

Global Gambling Giants Place High Bets on Japan Casinos

Passing the hunched denizens of a neighbourhood pachinko parlour late at night, their fingers flying on the pinball-slot machine hybrids that have entranced the country for decades, it is easy to imagine the potential for casinos in Japan.

While gambling for cash is technically illegal in Japan, pachinko operators have managed to skirt this issue through having players win prizes, rather than money (although later traded for cash). There are also exceptions to the law that allow for betting on public sports such as football, horse racing and boat racing and also on the state run lottery, given their promotion of industry, sports and the public good and their raising of funds for local governments.



After nearly 15 years of deliberation it appears that a ban on casinos in Japan may be lifted this year. A number of factors are believed to have contributed to this long-awaited deregulation, among them: The Olympic Committee's 2013 selection of Tokyo as the host of the 2020 Olympic Games and thus the assumed encouragement of tourism, as well as the "Abenomics" growth programme of economic liberalisation introduced by prime minister Shinzo Abe, who himself reportedly stated in 2013 that there would be "significant merit" in casino legalisation. Mounting government debt and the success of casinos in nearby Macau and Singapore, along with their notable revenue generation, are also believed to have spurred fresh hopes for a casino industry's potential to assist in the revitalisation of Japan's economy. From the casino operators' viewpoint, Japan's wealthy population renders it an enticing market, as does its geographical position to China, where some of the world's most prolific gamblers are based.

Key Players and Local Partners

Global gaming industry giants are already seeking entrance into the potential Japanese market, with major players such as Wynn Resorts Ltd., MGM Resorts International, Las Vegas Sands Corp. and Caesars Entertainment Corp. announcing sweeping plans for investment. Not surprising given the benefits as highlighted by a senior source within one of these companies, "There isn't a hugely competitive local set of players, it's going to be well-regulated, and it's a rich country."

Sheldon Adelson, Chairman and Chief Executive Officer of Las Vegas Sands Corp., announced earlier this spring that he would "spend whatever it takes" to build in Japan. Wynn Macau's President Gamal Aziz has stated that Wynn will pour far more into Japan than its current US\$4 billion investment in Macau's Cotai Strip,¹ while MGM has claimed it will invest "several billion," and even Macau-based Melco Crown Entertainment is slated to invest a minimum of US\$5 billion.²

Most major casino operations have expressed an interest to invest in casino resorts in Tokyo and Osaka, with Tokyo's large and well-off population and Osaka's comparatively cheaper, faster development cited as benefits. However, a number of prefectures, among them Hokkaido, Chiba, Nagasaki and Okinawa, as well as Chiba and Yokohama cities, were all said to have earmarked budgets as of April 2014 for casino-related studies this fiscal year.³

Concerns over Legislation

While clearly there is much speculation and anticipation as to the potential of the casino legislation, it should be noted that extensive regulatory deliberation and drafting could slow down the process for opening a casino — making it difficult to realistically open any casinos before the 2020 Olympics. The drafting of regulatory frameworks would be expected to take up to a year to work through and without a clear understanding of what this regulation will look like, it is difficult for any party to present concrete plans at such an early stage. In addition, construction work could take potentially take at least three years to complete.

Questions have been raised regarding return on investment in the country's gaming sector. While Macau's largest gaming operators expect a 20% return on investment, Morgan Stanley cautioned in April that the actual return could be less than half of expectations.⁴ Labour shortages during the Olympics

¹ <http://www.bloomberg.com/news/2013-09-18/abe-ally-to-submit-casino-bill-as-wynn-mgm-plan-investments-draft.html>

² <http://www.reuters.com/article/2014/04/09/us-melcocrownentertainment-japan-idUSBREA3726E20140409>

³ http://ajw.asahi.com/article/behind_news/social_affairs/AJ201404150004

⁴ <http://macaubusinessdaily.com/Gaming/Reality-check-Japan>

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preparation could also prove to be an issue, as well as larger-than-projected budgets due to soaring property prices, increasing taxes and high construction costs.

It is unlikely that foreign companies will wish to or indeed be able to enter the Japanese market without engaging in joint ventures with local partners. Large Japanese corporations would be able to provide necessary real estate development experience, while gaming companies such as Konami Corp. and Sega Sammy Holdings Inc. — the latter of which has already helped to develop a US\$1.7 billion casino near Seoul — would contribute gaming technology and overseas casino development expertise. Local companies, such as TV and publishing group Fuji Media Holdings, construction company Kajima and property developer Mitsui Fudosan, are also lobbying for casino development, notably pushing for a casino in seaside Odaiba. Pachinko operators are also eager to be involved, with Dynam Japan Holdings Co. reported in April to be in discussion with several Asian gaming operators.

Concerns have also risen in Japan over the social impact casinos could have on the country, particularly with regards to addiction, anti-social behaviour and the gaming industry's purported gangster connections. Critics have highlighted the effect of casinos on other communities, such as in South Korea's northern Gangwon province where a once-thriving small town has been ravaged over the past decade by gambling addiction, suicides and thousands of citizens fleeing the area.

Whether current profitability estimates ultimately prove overconfident, most still believe that casino legalisation could make Japan the world's third largest gambling market after Macau and the U.S., with projected annual revenue of over US\$40 billion.⁵ From Las Vegas to Macau, casino operators are eagerly awaiting the next step in government approval, with legalisation supporters aiming to pass their bill through the Diet before the current parliament session ends in late June.

Our Assessment

Casino legislation is undeniably a major prospect for Japan and as such it would be seen as unlikely that it will not be implemented. While there is much current speculation and discussion among the industry players about the opportunities, it should be noted that 2020 is an ambitious target. Preparation and activity related to the Tokyo Olympics will certainly take precedence and could result in casino plans being further delayed.

⁵ <http://www.reuters.com/article/2014/05/28/konami-gambling-japan-idUSL3N00E18R20140528>

The major incentive for Japan is tourism and for this reason it should be expected that Japan will look to adopt an integrated resort model rather than to just build and develop casinos. This will present more opportunity for hotels and leisure facilities, and for retail to provide further investment opportunities related to the market.

Discussions around the social impact are relevant and will also be a significant factor in determining possible locations and buy-in for the success of any potential gaming operation/s. For this reason we expect a highly regulated and restrained approach to licensing and resort development.

Entering the Japanese Market

As the world's third largest economy, Japan is of major importance to global organisations across a wide range of industries. However, despite Japan's clean business image, recent media attention has served to highlight the existence, and more importantly, the risks of corruption, fraud and association with organised crime.

Clients should beware of the potential pitfalls of conducting business in Japan, many of which are not immediately identifiable without a current and innate understanding of the country's complex and often opaque operating environment.

In securing an advantageous position and competitive edge, companies should develop and implement an informed and strategic approach to market entry that takes into account local best practices. In particular, companies looking to take advantage of the casino legislation should look to:

- Understand the key players and influencers within government and industry bodies who will be engaged in legislative and regulatory discussions and finalisation.
- Undertake increased monitorship of the legislative and approval processes.
- Gather intelligence on market trends and industry movements to assist with the acquisition of a license.
- Implement compliance-related procedures to enhance internal controls and anti-bribery and corruption risk policies.
- Protect their operations against the elevated risk of anti-social forces/organised crime involvement or influence directly or indirectly in business operations.
- Conduct comprehensive background checks and reputational due diligence on potential third-party contractors and business partners.

Businesses should keep in mind, while new legislation around casinos have the potential to bring in substantial return on investments, rushing into the process without adequate protection from local business risks could potentially erode and destroy any expected value.



Ben Fouracre
Managing Director
+81 3 5369 3933
ben.fouracre@fticonsulting.com

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