

6 March 2024

Consumer Cyclical | Gaming

Gaming – NFO

Neutral (Maintained)

4Q23 Wrap: Bumpy Road To Recovery

Stocks Covered 2
 Rating (Buy/Neutral/Sell): 0 / 2 / 0
 Last 12m Earnings Revision Trend: Negative

- **Still NEUTRAL on number forecast operators (NFOs).** We believe the NFO stocks under our coverage should have high defensiveness, thanks to their dividend yields (5-7%) and the relatively inelastic demand from punters. That said, we think the current market valuations (close to mean levels) are fair, and the sector lacks re-rating catalysts for their earnings and valuations to reach new highs. We prefer Sports Toto (SPTOTO) on valuation grounds and its superior dividend yield.
- **4Q23 results below expectations.** SPTOTO's earnings fell short of expectations due to a higher-than-average prize payout resulting from a sizeable jackpot payout (Figure 5) during the quarter, coupled with higher-than-expected operating costs from HR Owen. That said, its DPS of 2 sen (YTD: 5sen) was within expectations. Meanwhile, Magnum's earnings and dividends exceeded our projections, due to our previous conservative forecasts. We upgraded the stock to NEUTRAL from Sell, as we see limited downside to valuations after lifting our forecasts.
- **Outlook.** We believe that lottery ticket sales in 1Q24 could swing north due to positive seasonal factors, particularly driven by the Lunar New Year period. Beyond the immediate term, the NFOs' management teams noted that illegal NFOs are gaining significant market share in two northern states, which are underserved, following the closure of legal NFO outlets. The path to sales recovery may not be straightforward due to the strong market share of illegal NFOs. However, we believe stricter legislation and enforcement, as well as the legalisation of online gaming could be key catalysts for the sector. However, it appears that such policies are not presently the Government's top priority.
- **Service tax hike.** The Government's decision to raise the service tax rate by 2ppts, from 6% to 8% starting Mar 2024, will impact the profitability of NFOs. NFOs have been absorbing similar taxes since the introduction of the Goods and Services Tax or GST in 2015, and the subsequent re-implementation of the Sales and Services Tax or SST in 2018. This additional increase further burdens them with taxes. Meanwhile, reducing prize payouts or increasing ticket prices could lead to decreased sales and a loss of market share to illegal NFOs. Therefore, NFOs must absorb these additional costs without adjusting ticket prices or diminishing prize payouts. We have taken into account the higher tax rates in generating our forecasts.
- **SPTOTO's HR Owen will continue to face challenges** from high inflation and interest rates in the UK. With higher depreciation and interest expenses from its newly launched Hatfield showroom, we believe HR Owen's GPM will remain under pressure. That said, we highlight that SPTOTO's dividends are mainly from its lottery business – so the challenges at HR Owen should not hamper the former's dividend payouts.
- **Key downside risks** include unfavourable luck factor and policies, as well as softer-than-expected ticket sales. The converse represents the upside risks.

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ESG scores for the gaming companies

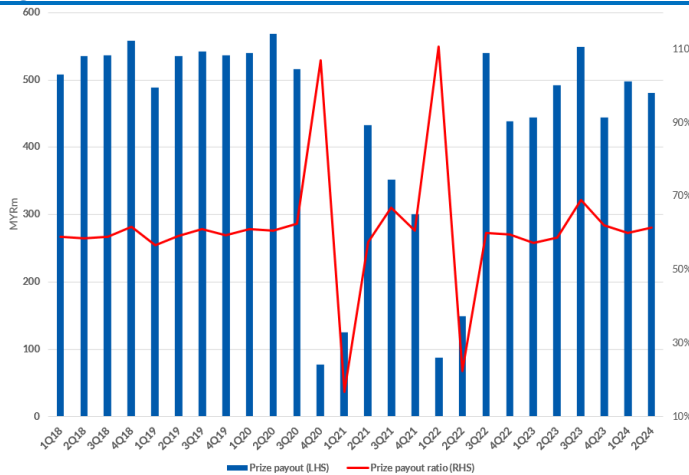
Company	ESG Score	TP Premium/ (Discount)
Sports Toto	3.1	2%
Magnum	3.0	0%

Source: Company data, RHB

Company Name	Rating	Target (MYR)	% Upside (Downside)	P/E (x) Dec-25F	P/B (x) Dec-25F	ROAE (%) Dec-25F	Yield (%) Dec-25F
Magnum	Neutral	1.13	(1.0)	12.6	0.7	5.2	5.5
Sports Toto	Neutral	1.55	9.1	9.8	1.6	16.7	7.6

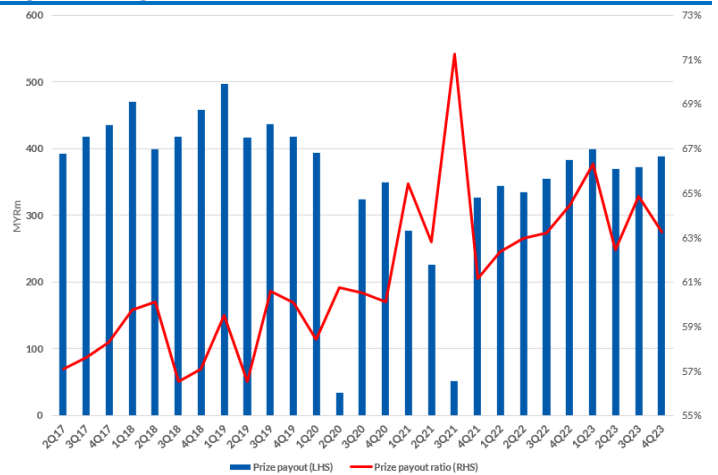
Source: Company data, RHB

Figure 1: SPTOTO's prize payout trend



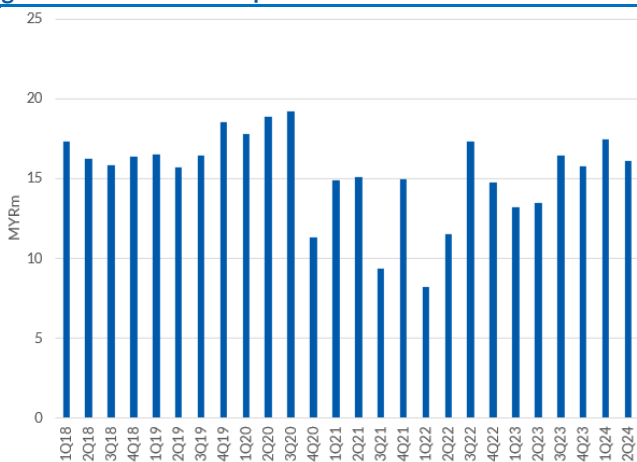
Source: Company data, RHB

Figure 2: Magnum's prize payout trend



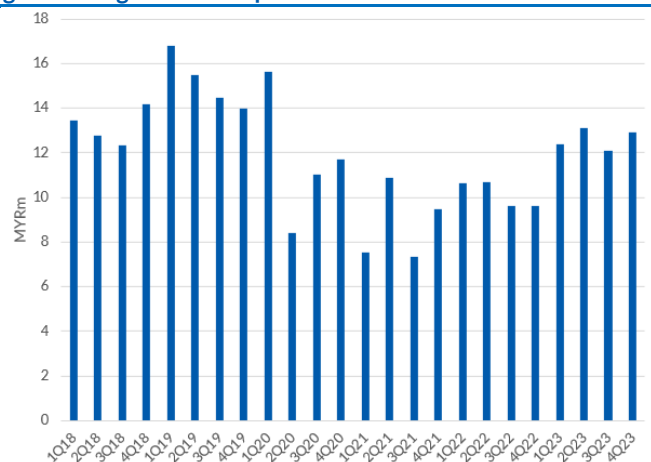
Source: Company data, RHB

Figure 3: SPTOTO's sales per draw trend



Source: Company data, RHB

Figure 4: Magnum's sales per draw trend



Source: Company data, RHB

Figure 5: SPTOTO's 2QFY24 Jackpot prizes

		2QFY23	1QFY24	2QFY24	QoQ	YoY	1HFY23	1HFY24	YoY
Draws		49	41	42	2%	-14%	94	84	-11%
Special Draws		8	2	2	0%	-75%	15	4	-73%
Average jackpot size	4D Jackpot	10,346,176	13,396,396	11,864,600	-11%	15%	10,484,629	12,630,498	20%
	Power 6/55	5,391,135	8,724,990	6,044,571	-31%	12%	5,736,858	7,384,781	29%
	Supreme 6/58	16,568,515	23,503,788	15,815,937	-33%	-5%	19,955,432	19,659,863	-1%
	Star 6/50	5,986,551	4,661,419	1,971,547	-58%	-67%	4,961,577	3,316,483	-33%
	Total	38,292,377	50,286,594	35,696,656	-29%	-7%	41,138,496	42,991,625	5%

Source: Company data, RHB

Figure 6: Magnum's 4Q23 Jackpot prizes

		4Q22	3Q23	4Q23	QoQ	YoY	FY22	FY23	YoY
Draws		48	41	42	2%	-13%	179	165	-8%
Special Draws		8	2	2	0%	-75%	22	8	-64%
Average jackpot size	4D Jackpot	7,388,435	8,986,077	12,209,664	36%	65%	7,039,075	9,725,556	38%
	4D Jackpot Gold	8,043,490	6,919,116	3,901,140	-44%	-51%	8,069,228	7,217,550	-11%
	Total	15,431,926	15,905,193	16,110,804	1%	4%	15,108,303	16,943,105	12%

Source: Company data, RHB

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