

GVC Holdings

Excellent interim results

Interim results

GVC's interims demonstrate the rapid progress it is making integrating bwin, with proforma EBITDA up 42%. In a confident statement management believes the group's organic growth potential is greater than originally anticipated; it plans to increase marketing investment to take advantage of new opportunities. Our EPS estimates have increased, as has our 2016 EBITDA forecast (up 3%), but our 2017 EBITDA is unchanged to allow for regulatory and tax headwinds. Management is delivering on its ambitious targets yet the 2017e EV/EBITDA is below the peer group average at 10.1x.

Year end	Revenue (€m)	EBITDA* (€m)	PBT* (€m)	EPS* (dil) (c)	DPS (c)	P/E (x)	Yield (%)
12/14	224.8	49.2	41.3	61.4	55.5	13.7	6.6
12/15	247.7	54.1	50.0	76.4	56.0	11.0	6.6
12/16p**	860.0	202.1	102.9	31.3	0.0	27.0	0.0
12/17e	890.0	250.0	188.4	56.2	25.0	15.0	3.0
12/18e	937.0	285.0	234.0	69.0	32.5	12.2	3.9

Note: *Normalised, excluding amortisation of acquired intangibles, exceptional items and share based payments. ** Pro forma includes 12 months of bwin.

Reaching milestones ahead of schedule

Bwin synergies are coming through slightly ahead of target and management is confident that the integration will be complete by end Q217 and full €125m of cost savings secured. With both GVC and bwin labels delivering H116 top-line growth, marketing cost is to be increased from the current 21% of revenues, with plenty of scope for revenue synergies through improved cross-selling. Meanwhile the senior management team has been strengthened, product enhancements are underway, the New Jersey gaming licence has been confirmed and a B2B deal with Betfred (the UK's fourth-largest bookie) demonstrates the value of the group's IP.

Proforma H116 clean EBITDA up 42%

Reported interim results only include five months of bwin so the proforma comparison is more useful: H116 EBITDA of €104.4m, up 42%. We have increased our 2016e proforma EBITDA from £196.5m to £202.1m and raised our normalised EPS estimate by 17% (mainly lower D&A). Our 2017 and 2018 EBITDA estimates are unchanged to allow for some pressure on margins from the extension of the UK POC tax to free play (from August 2017) and additional costs in newly regulating markets. However, we have increased our EPS estimates (2017e up 6%). Cash flows are stronger than we forecast and we expect net debt to fall to €145m at end 2016 (previously €185m) and for GVC to be cash positive at end 2018.

Valuation: Strong upward momentum

GVC shares have risen by 55% since the start of 2016 as the success of the bwin deal has become increasingly apparent, while the step-up to the premium list and into the FTSE250 on 19 September has widened the potential investor base. The 2017e EV/EBITDA of 10.1x is below the peer group average of 10.6x despite the group's above-average growth potential, scale and diversification.

Travel & leisure

20 September 2016

Price **721.5p**

Market cap **£2,109m**

€1.17/\$1.13/TRY3.89/£

Net debt (€m) at 24 July 2016 154

Shares in issue 292.3m

Free float 94%

Code GVC

Primary exchange LSE (Premium segment)

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 2.7 27.6 82.0

Rel (local) 3.2 13.6 64.7

52-week high/low 726.5p 372.0p

Business description

GVC Holdings is a leading e-gaming operator in both B2C and B2B markets with four main product verticals (Sports, casino, poker, bingo). Just under 70% of revenues come from regulated markets (H116). GVC acquired bwin.party digital entertainment (bwin) on 1 February 2016 for €1.51bn

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Interim results and revisions to full year forecasts

GVC has adopted bwin's label-based approach and thus its Sports labels include both sports and the gaming cross-sell net gaming revenue (NGR). Its Games label includes stand-alone gaming brands such as *Foxy Bingo*, *partycasino* and *partypoker*. B2B services are provided to other well-known gaming operators such as Danske Spil, while non-core includes Intertrader and Kalixa (discussions regarding a disposal of the latter are ongoing).

Exhibit 1: Pro forma* half-yearly normalised results and estimates

€m	H115	2015	H116	H216e	2016e	2017e	2018e
Sports labels	275.4	567.1	312.4	303.6	616.0	641.0	673.0
Games labels	109.0	193.6	102.0	87.5	189.5	191.5	200.0
B2B	7.5	12.8	6.5	7.0	13.5	15.5	20.0
Total core	391.9	773.5	420.9	398.1	819.0	848.0	893.0
Non-core	9.9	36.3	11.1	9.9	21.0	20.0	20.0
Revenue by labels	401.8	809.8	432.0	408.0	840.0	868.0	913.0
VAT	6.6	N/A	9.8	10.2	20.0	22.0	24.0
Net gaming revenue (NGR)	408.4	809.8	441.8	418.2	860.0	890.0	937.0
Variable costs	(196.1)	(384.1)	(203.9)	(208.9)	(412.8)	(431.6)	(459.1)
Contribution	212.3	425.7	228.1	219.1	447.2	458.3	477.9
Contribution margin %	52.0%	52.6%	51.6%	52.4%	52.0%	51.5%	51.0%
Sports labels contribution	149.2	306.3	177.7	171.3	349.0	355.0	367.5
Games labels contribution	54.7	102.6	44.4	41.8	86.2	88.8	92.0
B2B contribution	7.3	3.2	6.4	6.6	13.0	14.5	17.5
Non-core contribution	1.1	13.7	(0.4)	(0.6)	(1.0)	0.0	0.0
Contribution	212.3	425.7	228.1	219.1	447.2	458.3	477.0
Other operating costs	(138.8)	(262.2)	(123.7)	(121.4)	(245.1)	(208.4)	(192.9)
Other op costs ratio	34.0%	32.4%	28.0%	29.0%	28.5%	23.4%	20.6%
Clean EBITDA	73.5	163.5	104.4	97.7	202.1	250.0	285.0
Clean EBITDA margin	18.0%	20.2%	23.6%	23.4%	23.5%	28.1%	30.4%

Source: GVC accounts, Edison Investment Research. Note: *Assumes that bwin.party is consolidated from 1 January.

Sports labels: Strong H116

Proforma revenue increased 13% to €312.4m (19% at constant currency) helped by an improved win margin of 9.1% (H115: 8.1%). Contribution (which is stated after marketing, betting taxes and duties and variable costs such as platform fees and payment processing) increased 19% to €177.7m. Mobile is a key driver of growth, with sports wagers on mobile up 55% and casino & games up 98%. Gaming cross-sell improved and new content deals have been signed. Euro 2016 was a success, generating €162m in wagers across the whole tournament at an impressive win ratio of 18.3%, implying gross win of almost €30m, of which 35% is reported to have fallen in Q316. The first platform migration from Sportingbet to bwin.party was completed in September and the main territories will be migrated between now and Q217 – there is some execution risk but management is extremely experienced and this is a key area for the delivery of the target cost synergies (see our [Update report](#) dated 4 February).

Games labels: New road map now in place

Proforma revenue declined by 6% to €102.0m (-2% at constant currency) and contribution fell by 19% to €44.4m. Much of the revenue decline was due to a competitive bingo market, with rivals marketing aggressively, while contribution was also affected by increased gaming taxes in Austria and Germany. During H116 GVC focused on putting in place a long-term strategic road-map for the business and bringing in some new senior hires and Q316 Games labels revenue to 15 September is reported to be up 6%.

H116 results: Proforma clean EBITDA up 42%

Management provided proforma results (assuming that bwin was consolidated from 1 January) down to the clean EBITDA level: EBITDA of €104.4m showed a 42% increase. On a group reported basis (including bwin from its date of acquisition, 1 February 2016) NGR was €390.6m (H115: €120.9m) and clean EBITDA was €91.2m (H115: €25.5m). Below the EBITDA level the reported results include material exceptional charges of €89.3m (mainly deal related costs) and €65.5m of depreciation and amortisation, of which the bulk (€52.2m) related to amortisation of acquired intangibles. The overall reported loss before tax was €86.1m (H115: PBT 17.1m).

Very positive outlook for H216 and beyond

Management's trading statement is very positive. Q316 has started strongly with NGR for the 11 weeks to 15 September up 12% (15% at constant currency) helped by Euro 2016. We believe that around €30m of synergies will now fall in 2016 (previous estimate €20m) although some of this will be ploughed back into marketing. Thus we increase our 2016 clean EBITDA estimate by €5.6m to €202.1m. This allows for tougher H2 comparatives and some short-term disruption during the sportsbook platform migration process.

Management believes that "the organic growth potential of the group is now greater than originally anticipated". Against this, however, there are continued regulatory and tax headwinds including the extension of the UK point of consumption tax (POCT) to gaming free bets from August 2017, and new taxes in countries that are in the process of regulating (eg Poland, Netherlands, Czech Republic). Moreover, GVC has indicated that it intends to increase investment in the business, especially in marketing (currently low versus peers at c 21% of NGR). Taking all this into account, we have increased NGR slightly (2017e now €890m, previously €878.5m) but left our 2017 and 2018 clean EBITDA estimates unchanged (Exhibit 2). We note that NGR outperformance will partly be applied to staff bonuses as part of the employee incentivisation programme.

Changes to estimates

Exhibit 2 summarises the changes to our forecasts. The interim results provided detail on the acquired assets enabling us to make a better estimation of the ongoing depreciation, amortisation of own work (which we include in our normalised profit calculations) and amortisation of acquired assets (which we exclude). As a result we have materially reduced our estimated depreciation and amortisation charge: we had cautiously allowed for €51.1m in 2016 but we now reduce that to €35.0m. With the reduction also flowing through for 2017/18 it is the main factor behind the increase to our normalised EPS forecasts (up 17% in 2016 and 6% in 2017).

Exhibit 2: Changes to estimates									
	EBITDA* (€m)			PBT* (€m)			EPS* (c)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2016p**	196.5	202.1	+2.8	81.2	102.9	+26.7	26.7	31.3	+17.2
2017e	250.0	250.0	-	177.6	188.4	+6.1	53.0	56.2	+6.0
2018e	285.0	285.0	-	228.0	234.0	+2.6	67.3	69.0	+2.5

Source: Edison Investment Research. Note: *Normalised. ** pro forma includes 12-months of bwin.

Cash flow and net debt: Better than previously forecast

Net debt at 30 June was €165.1m but this is reported to have fallen to €154.3m at 24 July (post Euro 2016) which is only 0.8x annualised clean EBITDA and 11% of group net assets. H216 will bear the brunt of the cash restructuring costs but despite that, we expect a reduction to €145m at end December, which is much better than our previous estimate of €185m. The group's underlying cash conversion is very strong and we continue to expect a material reduction in net debt, to €60m at end 2017 and into a net cash position by end 2018 in the absence of further material acquisitions.

On 2 August GVC announced that its Cerberus loan (which bears interest of 12.5%) is to be refinanced with Nomura with a new €250m facility at an initial rate of only 2%, probably from 1 February 2017. We viewed this as a big vote of confidence in GVC's early progress and discussed it in detail in our Update note dated 4 August. At that stage we reduced our estimated finance charges and we leave them unchanged for now. We include both cash interest and fees in our estimates.

Exhibit 3: Net finance charges

	2016e	2017e	2018e
Interest	46.7	8.8	6.8
Fees	17.5	14.8	3.3
Total finance charges (Exhibit 4)	64.2	23.6	10.0

Source: Edison Investment Research estimates

Exhibit 4: Financial summary

	€m	2014	2015	2016p*	2017e	2018e
Year end 31 December		(IFRS)	(IFRS)	(IFRS)	(IFRS)	(IFRS)
PROFIT & LOSS						
Net gaming revenue		224.8	247.7	860.0	890.0	937.0
Cost of Sales		(101.5)	(112.4)	(412.8)	(431.6)	(459.1)
Gross Profit (contribution)		123.3	135.4	447.2	458.3	477.9
EBITDA		49.2	54.1	202.1	250.0	285.0
Depreciation and amortisation		(5.5)	(1.4)	(35.0)	(38.0)	(41.0)
Operating Profit (norm)		43.7	52.7	167.1	212.0	244.0
Amortisation of acquired intangibles		0.0	0.0	(52.2)	(45.0)	(40.0)
Exceptional/ one-off items		0.0	(24.5)	(145.0)	(5.0)	0.0
Share based payments		(0.7)	(0.4)	(15.0)	0.0	0.0
Operating Profit		42.9	27.7	(45.1)	162.0	204.0
Net finance charges (interest plus fees)		(0.1)	(2.2)	(64.2)	(23.6)	(10.0)
Other financial expense		(1.6)	0.0	0.0	0.0	0.0
Profit Before Tax (norm)		41.3	50.0	102.9	188.4	234.0
Profit Before Tax (FRS 3)		41.3	25.5	(109.3)	138.4	194.0
Tax		(0.7)	(0.8)	4.0	(7.5)	(11.7)
Profit After Tax (norm)		40.6	49.2	106.9	180.9	222.3
Profit After Tax (FRS 3)		40.6	24.7	(105.3)	130.9	182.3
Average Number of Shares Outstanding (m)		61.1	61.3	292.0	292.0	303.0
EPS - normalised fully diluted (c)		61.4	76.4	31.3	56.2	69.0
EPS - (IFRS) (c)		66.4	40.2	(36.1)	44.8	60.2
Dividend per share (c)		55.5	56.0	0.0	25.0	32.5
Gross Margin (%)		54.8	54.6	52.0	51.5	51.0
EBITDA Margin (%)		21.9	21.8	23.5	28.1	30.4
Operating Margin (before GW and except.) (%)		19.4	21.3	19.4	23.8	26.0
BALANCE SHEET						
Fixed Assets		159.2	159.2	1,681.5	1,685.5	1,689.5
Intangible Assets		154.3	155.2	1,660.0	1,660.0	1,660.0
Tangible Assets		1.1	1.4	20.0	24.0	28.0
Deferred tax asset		3.8	2.6	1.5	1.5	1.5
Current Assets		49.5	72.6	535.0	460.0	447.5
Stocks		0.0	3.8	0.0	0.0	0.0
Debtors		31.7	40.6	140.0	150.0	160.0
Cash		4.8	13.4	285.0	190.0	157.5
Customer balances		13.0	14.8	110.0	120.0	130.0
Current Liabilities		(50.4)	(81.0)	(320.0)	(450.0)	(385.0)
Creditors		(46.4)	(77.3)	(290.0)	(300.0)	(310.0)
Short term borrowings		(4.1)	(3.7)	(30.0)	(150.0)	(75.0)
Long Term Liabilities		(8.8)	(22.6)	(480.0)	(180.0)	(130.0)
Long term borrowings		(3.1)	(19.8)	(400.0)	(100.0)	(50.0)
Other long term liabilities		(5.7)	(2.8)	(80.0)	(80.0)	(80.0)
Net Assets		149.5	128.1	1,416.5	1,515.5	1,622.0
CASH FLOW						
Operating Cash Flow		48.5	62.5	26.5	207.5	263.0
Tax		(0.5)	(0.7)	(4.6)	(10.0)	(12.0)
Net Interest		(0.1)	0.0	(46.7)	(23.6)	(10.0)
Capex		(5.3)	(6.2)	(45.0)	(45.0)	(50.0)
Acquisitions/disposals		(8.0)	(2.4)	(1,510.0)	0.0	0.0
Financing		0.9	(24.5)	1,439.7	0.0	0.0
Dividends		(33.6)	(34.3)	0.0	(44.0)	(98.5)
Net Cash Flow		1.9	(5.6)	(140.0)	85.0	92.5
Opening net debt/(cash)		4.3	2.4	10.2	145.0	60.0
HP finance leases initiated		(0.6)	(1.5)	0.0	0.0	0.0
FX/ Other		0.7	(0.7)	5.2	0.0	0.0
Closing net debt/(cash)		2.4	10.2	145.0	60.0	(32.5)

Source: GVC accounts, Edison Investment Research. Note: * 2016p is pro forma, including bwin.party for 12 months (reported will include it from the date of acquisition, 1 February 2016).

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