China's president just declared war on global gambling

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News

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Chinese President Xi Jinping has officially declared war on the global gambling industry, warning foreign casinos that Chinese citizens will be gambling much less in China, neighboring countries, and the US.

"Some foreign countries see our nation as an enormous market, and we have investigated a series of cases," said Hua Jingfeng, a deputy bureau chief at the Ministry of Public Security. "A fair number of neighboring countries have casinos, and they have set up offices in China to attract and drum up interest from Chinese citizens to go abroad and gamble. This will also be an area that we will crack down on."

In other words, Xi is telling companies around the world that saw their revenue triple when Macau opened up to foreigners that the Chinese gambler will not be following them abroad to countries like Singapore and the Philippines where billions have been spent on new projects to attract those same people.

Asian companies have heretofore capitalized on the traveling Chinese gambler in the Philippines, Australia, and especially Singapore. A combination of tax credit and increased gambling revenue in Singapore saved Las Vegas Sands' fourth-quarter earnings. Now that's set to take a hit.

And Chinese gamblers apparently won't be going to Macau as much to gamble, either. Xi's government has sworn to cut down on advertisements — sometimes in the form of annoying text messages — promoting Macau casinos. Visa restrictions will tighten, according to analysts, and even retail gamblers will have their money tracked as officials monitor UnionPay, the only domestic bank card in mainland China.

The latest announcement goes above and beyond the pain Xi's administration has already put Macau's casinos, and the world's casino companies, through over the past year. The president's anticorruption crackdown has slowed the movement of mainlanders to the island — the world's largest gambling center — dramatically.

Gaming revenue in Macau contracted for the first time since foreign companies were allowed to do business on the island in 2002. It plummeted 30% in December alone. The junket system, Macau's financing system for high rollers most affected by the anticorruption drive, is on life support after 16% of junkets closed in 2014.

So Xi's declaration is coming when companies around the world — from MGM to Las Vegas Sands, from Macau-based companies Melco to SJM Holdings — are at their most vulnerable.

Casinos, especially foreign firms, have given no indication that they saw this coming. On a conference call earlier this week , Steve Wynn, CEO of Wynn Resorts, lamented his company's weak fourth-quarter earnings, and struck an almost defeated tone about the government's control over the future of his business.

"China remains a big question mark. We have more questions than answers, thousands of our Macau employees are anticipating promotion and a better life because of Wynn Palace ... We have learned in the last 12 years to behave in China, and that is to listen carefully to what the leadership says and to conform with the program as we are their guest," said Wynn. "We wait for an announcement from the government with baited breath ... What we are seeing in China is an entrenchment."

He said he could only hope "our ambitions to grow in Macau will continue to develop" and that that was the only kind of statement he could appropriately make at the moment.

At the same time, he assured listeners that Wynn's dividend was not at risk in the near future, and that the company would continue to diversify its offerings in Macau away from gambling and toward more hospitality. He was still talking about building in 2016.

Xi's declaration against foreign companies is likely not the announcement Wynn was hoping for.

Now, the Chinese government will be hitting the global gambling industry on two fronts. One is in Macau, where Wells Fargo analyst Cameron McKnight argues that the anemic revenue we saw in the last quarter or two of 2014 is here to stay.

In a recent note, McKnight wrote:

China's President Xi Jinping has stated that China must adapt to a "new normal" as the government balances economic reform with healthier and more sustainable growth.

We believe Beijing has imparted this view on Macau and is targeting Macau market growth that is in line with that of the broader Chinese economy.

The government has deliberately slowed growth through several policy actions: (1) visa restrictions, (2) the anti-corruption campaign, and (3) UnionPay monitoring. We believe the Macau government has embraced the "new normal" environment, evidenced by the changes in government leadership and a tough stance on smoking, dealer labor, and gaming tables.

Indeed, as the chart above shows, junket financing for China's high rollers — the people who contribute most heavily to Macau's gaming revenue — correlates with the country's total social financing (TSF) . TSF is a measure the Chinese government created in 2011 to paint a more accurate picture of credit growth in the country. It includes debt held by nonstate entities, and the Chinese government is trying (often unsuccessfully) to get that number to shrink.

That means Macau will shrink too — at least until it becomes a land of Cher concerts and family-friendly restaurants.

One of the worst parts of all of this for casino companies is that they've spent about $23 billion on new Macau projects set to open over the next year or two, according to Union Gaming Research.

It's going to be a very ugly 2015.

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