Shifting Sands

After suffering for two years at the hands of President Xi Jinping's crackdown on corruption and weak mainland economic growth, it seems that the tide is about to turn for activity in the Macau gambling market. As the nimblest regional operator, Las Vegas Sands stands to benefit disproportionately from this change in fortune.

In the wake of Xi's crackdown, the appetite for conspicuous consumption has waned amongst China's elite, leaving a miasma over casino operators' revenues. Over the past year, VIP gross gambling revenues have declined by nearly -22%. Though this weakness is expected to persist for the remainder of the year in the VIP segment, long-term growth in the mass market segment is anticipated to more than compensate: in June of this year mass gaming volumes and revenues increased year on year at Las Vegas Sands' Macau properties for the first time since September 2014. In a recent conference Sheldon Adelson, Chairman and CEO of Las Vegas Sands, declared he can "smell and feel" a recovery in the Macau market.

He may well be proven right. In the twelve months to June, the company derived 6.5x more profit from mass tables and slots than VIP tables. Among competitors, Las Vegas Sands is uniquely positioned to benefit the most from the growth in mass market revenues: with the opening of the Parisian luxury hotel in September, the company will control nearly 40% of the Macau casino hotel supply, or approximately 13,000 rooms. The hotel will be replete with all the gaudy trappings of its kind, including a half-sized Eiffel Tower and a rainbow-coloured light show; it is expected to become another "must-see" property in Macau.

Of course, Las Vegas Sands is not the only operator in the region. However, of their five major competitors the company comfortably eclipses four in efficiency: the company enjoys a share of market revenue 30% above its capacity share. Moreover, Las Vegas Sands excels in attracting custom: it estimates its 2015 visitations to be in the range of 62 million, or twice the approximate 30 million annual visitors to Macau.

Though equity valuations for the Macau casino operators have already begun to benefit from improving trends and the anticipation of new casino openings, we believe there is more upside in the share price given the stable earnings growth due to its high mass market exposure, relatively cheap valuation, and high dividend yield. The latter of which is the highest within the sector at over 6% and is sustainable in the long-run, given the company's strong free cash flow and balance sheet.

For now, the Macau gaming industry remains volatile. Over time, however, this will subside as the region's revenues shift in focus from VIP to mass market. In the shifting sands of the Macau gaming market, little is certain. However, with revenue up 3% in spite of continued softness in the VIP segment, and a dominant mass and non-gaming position on the central Cotai strip, we believe Las Vegas Sands is poised for successful long-term growth.

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