

Far East Consortium

Acquiring a small casino & hospitality group in Europe

Significant pace in European continent

FEC has announced that it had entered merger agreement with Trans World Corporation, which is engaged in hospitality and gaming business in Germany, Austria and Czech. The deal is subject to satisfied 6 condition precedents to complete (88% shareholder consent obtained). Total consideration will be US\$ 42 million for 100% equity of the target company. The consideration represents 26% discount to NAV of the target company and 1.3% of our estimated FEC Sep-18 Net Asset Value. We believe this acquisition would mark a milestone for FEC as it gives FEC expertise especially casino operation experience in European continent, enabling it to expand its casino business from Australia to Europe.

Mature casinos provide incremental income

We believe the acquisition will have incremental income from casino business, enhance the FEC's hotel revenue and further diversify its recurring income. The target company owns and operates three casinos in Czech with 6 years basic casino licenses renewed from Jan-18, generating steady income US\$37.6 million, 38.8 million and 48.3 million in FY14 to FY16, respectively. We haven't factored in Queen's Wharf Casino in Brisbane in FEC's NAV.

Impact from gambling tax change may be one-off in 2017

We believe FEC entered the deal at a good price at 2.7x 2016 EBITDA and 6.64x 2016 pe, as it took advantage of the change in casino regulations in Czech which resulted in a one-off drop in casino revenue. Czech has tightened licensing requirement, enhanced customer protection (including ID registration) and raised the gaming tax in 2017. The tax rate used to be 20% of winning revenue and was changed to be 35% of slot game and 23% of live game for the operators. As a result, the gaming revenue of the target decreased to US\$31.6 million in 3QFY17, as compared with US\$48.3 million in FY16. In the long run, the regulations are likely to result in reduced supply in casinos and gamblers are likely to get used to more stringent scrutiny slowly.

Trans World Corp's hotel business is growing

Additionally, Trans World Corp has 2 four-star hotels and 1 three-star hotel in Germany, 1 four-star hotel in Austria and 1 four-star hotel in Czech. Gaming segment contributed over 90% in the last 3 years. In 3QFY17, thanks to acquisition of Hotel Steigenerger in March 2017, hotel revenue increased from US\$ 4.9 million in FY16 to US\$ 9.6 million in first 3Q in FY17. The target company's net gearing ratio is only 14% (cash of US\$8.6 million and loans of US\$16.5 million). However, the EBITDA margin fluctuated in last 3 year, which is 11.7%, 7.7% and 17.4% in FY15, FY16 and 3QFY17.

Reiterate "BUY" and Price target of HK\$5.34 (26% upside); long term player with consistent strategy and deep NAV discount

We believe FEC's acquisition of the small operation is consistent with the company's step-by-step method and represents a good start to its operation in continental Europe. We reiterate 'Buy' for FEC. We maintain our PT to HK\$5.34, which is derived by using sum-of-the-parts method. Current share price implies a 61% discount to our estimated Sep-18 Net Asset Value (NAV).

Stock code: 35.HK

Rating: Buy

Price target (HK\$)	5.34
Previous Price target (HK\$)	5.34
Current price (HK\$, 27 Nov 2017)	4.25
Upside/downside %	26%
Market cap (HK\$ m)	9,780
Market cap (US\$ m)	1,249
Avg daily turnover (HK\$ m)	6.51

Source: Bloomberg, AMTD estimates

Key forecasts

(HK\$ m)	FY17	FY18e	FY19e	FY20e
Net profit	1,118	1,473	2,060	2,211
yoy %	52%	32%	40%	7%
Revenue	5,005	5,908	7,549	9,877
yoy %	25%	18%	28%	31%
EBITDA	2,051	2,654	3,496	3,694
Net gearing	31%	31%	31%	26%
EPS	0.51	0.66	0.92	0.99
BPS	4.82	5.26	5.88	6.52
DPS	0.18	0.22	0.30	0.35

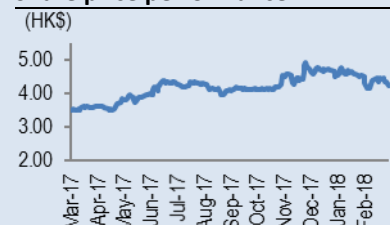
Source: Company data, AMTD estimates

Valuation

(HK\$ m)	FY17	FY18e	FY19e	FY20e
P/E (x)	9.3	7.0	5.0	4.7
P/BV (x)	0.95	0.87	0.78	0.70
Div yield	4.2%	4.9%	6.9%	7.8%
ROE	10.7%	17.7%	16.5%	15.9%
ROA	4.1%	6.7%	6.2%	5.6%

Source: Bloomberg, AMTD estimates

Share price performance



Source: Bloomberg

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Figure 1: FEC P&L forecast

P&L	HK\$ m						YoY growth %				
	FY15	FY16	FY17	FY18e	FY19e	FY20e	FY16	FY17	FY18e	FY19e	FY20e
Revenue	5,110	3,995	5,005	5,908	7,549	9,877	-22%	25%	18%	28%	31%
Property development	2,962	1,971	2,937	3,416	4,920	7,153	-33%	49%	16%	44%	45%
Hotel	1,454	1,285	1,309	1,655	1,753	1,802	-12%	2%	26%	6%	3%
Car park	616	623	641	674	707	743	1%	3%	5%	5%	5%
Property investment	56	59	55	64	69	79	5%	-8%	16%	8%	15%
Others	78	58	64	100	100	100	-25%	10%	57%	0%	0%
Cost of sales and services	(2,884)	(1,990)	(2,709)	(3,020)	(3,540)	(5,261)	-31%	36%	11%	17%	49%
Depreciation & amortization of hotel & car park assets	(279)	(299)	(307)	(329)	(329)	(329)	7%	3%	7%	0%	0%
Gross profit	1,946	1,706	1,990	2,558	3,680	3,957	-12%	17%	29%	44%	8%
Property development	1,086	1,002	1,272	1,602	2,653	2,886	-8%	27%	26%	66%	9%
Hotel	691	541	518	717	778	809	-22%	-4%	39%	8%	4%
Car park	124	117	114	119	125	132	-6%	-3%	5%	5%	5%
Leasing and others	45	46	86	119	123	131	2%	88%	38%	3%	6%
Other income	39	23	25	0	0	0	-40%	8%	n.a.	n.a.	n.a.
Other gains and losses	299	181	368	486	300	300	-39%	103%	32%	-38%	0%
Administrative expenses	(642)	(598)	(584)	(602)	(662)	(695)	-7%	3%	5%	10%	5%
Selling and marketing expenses	(93)	(105)	(46)	(118)	(151)	(198)	14%	-56%	154%	28%	31%
EBIT	1,536	1,206	1,744	2,325	3,167	3,364	-21%	45%	33%	36%	6%
Finance costs	(224)	(228)	(173)	(284)	(319)	(308)	2%	-24%	64%	13%	-4%
Profit before tax	1,328	979	1,567	2,041	2,847	3,057	-26%	60%	30%	40%	7%
Income tax expense	(330)	(221)	(434)	(551)	(769)	(825)	-33%	96%	27%	40%	7%
Profit for the year	998	758	1,133	1,490	2,079	2,231	-24%	49%	32%	40%	7%
Minority interest	41	24	15	17	18	20	-43%	-36%	10%	10%	10%
Attributable net profit	957	734	1,118	1,473	2,060	2,211	-23%	52%	32%	40%	7%
Tax rate	24.9%	22.6%	27.7%	27%	27%	27%	0%	0%	0%	0%	0%
Adjusted cash profit	836	853	1,424	1,802	2,390	2,541	2%	67%	27%	33%	6%
Dividend payout ratio	34%	47%	37%	33%	33%	35%					
DPS	0.16	0.16	0.18	0.22	0.30	0.35	0%	15%	18%	40%	14%
EPS	0.48	0.37	0.51	0.66	0.92	0.99	-23%	41%	28%	40%	7%

Source: Company data, AMTD Equity Research estimates

Figure 2: FEC balance sheet forecast

Balance sheet, HK\$ m	FY15	FY16	FY17	FY18e	FY19e	FY20e
Non-current Assets	12,031	12,460	12,509	12,524	12,762	13,060
Investment properties	3,154	3,304	3,002	3,161	3,404	3,731
Property, plant and equipment	7,492	7,720	7,482	7,337	7,332	7,304
Prepaid lease payments	541	522	486	486	486	486
Goodwill	68	68	68	68	68	68
Others	775	845	1,470	1,470	1,470	1,470
Current Assets	10,185	13,701	15,891	18,149	22,955	29,863
Properties for sale	5,452	8,640	9,170	11,064	16,631	23,580
Completed properties	201	584	280	280	280	280
Properties for/under development	5,252	8,056	8,890	10,783	16,350	23,299
Debtors, deposits and prepayments	393	527	375	375	375	375
Deposits receivable from stakeholders	417	587	252	252	252	252
Investment securities	1,150	1,218	1,466	1,466	1,466	1,466
Pledged deposits	273	25	25	25	25	25
Restricted bank deposits	51	162	268	268	268	268
Bank balances and cash	2,274	2,358	3,882	4,246	3,485	3,444
Others	174	183	452	452	452	452
Total assets	22,216	26,161	28,400	30,673	35,716	42,923
Current Liabilities	6,103	6,471	6,181	6,950	10,972	17,721
Creditors and accruals	737	829	889	889	889	889
Customers' deposits received	575	2,460	2,110	2,879	6,901	13,650
Obligations under finance leases	4	3	4	4	4	4
Tax payable	333	183	359	359	359	359
Bank borrowings	3,087	2,933	2,755	2,755	2,755	2,755
Bonds	1,250	-	-	-	-	-
Others	116	63	64	64	64	64
Non-current Liabilities	5,852	9,422	11,275	11,775	11,398	10,398
Bank borrowings	4,468	7,863	7,376	7,876	8,376	6,876
Obligations under finance leases	5	5	8	8	8	8
Amounts due to shareholders of non-wholly owned subsidiaries	-	247	247	247	247	247
Bonds	1,005	868	3,131	3,131	2,254	2,754
Derivative financial instruments	59	77	119	119	119	119
Deferred tax liabilities	315	362	395	395	395	395
Total liabilities	11,955	15,893	17,456	18,725	22,370	28,119
Equity						
Share capital	191	213	224	224	224	224
Share premium	2,982	3,731	4,034	4,034	4,034	4,034
Reserves	5,970	6,196	6,534	7,521	8,902	10,339
Shareholder's equity	9,144	10,140	10,792	11,779	13,159	14,596
Minority interest	1,117	127	152	169	187	207
Total equity	10,261	10,267	10,944	11,947	13,346	14,804
Hotel revaluation surplus	10,976	10,732	13,354	13,354	13,354	13,354
Adjusted shareholder's equity	21,237	20,999	24,298	25,301	26,700	28,158

Source: Company data, AMTD Equity Research estimates

Figure 3: FEC cash flow forecast

Cash flow forecasts, HK\$ m	FY15	FY16	FY17	FY18e	FY19e
Property sales	3,053	3,784	4,377	4,646	7,203
EBIT from hotel operation	166	221	342	333	382
EBIT from investment properties	95	164	119	123	131
Tax paid	-140	-372	-551	-769	-825
Depreciation	279	299	309	309	309
Cash flow from operation (CFFO)	3,454	4,096	4,596	4,642	7,199
Capex	-2,527	-5,270	-4,162	-8,363	-12,104
Acquisition of assets	-	-403	-	-	-
Others	-51	88	-	-	-
Free operating cash flow (FOCF)	875	-1,489	434	-3,721	-4,905
Interest paid	-393	-380	-455	-543	-516
Dividend	-107	-79	-100	-100	-100
Dividends paid to shareholders of non-wholly owned subsidiaries	-37	-19	-20	-20	-20
FCF	338	-1,966	-141	-4,384	-5,541
Equity issuance	14	6	-	-	-
Share buyback	-	-82	-	-	-
New debt	2,776	6,193	3,000	7,000	8,000
Repayment of debt	-2,660	-4,251	-1,500	-3,377	-2,500
Shareholder loan	-	246	-	-	-
Others	-2	-28	-	-	-
Change in FX	-55	-33	-	-	-
Change in cash position	377	85	1,359	-761	-41
Cash balance - period beginning	1,829	2,274	2,887	4,246	3,485
Cash balance - period end	2,274	2,358	4,246	3,485	3,444

Source: Company data, AMTD Equity Research estimates

Figure 4: FEC key ratios

Ratios	FY15	FY16	FY17	FY18e	FY19e	FY20e
Gross margin	38%	43%	40%	43%	49%	40%
Gross debt	9,815	11,669	13,270	13,770	13,393	12,393
Net debt	6,340	7,931	7,654	7,789	8,174	7,215
EBIT	1,536	1,206	1,744	2,325	3,167	3,364
EBITDA	1,815	1,505	2,051	2,654	3,496	3,694
Gearing ratio ex. Hotel revaluation gains (x)	69%	78%	71%	66%	62%	49%
Gearing ratio (x)	30%	38%	31%	31%	31%	26%
Net debt/EBITDA (x)	3.5	5.3	3.7	2.9	2.3	2.0
EBITDA cover (x)	8.1	6.6	11.8	9.4	10.9	12.0
Selling and marketing expense % of revenue	1.8%	2.6%	1.8%	2.0%	2.0%	2.0%
Admin expense % of revenue	13%	15%	12%	10%	9%	7%
Avg interest cost	4.0%	3.5%	2.6%	3.5%	4.0%	4.0%
ROA	4.3%	3.0%	4.1%	6.7%	6.2%	5.6%
ROE	10.7%	7.6%	10.7%	17.7%	16.5%	15.9%

Source: Company data, AMTD Equity Research estimates

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Buy	Stock with potential return of over 20% over the next 12 months
Hold	Stock with potential return of -20% to +20% over the next 12 months
Sell	Stock with potential loss of over 20% over the next 12 months

Analyst Certification

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