

Gaming Industry

GLOBAL GAMING STABILIZES AFTER MACAU SHAKEUP

Global gaming revenues will stabilize in 2016 after a sharp downturn in revenue last year. An anti-graft campaign and closer monitoring of ‘VIPs’ in the Chinese region of Macau sent gaming revenues plummeting by a third in 2015, to the lowest in 5 years. In Las Vegas, revenue has been stable at around US\$6½ bn for the last few years, and is on pace to match that in 2016 (chart 1). Economic conditions will remain supportive of gaming, with increases in travel volumes across Europe, the United States and the Asia-Pacific region through this year. China’s economic slowdown is unlikely to weigh on outbound tourism expenditures, as the nation shifts to consumption-based growth as opposed to resource extraction and manufacturing.

Tourism expenditure in China skyrocketed nearly 30% in 2014, even as real GDP growth slowed from 7½% to 7%. A rapidly growing middle class and rising wages in China will boost gaming revenues in the region, and has spurred large casino developments and expansions in Vietnam, Malaysia and the Philippines, amongst others. Australia is also betting that rising tourism demand from emerging Asia will lead to increased domestic gaming revenue, and has allowed several billion dollars of investment in casino projects across the country. Output growth in advanced economies has been weak in recent years, and will continue to underperform alongside commodity price volatility and a structural slowdown in global trade. Nonetheless, household expenditures have remained resilient, and will continue to support travel and the gaming industry.

Most large casino operators have ties to Macau, and experienced around a 50% drop in return on assets and equity in 2015 as a result. Attempting to replicate the shift that has occurred in Las Vegas (chart 2), Macau casinos have been directed by the government to diversify their revenue streams. Gaming accounted for 93½% of total revenue in 2014, while the government’s ‘five-year plan’ aims to reduce that to 90% by 2020. VIP gaming accounted for over 55% of Macau’s gaming revenue last year, even though it is estimated that the VIP cohort consists of only 100,000 people, compared with the 30 million annual visitors to Macau. Evidenced by last year’s decline, shifting government regulations and policy over gaming can have a huge effect on casino profitability, especially when directed at high-rollers. Diversification will add stability, but will likely come at the cost of lower revenue.

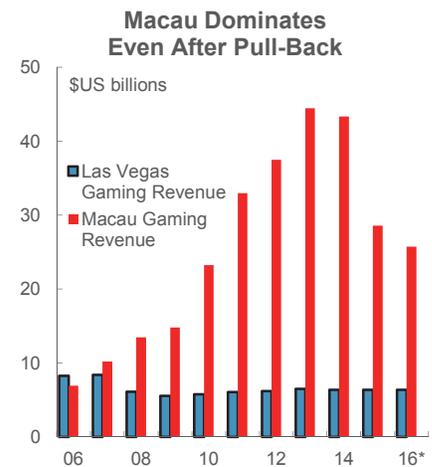
Casino operators have embarked on a series of high-profile expansions into both domestic and international markets. Las Vegas Sands, Wynn and MGM have large Macau casino developments opening soon, with the latter two companies also planning expansion in Massachusetts. Australian-based Crown Resorts recently reduced their stake in one of their jointly owned Macau properties to ensure they meet capital requirements for a proposed development in Sydney, and are aggressively pursuing expansion on the Las Vegas Strip.

Legal online gaming is in its infancy, with only a handful of countries embracing the technology. The U.K. passed a series of regulations in late 2014 to control and tax offshore and domestic online gaming platforms, leading to full year 2015 receipts of \$4.3 bn. New Jersey and Delaware have allowed online gaming since 2013, with combined annual revenue of around \$125mn. Nevada also allows the

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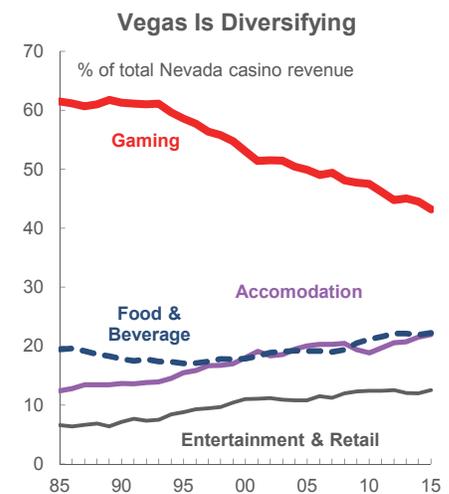
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Chart 1



*year-to-date. Source: Las Vegas Convention and Visitor Authority, The Statistics and Census Service Macau SAR Government, Scotiabank Economics.

Chart 2



Source: UNLV Center For Gaming Research.

practice, but doesn't release separate statistics on online versus other gaming. Montreal-based Amaya Inc. became the world's largest online gaming company in 2014 when it acquired poker websites Full Tilt and Poker Stars for nearly \$5 bn. The company has grown rapidly, with revenue of only C\$18mn in 2011 increasing to C\$1.4 bn in 2015. It is difficult to gauge the size of the actual and potential market for online gaming, but the practice is becoming more widespread and accepted, especially in the United States. Several states have been working on legislation, including California, New York and Pennsylvania, with resolution (for or against) likely to occur over the next few years. Currently, legal online gaming accounts for around 3% of global gaming revenue, but will increase rapidly if populous states legalize the practice.

Slot machines account for about half of gaming revenue at Nevada Casinos, compared with only 5% in Macau, where baccarat is the preferred game. With development in Macau outpacing Las Vegas, slot machine demand will not rise proportionally with new casino builds. Nonetheless, there will be substantial demand for new slot machines for upcoming U.S. casino developments, and ongoing software support needed for existing machines. IGT, the world's largest slot machine manufacturer, is also involved in online gaming, and provides New Jersey with online wagering services.

CASINOS & GAMING INDUSTRY FUNDAMENTALS

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016Q1</u>
	Return on Assets (y/y % change)				
Las Vegas Sands Corp.	6.9	10.3	12.6	9.1	8.6
MGM Resorts international	-6.5	-0.7	-0.6	-1.7	-2.1
Wynn Resorts Ltd.	7.1	9.3	8.4	2.0	3.0
Crown Resorts	9.4	6.7	10.4	5.1	4.4
	(y/y % change)				
Advanced Nations GDP*	1.2	1.2	1.8	1.9	1.9
Emerging Nations GDP*	5.3	4.9	4.6	4.0	4.1
Global Travel Volumes*	4.7	4.6	4.2	4.4	4.0

Source: Scotiabank Economics, Bloomberg, IMF, UNWTO. *Full year 2016 forecast from IMF & UNWTO.

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