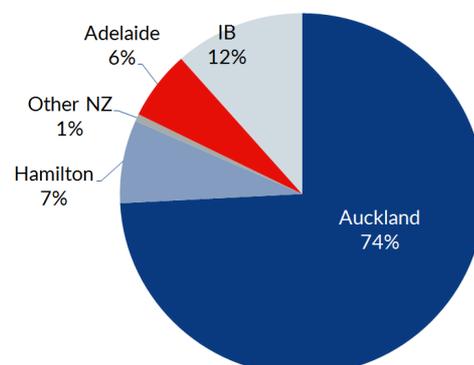
- **Gaming regulation:** Unexpected regulatory and taxation changes.
- **Mature local gaming market:** The market is not only mature but vulnerable to changing entertainment spending patterns.
- **COVID-19:** The key risk to SKC is the domestic backdrop and ultimately consumer behaviour (which could be dictated by containment/self-quarantine measures). Temporary closure is now reality in both NZ and Australia, and we expect at least some period of material disruption thereafter. However, being definitive on timelines is difficult.

Figure 10. FY19 revenue breakdown (cont. operations)

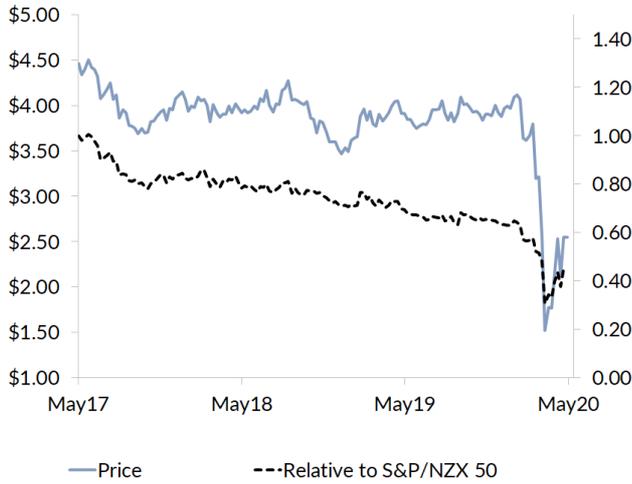


Source: Forsyth Barr analysis, Company reports

Figure 11. FY19 EBITDA breakdown (cont. operations)



Source: Forsyth Barr analysis, Company reports

Figure 12. Price performance


Source: Forsyth Barr analysis

Figure 13. Substantial shareholders

Shareholder	Latest Holding
Sumitomo Mitsui Trust Holdings	10.0%
Lazard	8.5%
Commonwealth Bank of Australia	8.2%
BlackRock Investment Management	7.1%
Investor Mutual	7.1%
Colonial First State	5.4%

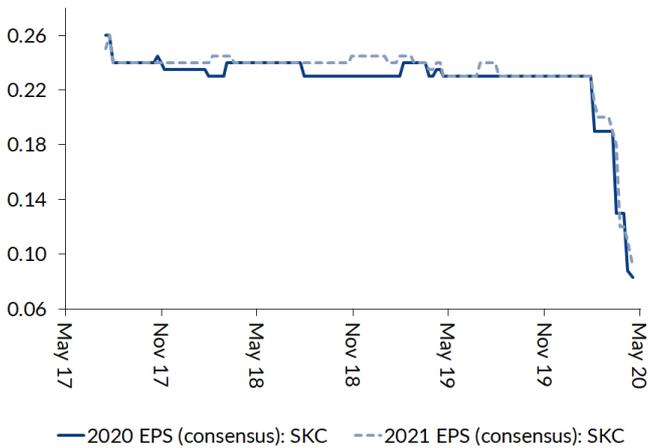
Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

Figure 14. International valuation comparisons

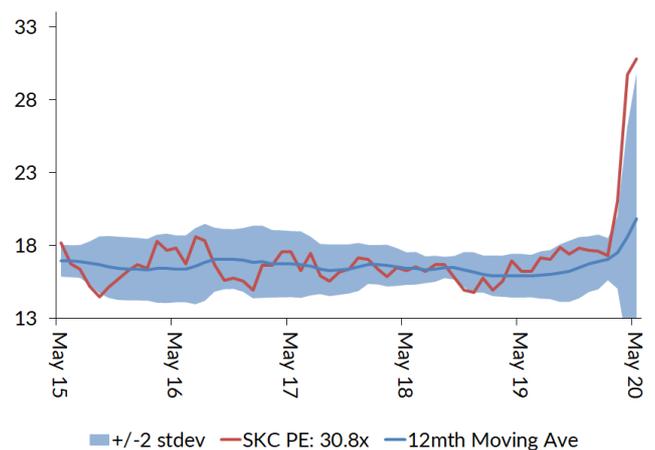
Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2021E
				2020E	2021E	2020E	2021E	2020E	2021E	
(metrics re-weighted to reflect SKC's balance date - June)										
SKYCITY	SKC NZ	NZ\$2.55	NZ\$1,701	32.2x	30.1x	11.9x	10.1x	23.3x	19.6x	2.0%
CROWN RESORTS	CWN AT	A\$8.60	A\$5,824	45.0x	45.3x	13.2x	12.1x	33.9x	36.3x	4.8%
TABCORP HOLDINGS	TAH AT	A\$2.97	A\$6,036	21.2x	19.4x	10.1x	9.8x	16.7x	15.5x	4.8%
STAR ENTERTAINMENT GRP/T	SGR AT	A\$2.56	A\$2,348	30.5x	32.4x	9.8x	9.8x	22.5x	23.9x	3.0%
GENTING MALAYSIA BHD	GENM MK	RM2.21	RM12,494	16.2x	17.2x	7.2x	7.1x	14.7x	14.5x	6.5%
KANGWON LAND INC	035250 KS	KRW25200.00	KRW5,391,301	16.2x	15.4x	7.1x	7.0x	7.8x	7.7x	3.7%
			Compc Average:	25.8x	25.9x	9.5x	9.2x	19.1x	19.6x	4.6%
			SKC Relative:	25%	16%	25%	10%	22%	0%	-57%

EV = Current Market Cap + Actual Net Debt

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

Figure 15. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 16. One year forward PE (x)


Source: Forsyth Barr analysis

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