

Asia Entertainment & Resources Ltd.

HK Listing likely delayed, but still on; Thesis remains

Our Call

This morning, AERL announced its sponsor's (investment bank's) principal (banker) in charge of its HK listing application passed away. Due to this, we believe AERL's HK listing by introduction could be delayed to 1Q or early 2Q14 from December 2013.

This morning, AERL announced its lead banker in charge of its HK listing transaction passed away. The deceased banker has signed AERL's listing documents to date, including its draft prospectus filing. In the HK listing application process, a company's sponsor/lead banker is called on to verify the due diligence performed. Unfortunately, AERL's former lead banker will not be available for regulators, and if the information signed is inaccurate, the investment bank and the deceased banker are subject to civil and/or criminal liability.

We believe that AERL's Mainland China investment bank will assign a new lead banker that will need to perform personal due diligence before signing HK listing application documents. The deceased banker had interviewed over 200 agents and met with management multiple times. If a listing application is not approved before year-end, AERL will need to complete a full year audit before listing (its June audit – completed by its HK auditor - lasts 6 months). As such, we believe the likely timeframe for a listing by introduction is now late 1Q or early 2Q14.

While we find the likely delay of AERL's prospective HK listing disappointing given its expected benefits to its US share price, it does not change our overall thesis on shares.

Buy

AERL

Price: Last \$3.95

Price Target \$9.50

Leisure & Entertainment

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Company Data

Rating	Buy
Price: Last	\$3.95
Price Target	\$9.50
52-Week Range	\$2.70 - \$5.18
Market Capitalization (M)	\$236.0
Shares Outstanding (M)	60.0
Avg. Daily Vol. (000)	201.0
Dividend	\$0.28
Dividend Yield	7.1%
Assets (M)	\$377.5

FYE Dec	2013E (Curr)	2014E (Curr)	2015E (Curr)
EPS (\$)			
Q1 (Mar)	0.32A	0.21	0.24
Q2 (Jun)	0.21A	0.22	0.27
Q3 (Sept)	0.16	0.24	0.30
Q4 (Dec)	0.20	0.27	0.33
FY EPS	0.85	0.95	1.14
P/E	4.6x	4.2x	3.5x

Price Performance



Source: FactSet

Important Disclosures regarding Price Target Risks, Valuation Methodology, Regulation Analyst Certification, Investment Banking, Ratings Definitions, and potential conflicts of interest begin on Page I of the Appendix Section.

Quarterly Income Statement

(Millions, except per share data)	DEC CY12	Mar 13 Q1:13	Jun 13 Q2:13	Sep 13 Q3:13E	Dec 13 Q4:13E	DEC CY13E	Mar 14 Q1:14E	Jun 14 Q2:14E	Sep 14 Q3:14E	Dec 14 Q4:14E	DEC CY14E	Mar 15 Q1:15E	Jun 15 Q2:15E	Sep 15 Q3:15E	Dec 14 Q4:15E	DEC CY15E
REVENUE																
Cage Capital Est.	262.35	300.58	302.96	307.52	318.49	318.49	309.08	321.53	327.40	337.17	337.17	330.25	345.21	362.72	376.56	376.56
Turns per month Est.	5.79	4.83	4.93	5.10	5.83	5.17	5.53	5.77	5.83	6.23	5.84	5.58	6.10	6.20	6.37	6.06
Rolling Chip Turnover	18,196.0	4,070.0	4,460.0	4,711.8	5,504.4	18,746.2	5,302.2	5,489.4	5,705.1	6,240.5	22,737.3	5,694.8	6,223.4	6,596.4	7,099.6	25,614.3
% seq.	-9%	-1%	10%	6%	17%	3%	-4%	4%	4%	9%	21%	-9%	9%	6%	8%	13%
% yoy.	-9%	-24%	-5%	17%	34%	3%	30%	23%	21%	13%	21%	7%	13%	16%	14%	13%
Fixed Commission Operation																
Roll from fixed commission operation	15,628.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
% of total rolling chip win	117%	0%	0%	0%	0%	100%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Revenue from fixed Commission	160.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
% commission rate	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%
Revenue Share Operation																
Win from revenue share operation	na	4,070.0	4,460.0	4,711.8	5,504.4	18,746.2	5,302.2	5,489.4	5,705.1	6,240.5	22,737.3	5,694.8	6,223.4	6,596.4	7,099.6	25,614.3
% of total rolling chip win	na	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Gross Revenue from revenue share	na	60.4	63.5	63.0	73.0	240.4	70.3	72.8	75.8	82.9	301.7	75.6	82.7	87.6	94.3	340.2
% VIP hold	2.85%	3.33%	3.15%	2.93%	2.90%	2.85%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%	2.90%
% revenue share rate	45.0%	45.6%	45.2%	45.6%	45.7%	45.0%	45.7%	45.7%	45.8%	45.8%	45.8%	45.8%	45.8%	45.8%	45.8%	45.8%
Gross Revenue Est.	216.6	61.9	63.5	63.0	73.0	240.4	70.3	72.8	75.8	82.9	301.7	75.6	82.7	87.6	94.3	340.2
Adjustment, including Service Revenue	0.0	2.5	0.0	2.5	2.9	7.9	2.8	2.9	3.0	3.3	12.1	3.0	3.3	3.5	3.8	13.6
% of gross revenue	0%	4%	4%	4%	4%	3%	4%	4%	4%	4%	4%	4%	4%	4%	4%	4%
Revenue from VIP gaming operations	236.3	64.4	63.5	65.5	75.9	248.3	73.1	75.7	78.8	86.2	313.8	78.7	86.0	91.1	98.1	353.8
% yoy.	-6%	-4%	9%	21%	34%	5%	14%	19%	20%	14%	26%	8%	14%	16%	14%	13%
EXPENSES																
Commission to Junket agents	220.6	40.3	47.7	47.4	54.4	189.7	51.2	53.0	54.8	59.8	218.7	54.7	59.5	62.7	67.1	244.0
% of Rolling Chip Turnover	0.83%	0.99%	1.07%	1.01%	0.99%	1.01%	0.97%	0.97%	0.96%	0.96%	0.96%	0.96%	0.96%	0.95%	0.95%	0.95%
SG&A	18.3	5.9	6.3	5.9	6.0	24.1	6.1	6.1	6.1	6.1	24.4	6.1	6.2	6.2	6.2	24.7
% of Rolling Chip Turnover	0.101%	0.145%	0.142%	0.125%	0.109%	0.129%	0.115%	0.111%	0.107%	0.098%	0.107%	0.107%	0.100%	0.094%	0.087%	0.096%
Special Rolling Tax	1.8	0.4	0.4	0.5	0.6	1.9	0.6	0.6	0.6	0.7	2.4	0.6	0.7	0.7	0.8	2.8
% of total revenue	0.8%	0.6%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%
EBITDA	61.6	15.3	11.9	11.8	14.9	53.9	15.2	16.0	17.3	19.6	68.2	17.3	19.6	21.5	24.0	82.4
% margin	26%	24%	19%	18%	20%	22%	21%	21%	22%	23%	22%	22%	23%	24%	24%	23%
% of Rolling Chip	0.34%	0.38%	0.27%	0.25%	0.27%	0.29%	0.29%	0.29%	0.30%	0.31%	0.30%	0.30%	0.31%	0.33%	0.34%	0.32%
D&A	6.6	2.4	2.5	2.4	2.4	9.8	2.4	2.4	2.4	2.4	9.6	2.4	2.4	2.4	2.4	9.6
Income including pre-acquisition profit	55.0	12.9	9.4	9.4	12.5	44.2	12.8	13.6	14.9	17.2	58.6	14.9	17.2	19.1	21.6	72.8
Prior owners' interest in pre-acquisition profit*	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Income Attributable to ordinary shareholders	55.0	12.9	9.4	9.4	12.5	44.2	12.8	13.6	14.9	17.2	58.6	14.9	17.2	19.1	21.6	72.8
% Margin	23%	20%	15%	14%	16%	18%	18%	18%	19%	20%	19%	19%	20%	21%	22%	21%
Other Comprehensive Loss																
Foreign Currency Translation adjustment	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Adjusted Income	55.0	12.9	9.4	9.4	12.5	44.2	12.8	13.6	14.9	17.2	58.6	14.9	17.2	19.1	21.6	72.8
Adjusted EPS	1.30	0.32	0.21	0.16	0.20	0.85	0.21	0.22	0.24	0.27	0.95	0.24	0.27	0.30	0.33	1.14
% yoy.	-29%	-21%	-38%	-50%	-16%	-34%	-34%	6%	54%	34%	11%	13%	22%	25%	22%	21%
Ave shares outstanding	42.4	40.7	44.6	60.2	61.3	51.7	61.3	61.3	62.0	63.1	61.9	63.1	63.1	63.7	64.8	63.7

Note: 2Q13 Ajd EBITDA, net income and EPS adds back \$2.8m in one-time expenses related to HK Listing and acquisition costs.

Source: Company reports and Sterne Agee estimates

APPENDIX SECTION

Company Description:

Macau licensed casino operators grant AERL exclusive use of VIP gaming rooms within their casino facilities and AERL promotes and manages its own network of junket agents and players to optimize the casino gaming within the rooms. In return, AERL is paid on volume-based commission or a share of the gaming win. ~85% - 90% of VIP player chip volume in Macau casinos is generated utilizing the room promoter system.

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Company Specific Risks:

Risks to AERL include softness in the Chinese economy; unanticipated Mainland Chinese government intervention/regulation, including visa controls or other aspects negatively impacting visitation or patron spend in Macau; unanticipated Macau Government legislation; and/or the potential for higher junket operator commissions paid by promoters.

Valuation Methodology:

Methodology for assigning ratings and target prices includes qualitative and quantitative factors including an assessment of industry size, structure, business trends and overall attractiveness; management effectiveness; competition; visibility; financial condition; and expected total return, among other factors. These factors are subject to change depending on overall economic conditions or industry or company-specific occurrences. Sterne, Agee & Leach, Inc., analysts base valuations on a combination of forward looking earnings multiples, price-to-revenue multiples, and enterprise-value-to-revenue ratios. Sterne, Agee & Leach, Inc., believes this accurately reflects the strong absolute value of earnings, the strong earnings growth rate, the inherent profitability, and adjusted balance sheet factors. Additional company-specific valuation methodology is available through Sterne, Agee & Leach, Inc.

Company Specific Valuation:

Our valuation is based on a multiple of earnings per share.

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BUY: We expect this stock to outperform the industry over the next 12 months.

NEUTRAL: We expect this stock to perform in line with the industry over the next 12 months.

UNDERPERFORM: We expect this stock to underperform the industry over the next 12 months.

RESTRICTED: Restricted list requirements preclude comment.

Ratings Distribution:

Rating Category	Count	Percent	IB Serv./ Past 12Mos.	
			Count	Percent
Buy	226	47.58%	30	13.27%
Neutral	229	48.21%	14	6.11%
Underperform	20	4.21%	1	5.00%

ADDITIONAL INFORMATION AVAILABLE UPON REQUEST: Contact Robert Hoehn at 1-212-338-4731.

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