BEHIND THE ASIAN CURTAIN

The Asian gaming business thinks and operates according to its own rules and is extremely reluctant to make its rulebook public. G3 looks at the latest developments from an Asian perspective.

The greatest upcoming opportunity in SE Asia is undoubtedly the Philippines market. The resort casinos opening will change the dynamics of the region, though there are still doubts as to whether Entertainment City will become the gaming hub as PAGCOR intends, and if the fourth licence holder, Aruze/Universal, can complete within the time-frame of their licence. Universal has broken ground, but no date has yet been set as to the completion of the casino from contractors on the ground. Money is not the problem for Universal, despite Chairman Kazuo Okada's very public spat with Steve Wynn, the pachinko mogul is able to draw upon significant resources to complete the project on time and budget.

The first issue confronting Universal is that the licence agreement drawn up with PAGCOR was signed with the previous administration. The original delay with Universal's licence centred around the issue of land ownership in the Philippines, with foreign companies unable to own land parcels. To counter this, the former administration demanded that Universal move its entire slot machine production to the Philippines,

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creating a local business that would enable the Japanese company to acquire the land needed for its resort project. The changeover of the administration, however, nullified this arrangement, forcing Universal to renegotiate again, despite having moved its Aruze production facility to Manila.

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> The US Securities and Exchange Commission has asked to interview Mr. Okada in connection with an inquiry into a $135m Wynn Resorts donation to the University of Macau, as Universal sought a court order in January to back its Chairman's position that as a director he was entitled to inspect Wynn Resorts' books and records regarding the donation.

than $110,000 in payments and gifts to regulators and their families, according to a statement by the Las Vegas-based casino operator. Wynn's Macau unit ejected the Japanese billionaire from its board and Philippine President Benigno Aquino ordered a probe into payments allegedly made to PAGCOR.

Mr. Okada has since filed counterclaims in the US federal court, saying Wynn Resorts Chairman Steve Wynn runs the company as his 'fiefdom' and has asked the court to invalidate the redemption of his shares at an $800m discount. At the same time, the US Securities and Exchange Commission has asked to interview Mr. Okada in connection with an inquiry into a $135m Wynn Resorts donation to the University of Macau, as Universal sought a court order in January to back its Chairman's position that as a director he was entitled to inspect Wynn Resorts' books and records regarding the donation.

The dispute with Wynn Resorts has undoubtedly caused Universal issues in the Philippines, though they remain ostensibly superficial. The claims of complimentary hotel rooms being given to PAGCOR staff could be directed at any operator on the planet. Gaming board officials travel the world expecting operators to pick up the tab for their accommodation and subsistence. It's a practice that most operators would happily forgo if this were deemed unlawful - but is it really? The claim that Universal comped rooms to PAGCOR is understandable as it's as common in the Philippines as it is in Europe, the US or elsewhere. The fact that it's been used to highlight wrong-doing on the part of Universal is gamesmanship on the part of its detractors. PAGCOR chair and CEO Cristino Naguiat Jr. said that Okada described the alleged US$110,000 cash gifts to PAGCOR officials as 'inaccurate.' Mr. Naguiat readily admits that as part of standard industry courtesy and reciprocity, "complimentary accommodations are granted to casino executives from other gaming destinations." He added that PAGCOR extends the same courtesy to visiting casino executives whenever they visit the Philippines.

DELAYING TACTICS

Universal has been caught in administrative limbo as different administrations have come and gone in the Philippines and cost Universal both time and money as the country holds close to US$1bn in ESCROW as part of Universal's licence application. The requirement for Universal to relocate its manufacturing facilities to the Philippines is not part of its licence application and you won't see it mentioned anywhere in its bid document. These 'provisos' form part of the application process whereby they are tacitly accepted by applicants when they make their bids. Okada has alluded to another tacit agreement between Wynn and the Macau government, whereby Wynn has donated $12m each year to the Macau University as part of a similar arrangement. These tacit licence conditions might not be public, but they are nonetheless mandatory.

> **OKADA HAS ALLUDED TO ANOTHER TACIT AGREEMENT BETWEEN WYNN AND THE MACAU GOVERNMENT OVER THE $135M UNIVERSITY DONATION.**

In a forthcoming G3 interview with Universal's COO Alfred Yue, he makes clear that he believes the claims of Wynn Resorts of impropriety are attempts to smear Universal. The claims from Wynn began as Okada came to expand his operations into the Philippines market in direct competition to Wynn's own Asian developments. It marks the end of a 12 year relationship between the two men in which Okada originally helped to bankroll Wynn Resorts as the company started out.

At least Macau has had the decency to keep corruption within its government structure. The current scandal of choice in Macau concerns the Macau government looking to seize the site of the HKD$20bn "La Scala" development at the end of a corruption trial in which two Hong Kong tycoons are accused of paying a HKD$20m bribe to the former Secretary for Transport and Public Works, Ao Man Long. The developer in question is Chinese Estates, which is building the HKD$20bn luxury housing project called "La Scala" on land opposite Macau Airport and near the city's Cotai strip and which has already pre-sold hundreds of flats. Macau's chief executive Chui Sai On has declined to rule out the possibility of the government seizing the five plots of land involved.

"You can't buy a decent watch for the sum of money Wynn is claiming PAGCOR received from us," stated an outraged Mr. Yue at G2E Asia. "When does hospitality become a bribe and when does a donation become a back-hander?"

In addition to its licensing issues, building a resort in the Philippines right now in the timescale demanded by the Universal licence is seen as unfeasible. The demand for labour and building resources, just as in Macau, is under such strain that contracts are being signed that exclusively tie-up resources for years to come. One of the largest companies in the Philippines and one familiar with massive construction projects is SM Prime Holding, which is building the second licence in the market with an enormous mall/casino project, Belle Grande, through subsidiary company, Belle Corp, currently underway. SM Prime Holdings operates 43 shopping malls in the Philippines, one of which is the fourth largest in the world with 200,000 visitors per day. The group is planning to open new malls in the US, Singapore, UAE, Qatar, Saudi Arabia, Kuwait, UK, Bahrain, Germany and Malaysia. It's Mall of Arabia is set to become the second largest shopping centre in the world. However, it is believed that internal wranglings within the Sy family-owned and run group started causing its casino project in the Philippines to slow to a crawl.

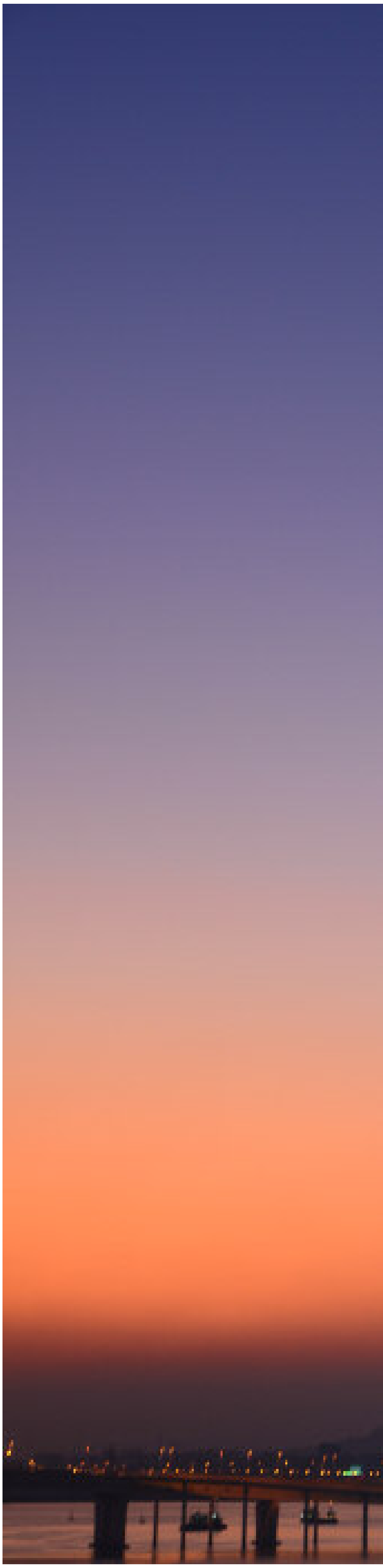
RESORTS WORLD MANILA OPENED WITH 500 HOTEL ROOMS THROUGH A STAGGERED DEVELOPMENT, BUT FOR SM MALLS, PAGCOR IS DEMANDING THE FULL QUOTA.

Originally the Sy family saw their malls as amusement parks, including cinemas, blowing alleys, convention centres and arcades into their locations, but the addition of casino gaming to the portfolio has split the family down the middle. The flow of capital into the Belle project has slowed as factions within the family are opposed to gambling, with the view that the second licence was in the balance. As such, Harrahs was linked with the second licence in the Philippines, as the US operator is keen to gain an Asian foothold but to date is without a presence in South East Asia. However, reports that SM Investments were in talks with Melco Crown Entertainment at G2E Asia appear accurate. Australian billionaire James Packer and Macau gambling tycoon Lawrence Ho are looking to sign a deal with the SM group to develop the casino project for a 20 per cent slice of Belle Corp. The Macau operator is set to take over the operation of the casino, which Belle had signed to Philippine bingo operator, Leisure & Resorts World Corporation. That deal would have seen Leisure & Resorts World get 15 per cent of net winnings, or 50 per cent of the casino's cash flow (as measured by EBITDA), whichever was higher. The likelihood now is that Melco Crown will take over Leisure & Resorts' operating rights and revenue, but the Philippine company will remain involved in the project in some capacity.

A further issue troubling the SM project is that of hotel rooms. Genting Resorts World Manila opened with 500 hotel rooms and through a staggered development added the requisite number (according to their licence) to take its tally to 800 hotel rooms which should, by rights, have been the minimum number with which the resort opened its doors. The SM Malls licence has exactly the same stipulation in its licence arrangement, but in their case PAGCOR is insisting that the full hotel room quota is met before the resort is operational. Having logically mirrored Genting and prepared 500 hotel rooms for launch, SM Malls must now add a further 300 rooms before PAGCOR will allow the second licence to open its doors. Such strict adherence to the licence conditions for one operator as opposed to another has led observers to conclude that the tacit licence conditions have not been observed in this case.

There has been a suggestion, not least from the AGA president Frank Fahrenkopf, that American companies are reticent about entering the Philippines market. Mr. Fahrenkopf told G3 in an interview at G2E Asia that no US operator will contemplate a Philippines operation. It's a stance that runs counter to opinions that Harrahs would bite off limbs to partake in market expansion in the Philippines, though Harrahs would predominately be involved in a management, not ownership, capacity.

PAGCOR is seen as a barrier to the market entry of many Nevada licence-holders in the US, not least the suppliers. One of the major US slot manufacturers is known to have only recently sent a team of lawyers to examine the Philippines market for exactly this reason. Their assessment, we are told, concluded that they 'had not seen any indication of corruption in the Philippines first-hand. It's such a



spectacularly diffuse statement that we're inclined to believe its authenticity.

The biggest recipient of gaming tax receipts in the Philippines is also the gaming industry's biggest detractor, the church. While priests mount demonstrations outside casinos, others are blessing the openings on behalf of their parish. In a similar predicament, PAGCOR sit in an awkward position as regulator and operator, which is beginning not only to be compromised from a regulatory viewpoint (as you might expect), but also from an operational perspective. PAGCOR simply can't measure up against an experienced operator such a Genting. Resorts World Manila is hurting PAGCOR's neighbouring locations - in a big way. Inviting international operators into your market to reap the licensing rewards is one thing, but to have them outperform you on your

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home turf is something that seems to have caught PAGCOR by surprise. The fact that any new slot, game or attraction at Resorts World Manila must be agreed in advance, in triplicate, by PAGCOR is a classic example of why competitors should not be regulators. The homologation of games has slowed to a crawl because PAGCOR currently insists that the latest games are 'tested' in its own locations before they're released to the rest of the market.

What's perhaps sticking in PAGCOR's craw is the fact that its 'City' project is just not happening. There are a series of articles in well respected publications that continue to describe the development of the Philippines market in relation to PAGCOR City. Nothing is actually happening as part of that project, with the current licences opening within Manila Bay, but as totally separate resorts. PAGCOR city is dead. It will not become the entertainment capital of Asia as it doesn't exist and is unlikely to come to fruition. Each licence holder is building separate individual resorts. All the casinos are to be within 10 miles of each other, but to describe them as part of 'PAGCOR City' would be disingenuous. Not that the relationship between PAGCOR and its status as regulator and operator is completely clear.

Outside of the major resort licences we've alluded to already, the fact that additional operators have locations in free port locations, from Clark to Subic Bay, confuses matters slightly. For the Philippines to be taken seriously as an internationally recognised gaming market, PAGCOR must stop operating and purely conduct itself as a regulator. It must relinquish its own operations and desist from taking its protective stance in regards to its own facilities. The highly publicised spat between PAGCOR and Thunderbird Casinos in 2011 centred around claims that Thunderbird had been operating without a licence since 2009, despite accepting taxes and licensing payments. PAGCOR threatened to close Thunderbird's Risal and Poro Point resorts unless it agreed to new operational provisions. Thunderbird responded by selling a large portion of its operations to a Philippines senator, a move that quelled all objections within PAGCOR. However, opinion now holds that with Thunderbird now safely out-of-reach, PAGCOR could turn its envious attention upon Resorts World Manila for being, in the words of a regional operator, 'too damn successful.' The view is that PAGCOR will don its operators cap and take a competitive stance to rein back Genting in its domestic market.

PAGCOR has made claims that it wants the Philippines to become the world's second largest gaming market. Notwithstanding the issues PAGCOR has with opening its market to international gaming companies, the market is unlikely to ever challenge the Singapore market, let alone Macau. While PAGCOR will certainly prove an obstacle to its own target, the infrastructure of the Philippines is likely to present the greatest challenge. The hours taken to travel between locations only miles apart is an unsurmountable issue at present. The fact that locals recommend that visitors walk in the centre of road, to avoid being dragged from the pavements and assaulted, poses additional obstacles not described in licensing agreements. The perception, real or otherwise, is that the Philippines is dangerous, poor and corrupt. It's a combination that has historically not played well with others - especially gaming.

At least Macau has had the decency to keep corruption within its government structure. The current scandal of choice in Macau concerns the Macau government looking to seize the site of the HKD$20bn "La Scala" development at the end of a

corruption trial in which two Hong Kong tycoons are accused of paying a HKD$20m bribe to the former Secretary for Transport and Public Works, Ao Man Long. The developer in question is Chinese Estates, which is building the HKD$20bn luxury housing project called "La Scala" on land opposite Macau Airport and near the city's Cotai strip and which has already pre-sold hundreds of flats. Macau's chief executive Chui Sai On has declined to rule out the possibility of the government seizing the five plots of land involved.

The latest opening in the Macau market, that of the Sands Cotai is currently performing above expectations. The casino occupies only a third of its allocated space, with over 1,000 slots still to be allocated across its floors. The present tables cap in Macau has forced the Sands Cotai to re-allocate tables from within its operations in Macau, moving them to the new location and filling vacant floor space with additional slots. The increasing requirement for slots in Macau is as a direct result of this 'Musical Tables' arrangement in which operators are circulating tables from location to location. Slot machine numbers are increasing to disguise the lack of tables per location, with hot and cold spots within the casinos determining which tables are moved from venue to venue. It's a situation that Wynn Resorts believes will have been resolved before it opens its Cotai resort, with the view that there will be no tables cap at the time of its launch mid-2015. Whether Wynn is guessing or knows this to be fact, is open to speculation.

In addition to Wynn Cotai, the development of Macau Studio City now appears to have recommenced. Macau Studio City is an integrated television/film production facility combining retail and hotels. Melco Entertainment took 60 per cent of the project following internal disputes that left the project in a three year limbo. Melco now plans to invest US$1.7bn to develop Studio City with a planned opening now scheduled for 2015 to coincide with the Wynn unveiling on Cotai. Last month, Melco Crown co-chairman Lawrence Ho said that Studio City will cost US$1.9bn and take 36 months to complete. Mr. Ho said the company hoped for a construction permit from the government enabling Studio City to open in 2015 with 300 to 400 gaming tables and 1,200 slot machines, pending government approval. This last part is critical, as Studio City was not originally slated to include any gaming facilities.

While the consensus of opinion among the major operators in Macau is that the table limit will be lifted in the near future, the restrictions on visitors from mainland China remains an issue for concern. Last month the mainland authorities once again tightened Individual Visit Scheme visas, reducing the number of allowed visits per person to three per year from the previous four.

GENTING, WITH ITS PERCENTAGE STAKES IN THE VAST MAJORITY OF LISTED GAMING COMPANIES, IS THE LARGEST OPERATOR ON THE PLANET.

In December 2011, Melco made a formal request to the Macau Economy and Finance Ministry to include a casino as part of the development. Melco sees the granting of its request as a formality, though as of yet it has not received confirmation one way or the other. Studio City was originally an SJM licence, but since the transfer to Melco has struggled with the perennial issue in Macau of a lack of builders. As Galaxy World on the Cotai Strip is currently doubling in size as part of its phase 2 expansion at a rapid pace, labour resources in Macau are at an all-time premium. It appears that Galaxy is developing phase 2 using internal resources only. If Galaxy can develop phase 2 of Galaxy World without calling upon external investment it will be an impressive feat, but also one that could see it competitively disadvantaged in the short-term.

Genting meanwhile remains on the periphery in Macau, though it has already invested in SJM and MGM in the US and is believed to have taken a substantial stake in Galaxy. In fact, Genting, with its percentage stakes in the vast majority of listed gaming companies around the world (with thresholds just below those required to publicly declare their interest) is thought to make Genting the world's largest gaming operator. The company's lack of representation in Macau is a glaring hole in its gaming portfolio and one that could be filled with a deal through Melco/Crown, which is why the current interest in Echo Entertainment in Australia is so interesting. James Packer has declared his interest in Echo just as Genting increased its shareholding and aspirations in Australia and Macau, two markets that the company has yet to conquer, though again its shareholding in all the major gaming companies in these markets leaves the company poised not to win licences, but to control the businesses that do.

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visas, reducing the number of allowed visits per person to three per year from the previous four. At the same time, current overseas spending limits on China UnionPay cards has been cut to RMB1 million (MOP1.25 million) per trip from RMB5 million to 10 million per trip. Mainland mass-market players traditionally use their UnionPay cards to bypass the limitations on the cash they are allowed carry from the mainland. Players use the UnionPay cards to buy watches and jewellery at Macau's pawnshops, immediately reselling them to get cash to fund their gaming activities. Visa and UnionPay restrictions could impact on the Macau gaming industry in much the same way that visa restrictions have slowed player activity in the past.

THE HO CHI MINH TRACK

Looking outside of Macau, much of the interest at the G2E Asia show focused on the opening of the MGM Ho Tram Strip. MGM have the management contract at the casino and do not hold the licence, however, the property's owners are said to be running short of funds, enabling MGM to 'help' with funding as it acquires shares in the licence-holder. What remains an issue for Ho Tram itself is that the area is meant to be a Strip, mirroring both Las Vegas and Cotai. While the latter is only now looking like a Strip as new properties open in close proximity to each other, the MGM development is currently the only location planed for Ho Tram.

While the attraction of a single destination on the Ho Tram 'Strip' might only dampen the appeal of the MGM Ho Tram, what will definitely impact the casino resort is the lack of infrastructure, namely a road from the capital of Vietnam, Ho Chi Minh City, to Ho Tram. The two hour ferry to the remote location isn't an appealing prospect for most players, so the construction of a highway linking MGM Ho Tram to the capital is a vital element in the development of the resort. Unfortunately, the Vietnamese government is believed to have reneged on its original agreement to foot the bill, demanding that the casino now absorb the construction cost. It's a stalemate that has attracted Las Vegas Sands Sheldon Adelson, who said at G2E Asia that he'd pay for the construction of the road as part of a building project of his own on the Ho Tram Strip, with one of his now infamous provisos that both locals and tourists be allowed to play at his location. At present, only tourists are allowed to play in Ho Chi Minh's gaming centres, spreading the idea that MGM Ho Tram is also a tourist-only location. However, there's nothing in the licence that stipulates this, with MGM Ho Tram currently not precluded from allowing Vietnamese nationals to gamble. The perception is that this is the case and the government could still impose this measure, but at present when the construction teams hand over the casino in October, with the casino planning to hit its February 2013 opening date, the 600 slots (to double by the end of 2013) and limited hotel rooms (again to double over the course of the year), will be able to welcome local players as things stand today.

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NAGAWORLD IS REPLACING ITS CONCESSIONS WITH SLOTS OF ITS OWN, GROWING FROM TODAY'S 450 SLOTS TO 1,200 IN THE NEXT FEW MONTHS.

Even if the MGM Ho Tram is forced to accept tourist-only play, operations such as NagaWorld in Cambodia have shown that this isn't too much of a hinderance. The number of dual passport holders have ensured that local play is profitable, while the shipping (or in the case of NagaWorld, the coaching) of players to locations has proved beneficial in the case of NagaWorld, with hotel and F&B capitalising on the stay-and-play customers visiting the destination.

The expansion of NagaWorld (see interview with Naga Corp's Timothy McNally), is a very public demonstration of the success of the NagaWorld model. A single licence holder in Cambodia, whose competition rings the borders of the country, NagaWorld has in the past sub-licensed its concession to additional operators, with RGB, Elixir, Heritage etc. all sharing in the success of NagaWorld. However, a shift in the attitude towards these sub-licencees has meant that NagaCorp is not renewing any of the sub-licences as they expire. NagaWorld is replacing its concessions with slots of its own, growing today's 450 slots to 1,200 in the next few months, with plans as NagaWorld 2 opens by 2015 for additional hotels, restaurants and up to 5,000 slot machines, making it one of the largest gaming operations in the region.

At G2E Asia, NagaWorld is known to have placed significant orders with slot manufacturers for the next phase of its slots floor expansion, with additional staff being hired as quickly as Naga Corp can find them.

THE ASIAN ROUND-UP

Singapore is currently interesting in that Marina Bay Sands has stolen the lead against Resorts World Sentosa. The Genting location has fallen back having been the market leader, with suggestions that the Malaysian operator has taken its eye off the ball in Singapore, enabling Marina Bay Sands to play leap-frog and gain significant market share at the expense of Resorts World Sentosa. Aside from the casinos, the there is also movement in the clubs market in Singapore, which have had to raise their game in relation to the competition from the casinos. These gentlemens' clubs have begun to place the latest machines and invest in ticket-in, ticket-out technology to keep pace with the changing expectations of players. The clubs are refreshing the games regularly, with each club able to increase the number of slots it offers in direct relation to the number of members it has on its books. Currently the clubs market in Singapore is a 2,000 machine market and one that presents an interesting opportunity for slots suppliers as they seek to keep pace with MBS and RWS by offering the latest and greatest slots and technology to their players.

Quickly rounding up the rest of the region; Taiwan is still trying to find an island that will accept casinos, with the view that until an island resort is established the more lucrative Taipei licence will never come to pass. Korea's Kangwon Land casino, the only one of seven casinos in the country able to offer games to locals, was recently described by the US media as in difficulties and losing money. The reality is that Kangwon Land is cash rich and performing extraordinarily well. The government in Japan is struggling to recover from the earthquake and desperately needs revenue. However, history shows that only strong governments pass gambling regulations, a position that presently eludes the current administration. The consensus in Japan is that casinos will pass into law, but this will take several more years. A view expressed by several parties is that when casinos do arrive in Japan, US operators will not get a look in. There was also heightened expectations at the G2E Asia show concerning Australia. Queensland is currently drafting a new bill to convert its 56,000 machine market to ticket-in, ticket-out. Victoria is also going through a state of flux, with the monitoring licence awarded to Intralot and expected to be in operation by August. It could take until February before the system is up and running fully.

Finally, an optimistic delegation from Vladivostok took a stand in Macau with a view to attracting the interest of operators to Russia's farthest flung corner. Currently three casino licences have been awarded in Vladivostok, with two casinos now operational with a small number of slots shared between them (around 200).

The city is an enormous shipping port with both local wealth and short travel times for neighbouring Chinese players. However, the Russian visa situation doesn't currently make it easy for Chinese nationals to visit the region - though this predicament failed to dampen interest in Macau, so perhaps the delights of one of Russia's hardest faced cities can sustain a reasonable sized industry - though any trade event can definitely go whistle.

AN OPTIMISTIC VLADIVOSTOK DELEGATION TOOK A STAND IN MACAU WITH A VIEW TO ATTRACTING OPERATORS.

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