FINANCIAL REVIEW

HD **Keen eye on fate of Woolworths pubs**

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Investors are keeping a close eye on the hotel and gaming industry as supermarket giant Woolworths weighs up whether it will unload about $650 **million** worth of pubs and liquor stores through a **sale** to a trade buyer or press ahead with a sharemarket listing.

The pubs are held within ALH Group, which is 75 per cent owned by the supermarket and the remainder controlled by pub baron Bruce Mathieson. ALH is the country's largest and most profitable pub operator.

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If Woolworths opts for the trade **sale** route, analysts believe the country's largest owner of pub freehold properties, ALE Property Group, is in the box seat. ALE is one of the listed real estate sector's most solid performers, averaging a near 20 per cent compound return for the past decade. But although ALE has the potential to lob an aggressive bid, and could potentially tap shareholders for extra funds to finance the **purchase**, the trust has a distinctly conservative approach to acquisitions and has not bought a pub in five years.

ALE managing director Andrew Wilkinson and chief financial officer Andrew Slade made a presentation at the Credit Suisse Alternative Asset Conference earlier this month.

According to the Credit Suisse summary of the management presentation, ALE's assets – a high-quality portfolio of 86 pubs – "have demonstrated consistent value growth through volatile economic cycles with rent increases underpinned by embedded CPI [consumer price index]-linked growth.

"The high-quality nature of ALE's assets and lease structures justifies the relatively tight portfolio weighted average cap rate of 6.59 per cent."

What's more, "the bite-sized nature of ALE's pubs, which have an average value of $9.2 **million**, makes them highly liquid and attractive to a wide range of buyers".Petrol stations potentially attractive

The Credit Suisse note added ALE management viewed petrol stations "as a potentially attractive asset class" and also highlighted the opportunity to use its vacant land holdings on a number of the properties in its portfolio.

But other analysts say the risk for ALE is that if Woolworths opts to float its pub portfolio rather than pursue a trade **sale**, investors could start to question the trust's growth prospects.

Investors are paying particular attention to the fate of the Woolworths hotel arm, which owns more than 11,000 gaming machines, in the wake of Australian Gaming & Entertainment Limited's decision last month to pull its plans to float. The gaming-focused **company** failed to persuade investors to part with the $80 **million** needed to fund its **purchase** of five Sydney pubs and launch as a listed **company**.

Meanwhile, UBS Global Research has a buy recommendation on the country's two casino giants, Crown Resorts and Echo Entertainment Group. In a report this month, the UBS analysts trimmed their estimates of Crown's earnings for the next two years to reflect lower domestic earnings due to the softer than expected local economy and a number of one-off expenses. In addition, they expect the growth in earnings from Crown's Macau **operations** (it holds a 33.7 per cent interest in Melco Crown) will moderate as VIP demand slows.

Despite this, they argue Crown "remains compelling value in our view", trading on a price-earnings multiple of about 14 times estimated 2015 earnings. They add that "our forecasts do not incorporate potential upside from the Crown Sydney development [in Barangaroo] … or any potential from the coming Brisbane casino proposal."

They note that Crown's domestic casino licences are monopolistic and long-dated and that the **stake** in Melco Crown provides the **company** with an exposure to the high-growth Macau gaming market (which is now seven times the size of Las Vegas).

With respect to Echo Entertainment, the UBS analysts say the **company** has flagged it expects earnings before interest, tax, depreciation and amortisation (EBITDA) to rise to between $430 **million** and $435 **million** this financial year, above consensus estimates of $411 **million**.Significant improvement in operating performance

They point out this represents a significant improvement in terms of operating performance in the second half of the 2014 financial year, but say a key issue for the market will be whether Echo can maintain this operating performance into the 2015 financial year.

"We believe the outlook remains strong – with the benefits from the Queensland concessions expected to continue to benefit into the first half of 2015, improving momentum at Star, with the benefits of recent changes to player loyalty continuing to play out and expectations for ongoing cost control."

What's more they point out that although Echo's earnings are finally beginning to show some of the benefits from operational improvements and capital investment, "we note the stock continues to trade at a significant discount to peers".

UBS says that although the Queensland licence risk remains an issue, the market "is already pricing in over $500 **million** of value destruction in the current price for this issue".

This week, Echo threw down the challenge to Crown by teaming up two **Hong Kong** groups in the battle for Brisbane's second casino licence.

Echo is hoping to stop Crown trumping its existing 19-year-old Treasury Casino in Brisbane. Echo also operates The Star in Sydney and Jupiters on the **Gold** Coast and Jupiters Townsville.

**CO** aleprg : ALE Property Group | wolwth : Woolworths Limited

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