Hold or Fold: Should PAGCOR Sell Its Casinos?

Is the company a regulator or an operator? Some experts believe it's time to make a choice | By Andrew Klebanow

PAGCOR Heritage, downtown Manila

As the Covid-19 pandemic continues to wreak havoc on economies throughout the world, governments are exploring ways to recover lost tax revenues by privatizing certain industries under their control. Such is the case in the Philippines, where politicians are proposing the sale of casino assets owned and operated by the Philippine Amusement and Gaming Corporation (PAGCOR).

This is not the first time that the topic of privatization has been broached. Calls for PAGCOR to divest its gaming assets so the agency can devote its complete attention to casino regulation have come up numerous times in the past. The question is, is now the ideal time to sell?

Understanding the Roles of PAGCOR

PAGCOR performs a variety of vital functions. It is the regulator of all games of chance in the Philippines and oversees the privately owned casinos including the integrated resorts in Entertainment City and other casinos located in resort destinations. In addition, PAGCOR regulates other forms of gaming such as e-game cafes, sports betting and electronic bingo outlets.

These operations can be found throughout the provinces and collectively are sizable enterprises. There are approximately 26,000 electronic bingo machines serving the local population. In addition, there are approximately 200 e-gaming cafes, each with 50-100 machines that can be found in malls and storefronts throughout the country.

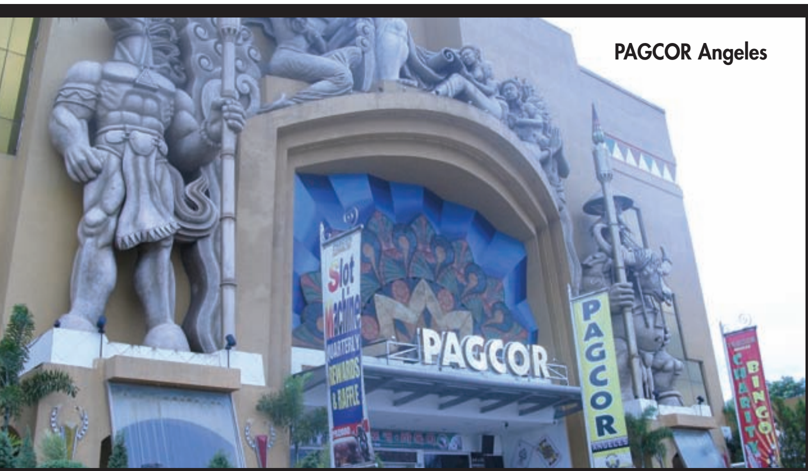
In 2016, PAGCOR took over regulation of the country's offshore gaming operations. Referred to as Philippine Offshore Gaming Operations or POGOs, these are essentially casinos housed in studios that feature a variety of table games staffed by live dealers.

Players residing outside of the Philippines can log onto one of the country's 60 online casinos, select a game and dealer, place real-money wagers, and observe the outcome in real time on their computers or mobile devices. Filipino citizens, regardless of where they live, are prohibited from wagering on these online portals. POGOs have become massive enterprises, and have become an important source of gaming tax revenue. They have also had a material impact on the commercial real estate markets, since they require copious amounts of office space. Their size and rapid growth have put pressure on PAGCOR to devote more resources to better regulate this industry.

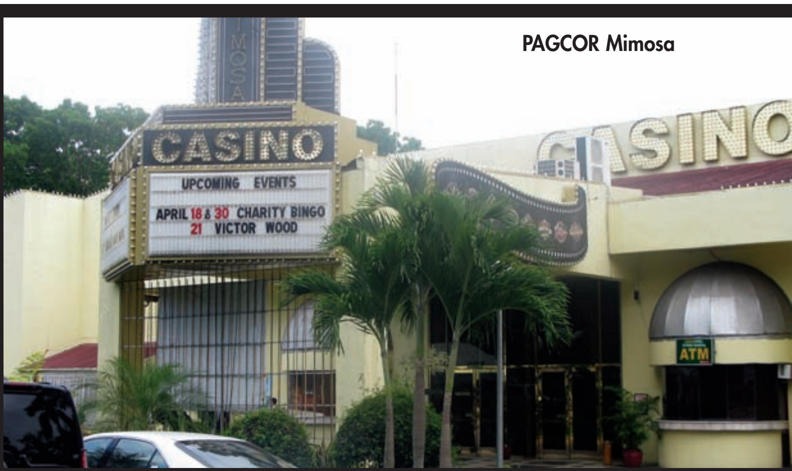
PAGCOR is also an operator of various casino enterprises, and these are the assets that private casino operators prize. PAGCOR operates casinos under the Casino Filipino brand. Located in popular tourism destinations, they serve a mix of locals and visitors. While PAGCOR owns these businesses and their gaming licenses, they do not own the properties in which these casinos are housed. In addition, PAGCOR operates 32 satellite casinos. They can often be found in hotels, and are operated as joint ventures with those hotels' owners. Once again, PAGCOR does not own the real estate in which these casinos are located. They simply own the licenses and operate the casinos.

PAGCOR has enjoyed robust growth, and is the third largest revenue contributor to the central government. As such, PAGCOR, in its current configuration, plays a vital role in supporting government services. In 2019, PAGCOR saw an 11.2 percent year-over-year growth in gaming revenue. It also employs 11,000 workers. Nevertheless, as the costs of dealing with the pandemic rise, there are calls for PAGCOR to cash out its casino operations.

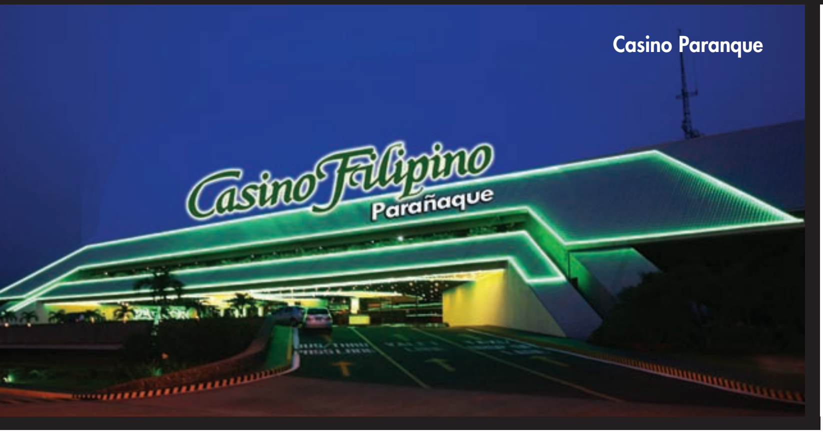
The initial questions that one must ask are, what is the value of these various gaming assets, and will a sale of those gaming assets exceed the annual contributions that PAGCOR makes to the central government? PAG-



PAGCOR Angeles



PAGCOR Mimosa



Casino Paranque

COR does own the gaming devices, table games, casino furnishings and underlying casino management system that serve as the backbone of each casino's accounting and marketing system.

Because of its commitment to upstream profits, PAGCOR must constantly weigh the benefits of updating its slot machines and gaming environments against the contributions it is obligated to make to the National Treasury. Invariably, it is the latter that wins, and, while PAGCOR's Casino Filipino properties provide an adequate gaming environment, the privately run casinos in Entertainment City offer a far more compelling gaming and entertainment experience. Any purchaser of a Casino Filipino or satellite casino will have to invest in new gaming equipment and casino management systems, and improve the gaming environments in order to grow revenue. Those capital costs must be factored in when trying to determine an appropriate price to pay for a particular casino.

In normal times, placing a valuation on a particular gaming asset is a fairly straightforward exercise. An examination of past gaming revenue performance coupled with an analysis of demographic trends within the primary markets would yield a forecast of future gaming revenue. Unfortunately, these are anything but normal times. The closure of the nation's casinos in order to stem the growth of the pandemic makes it very difficult to predict how quickly gaming revenue will recover.

What is certain is that social distancing strategies will reduce gaming capacity and with it, gaming revenue. In addition, it is impossible to predict if gamers will return and play at levels they did in the past. Also, without a widely available vaccine, the pandemic could once again escalate and force the central government to again implement lockdown measures. Given this uncertainty, any potential buyer will want a substantial discount on the proposed sale price.

An Act of Congress

PAGCOR was created by virtue of a presidential decree issued by President Ferdinand Marcos in response to calls for the Philippine government to put a stop to the proliferation of illegal casino operations. The decree was later amended and consolidated and is known as the PAGCOR charter.

In 2007, the Philippine Congress passed Republic Act No. 9487, extending the corporate life of PAGCOR by 25 years to regulate and operate games of chance, to issue licenses, and to enter into joint-venture, management and investment agreements with private entities. This led to the development of the highly successful Entertainment City integrated resort complex in Manila Bay. It would literally take an act of Congress to change PAGCOR's Charter and allow it to sell its casino assets. This is no small task.

Who Are The Likely Buyers?

Another question that arises: Should Congress authorize the sale of PAGCOR's casinos, who would be the likely buyers? The Casino Filipino properties represent an enticing opportunity, particularly for those casino operators who are familiar with both the local gaming and tourism markets.

Possible buyers might include Bloomberry Resorts, owner of the highly successful Solaire Resort Casino; Belle Corporation, the company that owns the land on which City of Dreams sits; and a few other Philippine-based companies that have ownership interests in other gaming enterprises and ready access to cash. The satellite casinos would probably garner the interest of the individual hotel operators where these casinos are located. The question again is, what price would they be willing to pay, given the uncertainty in trying to predict future gaming revenue?

Another issue that would have to be addressed is the future of PAGCOR employees and retirees. Those retirees rely on pensions that must continue to be funded, and current employees have received commitments from PAGCOR for future benefits. It is unlikely that any buyer of a casino would be willing to assume those liabilities.

PAGCOR remains under enormous pressure. The rapid growth of the POGO industry will require additional resources in order to regulate online gaming activities. The reopening of its Casino Filipino and satellite casinos also remains a challenge, as is its ability to regain the momentum those properties had prior to the pandemic.

PAGCOR's recent success and the robust contributions it made to the National Treasury have created expectations that those payments will continue. Faced with all of this, it may be tempting to explore the sale of its casino assets. Nonetheless, given the market's uncertainty, the steps required to effect a sale, and potential buyers' reluctance to pay a high price for those gaming assets, now may be the worst time to sell those assets.

Given all this, the most prudent course may be to hold onto the assets until a more opportune time arises.

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