EDISON

GVC Holdings

A game changer

Outlook for 2017/18

Travel & leisure

GVC's positive momentum a year on from the bwin deal is demonstrated by encouraging KPIs and the early resumption of dividends. Attainment of the target €125m of cost synergies is well on track, assuming successful platform migrations during H117. Strong cash generation underpins a generous dividend policy (50% payout). The 2017e EV/EBITDA of only 8.8x looks very good value for an ambitious group that is capitalising on industry growth and consolidation opportunities.

Year end	Revenue (€m)	EBITDA* (€m)	PBT* (€m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/14	224.8	49.2	41.3	61.4	55.5	11.5	7.9
12/15	247.7	54.1	50.0	76.4	56.0	9.2	7.9
12/16p**	885.0	204.5	105.3	32.1	14.9	22.0	2.1
12/17e	909.0	250.0	188.0	55.4	26.0	12.7	3.7
12/18e	960.0	285.0	234.0	68.2	33.5	10.3	4.8

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

Scale and diversification

GVC's scale and diversification is a key competitive advantage, as is its proprietary platform. We believe it is now the fourth largest online gambling operator, with 55% of revenues coming from regulated markets (c 70% including taxed and soon-to-regulate). It spent much of 2016 integrating bwin (estimated €55m of synergies achieved by year-end) and putting in place the building blocks for future growth: product enhancements and an impressive line-up of new management. We expect the main platform migrations to be completed by the end of Q217 and while there is some execution risk, management has a depth of experience. Better cross-sell is a key opportunity and GVC began to increase marketing spend in H216.

Margin gains and strong cash generation

Our 2016 normalised EBITDA estimate of €204.5m compares with €196.5m at the time of the bwin acquisition in February 2016. Our 2017 and 2018 forecasts allow for rising gaming taxes as markets regulate, but despite this we forecast normalised PBT growth of 79% and 24%, respectively, driven by synergies and falling interest charges. The underlying business is strongly cash generative and we expect net debt of €145m at December 2016 to fall to €80m at end 2017 and the group to be in a net cash position by end 2018. It will pay a special 14.9c (12.5p) dividend in February 2017, ahead of target, and thereafter has a generous 50% payout policy.

Valuation: 2017e EV/EBITDA only 8.8x

GVC has an excellent track record and strong organic growth prospects, which we expected to continue to be augmented by M&A at some stage. Our peer group comparison and DCF suggest a value of at least 700-770p/share, 15-27% above the current price, even allowing for some regulatory risks. Final results in late March and successful platform migrations by end H217 are key catalysts. The prospective 2017 dividend yield of 3.7% is attractive and the group also has a history of special dividend payouts.

18 January 2017

Price	**607.5p**
Market cap	**£1,777m**
	€1.16/$1.23/£
Net debt (€m) at 24 July 2016	154
Shares in issue	292.5m
Free float	94%
Code	GVC
Primary exchange	LSE (Premium segment)
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(6.3)	(17.3)	31.2
Rel (local)	(9.0)	(20.3)	7.3
52-week high/low		769.00p	421.50p

Business description

GVC Holdings is a leading e-gaming operator in both B2C and B2B markets with four main product verticals (sports, casino, poker and bingo). About 55% of revenues come from regulated markets (H116). GVC acquired bwin.party digital entertainment (bwin) on 1 February 2016 for €1.51bn.

Next events

Final results	Late March

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Edison profile page

GVC Holdings is a research client of Edison Investment Research Limited

Investment summary: A game changer

Company description: Top four online gambling operator

GVC is a leading online sports betting and gaming group serving over 25 markets, mainly in Europe and Latin America. Its main brands are *bwin*, *Sportingbet*, *betboo*, *partypoker*, *partycasino*, *Foxy Bingo* and *Casino Club* and it has its own proprietary platforms and content. It holds gambling licences in c 15 countries and is headquartered in the Isle of Man, with offices in the UK, Gibraltar, Europe and worldwide and over 2,500 employees. Management's strategy is to supplement organic growth with M&A, to build scale, diversify geographically and expand its product offering. Acquisitions include Betboo in 2009 (for c €21m), Sportingbet in March 2013 (€84m) and bwin.party digital entertainment in February 2016 (€1.51bn).

Valuation: Earnings and dividend attractions

GVC's share price increased by 38% in 2016 helped by encouraging KPIs, demonstration that the bwin acquisition is paying off, the move to a Premium Listing in August, entry to the FTSE 250 in September and increased analyst coverage. However, it ran into profit taking in Q416 and at 607.5p the 2017e EV/EBITDA of 8.8x is below the sector average. With the rapid momentum the group has established, we consider that it could easily merit a premium rating, with successful completion of the platform migrations by end Q217 an important catalyst. For example, a 2017e EV/EBITDA of 10.0-11.0x would imply a share price of 700-770p and a P/E of 14.5-16.0x. This is supported by our DCF (WACC of 9.5%), which produces a value of 779p. Flexing the WACC and terminal EBITDA margins by c 10% gives a range of 710-848p. GVC has resumed dividends earlier than expected and has a generous 50% payout policy; our 2017e yield is 3.7% rising to 4.8% in 2018e.

Financials: Synergies and falling interest drive PBT growth

2016 KPIs have been encouraging with pro forma group net gaming revenue (NGR) up 8% in H116 and 12% in H216 (to 12 December), although we allow for punter-friendly results at year-end. Our forecasts are unchanged from those published on 19 December and slightly up on those published at the time of the interims in September. Strong forecast growth in profits in 2017 and 2018 is partly the result of better products and cross sell, but particularly due to the bwin synergies flowing through (run-rate of c €75m at end 2016 and the full target €125m by end 2017). Additionally, interest charges are falling rapidly due to strong underlying cash generation and the Cerberus 12.5% debt being replaced with Nomura 2% (initial) debt from February 2017.

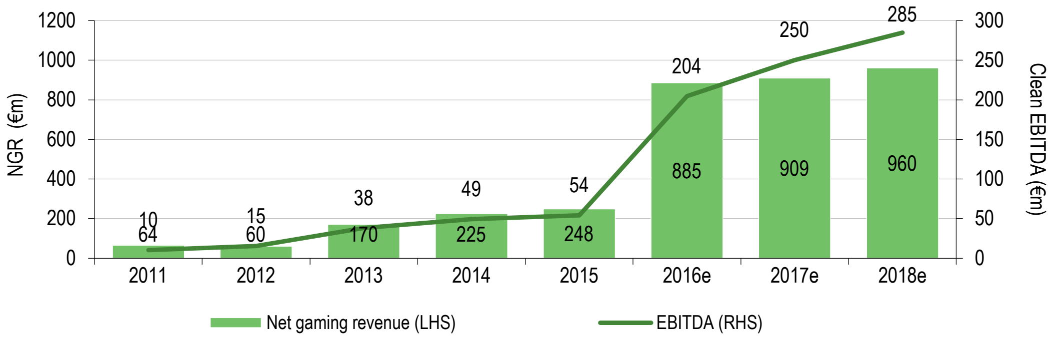
Sensitivities: Regulatory and general business

GVC's main sensitivities are regulatory. Licensed markets can and do change tax and other licence conditions from time to time, eg in the UK (gaming duty will apply to gross rather than net gaming revenues from August 2017) and Greece (rates up from 30% to 35%). Regulating markets will introduce new taxes, but market size is generally boosted, or they may restrict permitted products. There is still no formal licensing regime in GVC's largest market, Germany (although it pays both gaming tax and VAT there). A sports betting regulatory structure is in place and operators provide casino and poker based on the view that the State Treaty is not EU compliant (the länder are pushing for a review of it). The Turks remain enthusiastic gamblers and we do not foresee any change to the status quo there, although some risk cannot be ruled out. Other general business risks include loss of customers over the platform migrations (but management is extremely experienced), general economic risks (although GVC is well diversified and gambling is generally resilient) and competitive markets.

A top four global online gambling operator

GVC's acquisition of bwin.party in February 2016 marked a step change in scale, with margin gains set to come through strongly over the next two years. It follows on from the success of the Sportingbet acquisition in 2013, which was highly accretive, and the CEO has made no secret of his desire to continue to participate in industry consolidation. Online gambling markets are growing on the back of rising internet penetration and smartphone/tablet usage but are also changing as more countries introduce licensing regimes. This presents both opportunities and challenges. Based on the last four years' progress, when the company has moved up from AIM to a Premium Listing and the FTSE 250, a medium-term ambition to make it into the FTSE 100 is not a pipe dream.

Exhibit 1: A step change in scale



Source: GVC accounts, Edison Investment Research forecasts

Business overview

GVC is organised into two main divisions: Sports labels (72% of NGR) and Games labels (24%). Its Sports brands (*bwin*, *Sportingbet*, *betboo*, *Superbahis*) focus their marketing on sports betting and then cross-sell casino and other games such that NGR within the Sports labels is split roughly 50/50 between sports and games. The Games labels are standalone games brands that only cross-sell a small (2%) volume of sports and include *partycasino*, *partypoker*, *Foxy Bingo*, *gioco digitale* and *CasinoClub*. During 2016 GVC put in place a long-term strategic road map for each Games brand, improving the product and user experience, and we believe the benefits are already showing through in areas such as poker. Europe is GVC's biggest market, contributing almost 75% of NGR (Exhibit 9). It is well diversified, with 17 countries contributing 2% or more to NGR and scope to expand in a number of core markets.

Exhibit 2: 2016e revenue* by division

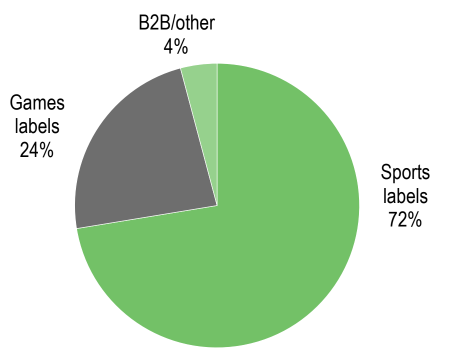
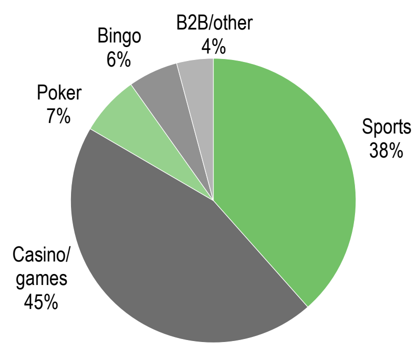


Exhibit 3: 2016e revenue* by product



Source: Edison Investment Research. Note: *2016e pro forma net gaming revenue (NGR) of €885m.

Bwin brought in a small B2B business whose clients include Borgata in the US and Danske Spil in Denmark. In May 2016 it announced a partnership with Betfred but the two parties recently mutually agreed to terminate it, which will allow GVC to focus on its own platform migrations and retain greater M&A flexibility, particularly in the UK. Bwin also brought in some non-core businesses including InterTrade (financial markets trading) and Kalixa (payment processing, sold for €29m in December 2016).

Track record of successful expansion and diversification

GVC Holdings (formerly Gaming VC) was founded and floated in 2004 when its main business was CasinoClub, a successful Germany-facing online casino. It launched a sportsbook in 2007, expanded across Europe, and diversified into Latin America in 2009 via the acquisition of Betboo. In November 2011 GVC entered into a B2B agreement to service EPC (which had acquired Sportingbet's Turkish operations) and in March 2013 GVC acquired Sportingbet (ex its Australian and Spanish businesses) in a consortium bid with William Hill, for €84m (£72m).

Sportingbet brought in a long-established online gambling business with revenues of about €125m (twice the size of GVC, whose 2012 revenues were €60m). It was loss-making but GVC cut €50m from the cost base and returned it to profitability ahead of target, in less than a year. The acquisition also meant that GVC (on behalf of EPC) no longer had to pay Sportingbet's earn-out from the 2011 B2B deal, saving over €110m on our estimates. GVC's normalised EPS jumped from 31.6c in 2012 to 57.2c in 2013 with much of the increase reflecting the accretive nature of the deal.

The bwin.party acquisition on 1 February 2016 (for €1.51bn) was GVC's second transformative acquisition in three years. Again GVC took on a company that was over twice its size (bwin 2015 revenues of €562m versus GVC's at €248m). bwin.party itself was the product of a merger between bwin AG and PartyGaming in 2011 but it seems there was never a good cultural fit between the two and a challenging market backdrop (especially for poker) meant the business declined materially between 2012 and 2014 (see our GVC Update report dated 20 November 2015). By contrast, bwin's CEO Norbert Teufelberger said that "one of the deciding factors in bwin.party's decision to side with GVC [over a rival bid by 888] was the shared DNA of their sports betting operations… GVC formulated a clear vision for growth, which is something we were lacking last year".

bwin materially increased GVC's scale and diversification, both important in changing online gambling markets. It also brought in a well-invested, highly scalable platform and strong brands. Cost synergies of €125m were identified and we expect GVC to have achieved €55m of them by end-2016 (with an exit run-rate of €75m, slightly ahead of the original target). We also believe there will be significant revenue synergies in the form of cross-sell.

Experienced management team, adding new talent

GVC's board and executive team has a considerable depth of experience in online gaming. Kenneth (Kenny) Alexander has been CEO since March 2007 and was previously MD of Sportingbet's European operations. Finance Director Richard Cooper joined in 2008 (from Trident Gaming/Gamebookers) and will be retiring next month to be succeeded by Paul Miles, currently CFO of Wonga plc (biographies on page 16).

Immediately after the bwin acquisition, Kenny began to restructure the management team to take the best talent from both bwin and GVC, with a management structure that emphasises clear reporting lines and management accountability. Shay Segev was brought in as group COO, having previously been COO of leading gaming software provider Playtech and Nick Batram joined from Peel Hunt as head of investor relations and corporate strategy. A number of new management positions have also been created, including chief product officer and VP business operations, as Kenny has put in place an organisation that can handle material group expansion. Exhibit 4 illustrates the calibre of new management who have joined GVC over the past year; many others have also joined from leading operators in key markets.

Exhibit 4: Recent new executive management hires

	Position	Joined	Former roles	Responsibility
Paul Miles	CFO	Feb-17	Wonga CFO; Capquest CFO, RSA financial controller	Finance and strategy
Shay Segev	COO	Mar-16	Gala Coral chief strategy officer, Playtech COO	Chief operating officer
Nick Batram	IR/corporate strategy	Apr-16	Peel Hunt head of leisure and gaming	IR and corporate strategy
Liron Snir	Chief Product Officer	Mar-16	Playtech, VP of product and strategy	Product management
Roni Maman	VP Business Ops	Mar-17	888 Holdings, Senior VP of Operations	Customer service
Adele Lawton	Head of Bingo	Aug-16	Betable Ops director Europe, Bet365, Gala, Skybet.	Cashcade bingo brands

Source: GVC, Edison Investment Research

GVC has always believed in management and employee incentivisation. Post the bwin acquisition a new option plan (LTIP) was put in place, with options over 18.7m shares held at 30 June 2016. Employee bonuses are linked to revenue outperformance. In December 2016 GVC announced that directors (who do not receive bonuses) would receive cash payouts totalling €10.7m as an alternative to selling c 80% of 3.7m options that had vested to cover the option cost and pay tax (Edison Update, 19 December 2016). The directors' shareholdings were unchanged and continue to represent a sizeable part of their total wealth (1.9m shares or £12m in the case of CEO Kenny Alexander).

Strategic vision for growth

The interim results presentation (September 2016) set out management's strategic vision. While the organic opportunity is greater than management originally anticipated, we also expect it to look at M&A opportunities as they arise. We consider that any large deal would be more likely to be sport-led, but that there may also be gaming bolt-on opportunities. The strategic vision is:

- To build further scale and international diversification:
  - GVC's largest market (Germany) is just 25% of NGR and 17 countries contribute over 2% to NGR. Grow in markets that are regulated or moving to regulate.
- To be a top three player in core markets:
  - Top three in five to six markets, under 10% share in 14 markets.
- To be best in class in core verticals:
  - Sports: good but not yet best; gaming: improving but much still to be done.
- To capitalise on a greater than expected organic opportunity:
  - Increase investment from 2017.

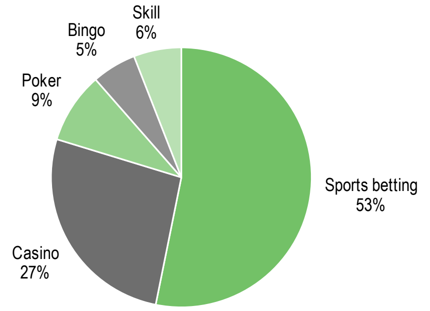
Market overview

GVC operates in growing markets, with positive structural drivers. Online gambling's share of the total gambling market is growing steadily but is still only 13%, up from 10% in 2010. Growth is driven by rising broadband penetration, product innovation and greater trust. Gambling on mobile devices is growing very rapidly and is expected to account for 40% of the online market by 2018. It is proving to be incremental rather than cannibalistic because it allows for play anytime, anywhere. Overall the global online gambling market is estimated to have been worth $32.3bn in 2015 (source: H2 Gambling Capital) and is forecast to grow at a CAGR of 10.5% to 2018.

By geography, the UK is the largest licensed market at €4.6bn in 2015, or 14% of the total (Gambling Commission). H2 Gambling Capital estimates that the rest of Europe accounts for about 32%, Asia and the Middle East 33% and the rest of the world 21%. There are material differences in the business model in different geographies depending on the local regulatory environment.

Exhibit 5: Online gambling market* growth

Exhibit 6: Online market product split



Source: Industry sources, H2Gambling Capital, Edison Investment Research. Note: Excludes online state lotteries.

Land-based gambling is tightly regulated in most countries (on both fiscal and moral grounds) but relatively few countries have specific online gambling regulation and the political and legal process for its introduction tends to be very slow. Fully regulated European countries include the UK, Italy, France, Spain, Denmark and Romania, while others are in different stages of introducing regulation (eg Czech Republic, the Netherlands). Tax structures, product and licence requirements vary considerably by market, eg whether all products are allowed and whether taxes are on revenue or profit. GVC applies for licences as they become available, assuming they are economically attractive (eg it was granted a new 10-year permanent licence in Romania in September 2016, having previously operated on an interim licence).

Industry consolidation and M&A

Scale is becoming increasingly important. There are significant economies of scale in the business model (eg adding new customer lists does not require major step-ups in capex) while regulatory and product development costs have risen significantly in recent years. As a result, there is a considerable amount of M&A activity and we expect this to continue. Exhibit 7 shows some of the larger deals of 2016, but there were also many smaller transactions.

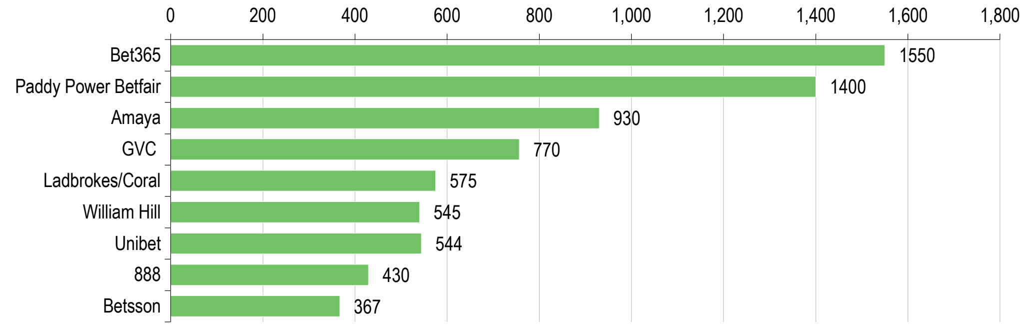
Exhibit 7: Online gambling sector M&A, 2016

Deal	Value (£m)	Announced/ completed	Business
GVC acquires bwin.party	€1.51m (£1.14bn)	Jul 15/Feb 16	B2C sports and gaming
Paddy Power merger with Betfair	£4.3bn	Aug 15/Feb 16	B2C sports and gaming
CVC acquires majority stake in Tipico	Est £1.1-1.2bn	Apr 16	German sports betting
NYX acquires OpenBet	£270m	Apr 16	B2B betting and gaming platform
CVC acquires Sisal Group	€1.0bn (£860m)	Apr/May 16	Italian gaming and payments
Stride acquires Tarco/8Ball	£30m (plus up to £40m earn-outs)	Aug 16	Online bingo
Ladbrokes merger with Gala Coral	£2.4bn	Jul 15/Nov 16	B2C sports and gaming

Source: Company announcements, press reports, announcements, Edison Investment Research

Post GVC's acquisition of bwin, we believe that GVC is the fourth largest online operator:

Exhibit 8: Leading gambling operators' 2016e online revenue (£m)

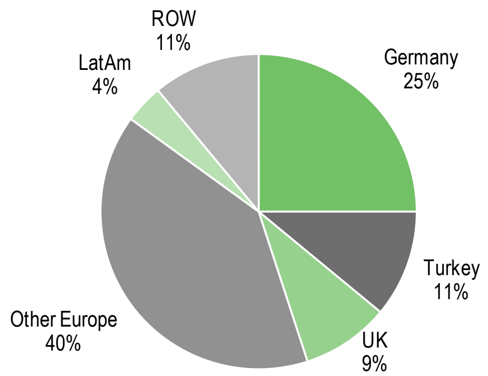


Source: Edison Investment Research, Bloomberg consensus estimates, GVC presentations

GVC is well diversified geographically

The bwin acquisition significantly improved GVC's geographic diversification. Before the deal, about 75% of GVC's revenues came from its top four markets (30% from Turkey, then Germany, Greece and Brazil) and a relatively small proportion from licensed markets. By contrast the enlarged group generates c 55% of its revenues from licensed markets (c 70% including markets that are in the process of regulating and/or are taxed). About 17 countries contribute 2% or more to NGR, with the largest single market being Germany (25%). In total, Europe (including the UK) is almost 75%. Latin America is mainly Brazil, while the rest of the world (ROW) includes bwin's nascent US operations (c 1%), Canada and elsewhere.

Exhibit 9: Estimated geographic split of 2016e revenues*



Source: GVC, Edison Investment Research. Note: *2016e pro forma net gaming revenue (NGR) of €885m.

Germany: bwin is a long established and leading sports-led brand in Germany while CasinoClub is a standalone online casino originally launched in 2001. German law relating to online gambling is in a state of flux with an Interstate Treaty of 2012 subject to legal challenge in both German and European courts. Twenty federal sports licences were provisionally awarded in 2014 (bwin was one of the approved operators) but they were not formalised due to challenges from unsuccessful applicants. The small länder of Schleswig-Holstein offered five-year licences in 2012 under a law that it then revoked, but these were only valid in-state and expire in 2017. Recent events have been much more positive: in April 2016 a German court ruled against the 20 sports-licence cap and in October the prime ministers of the 16 German länder agreed to remove it. They also agreed to consider regulating online casino and poker. A formal licensing regime is still some way off, but in the meantime GVC pays both sports betting taxes (5% of turnover) and VAT on casino revenue.

Turkey: We believe that GVC (via a B2B with EPC) and Sweden-listed Betsson (via a B2B with Realm Entertainment) are the leaders in the Turkish online gaming market. The Turkish government passed strict anti-gambling legislation in 2007 and reinforced it with an additional law in August 2013 (in part to protect the national lottery, which was privatised in 2015). However, the Turks are enthusiastic online gamblers and in practice the business has continued to grow steadily (GVC appears to have performed rather better than Betsson in 2016).

The UK: The UK is a fully regulated market but GVC has a fairly small market share (c 5%). As well as sports betting and casino it is one of the larger online bingo operators (*Foxy*, *Cheeky Bingo* brands) with a c 5% share. UK remote gaming duty (RGD, also known as POCT) is levied at 15% of revenue but from August 2017 it will be extended to include gaming 'free play' (bonuses), which will have an impact on the bingo brands in particular (see Financials).

Europe: We believe the larger territories include Italy (*gioco digitale*), Spain, France, Greece, the Netherlands, Denmark, Switzerland, Austria and a range of East European countries such as Bulgaria, Romania, the Czech Republic and Poland. Many of these are fully licensed (Italy, Spain, France) or in the process of licensing (Czech Republic, although the 1 January start date has been delayed; Netherlands). Greece is another market where there has been some flux; a tender process for new licences began in October 2016 (GVC/Sportingbet previously operated under interim licences and bwin re-entered the market in 2016). The rate of gaming tax increased from 30% to 35% in May 2016, backdated to January 2016. Poland's draft gambling act proposes an online casino monopoly and 12% turnover tax on sports; most of the turnover tax could probably be passed onto customers but a ban on casino products would be very unhelpful. However, allowing a monopoly is against EU laws and the industry is expected to file a complaint with the European Court (ECJ).

US: The US is potentially an enormous market for online gambling operators, but licensing progress has been painfully slow due to vested interests and a powerful Christian right lobby. Market size in those states that have regulated (eg New Jersey) has been disappointing, perhaps in part because of the continued existence of a substantial offshore industry (Online Casino City lists 755 gambling sites that accept US players, out of a total of c 3,500). However, GVC's successful award of a New Jersey licence in Q216 was an important vindication of the group's integrity and the US can only represent upside for the group. *Gaming Intelligence* recently reported that GVC's US B2B customer Borgata retained its market lead in New Jersey in 2016, in a market that grew by 32% to $197m.

Sensitivities

Legislative and regulatory

GVC's main sensitivities are regulatory. Licensed markets can and do change tax and other licence conditions from time to time, eg in the UK, HMRC is extending RGD to 'free play' from August 2017 (ie the 15% tax will be applied to gross rather than net real money gaming revenue, as is already the case for sports). The UK government is reviewing gaming machines and social responsibility; much of this is focused on terminals in betting shops but there is a possibility that bingo TV advertising before the 9pm watershed could be curtailed or banned, which would be unhelpful for *Foxy* (but also for its competitors). Overseas, the Greek government increased gaming taxes from 30% to 35% in 2016 while various countries (eg Germany) decreed that VAT was applicable to gaming from 2015. However, there have also been some positives. Spain legalised online slots in mid-2015 and Q116 industry revenues grew 32% (source: the regulator, DGJO). EU gaming regulators have recently been considering whether to let France, Spain and Italy pool poker liquidity, which would be helpful for GVC/partypoker.

GVC also operates in unregulated markets, where there is no formal licensing requirement yet in place (in common with most other online gambling operators). They are supplied on a 'dotcom' or 'point of supply' basis from its licensed operations in, for example, Malta. Numerous countries are discussing or in the process of introducing regulation but the process is often very slow, in part because of local vested interests including state lotteries. Typically there is a 'J-curve' in profits when new markets regulate, with an initial dip due to the introduction of new taxes and licensing costs but with the market subsequently growing more rapidly due to new advertising opportunities and greater consumer trust. GVC has indicated that it expects its gaming tax bill to be €50m higher in 2018 than in 2014 (pro forma for the enlarged group) and we estimate that implies a gaming tax bill of c €130m, which is in our forecasts.

There is still no formal licensing regime in GVC's largest market, Germany (although it pays both gaming tax and VAT there). A sports betting regulatory structure is in place and operators provide casino and poker based on the view that the State Treaty is not EU compliant (the länder are pushing for a review of it). We believe that Germany will eventually move towards a full licensing regime and there have been some recent encouraging moves, but the process is likely to be very slow and the current state of flux has persisted for five years now. Turkey is slightly different from most of GVC's other markets in that its anti-gambling laws also apply to the player. Tough new laws were passed in 2007 and 2013 but this was partly to protect the national lottery, which was privatised in 2015. In September 2016 the Cyprus news agency Havadis reported that 39 individuals related to an illegal online betting ring (with revenue of $100m a month) had been arrested. Most players are recreational but it is possible that Turkey's current regime is taking a tougher line than in the past. However the Turks are enthusiastic gamblers and we do not foresee any change to the status quo; the industry there has continued to grow steadily.

General business risks

GVC is also exposed to a variety of general business risks, including:

- Economic risks, including the strength of consumer spending in different markets. Online gambling is generally resilient in downturns but not immune.
- Platform migration execution risks: GVC will need to ensure smooth migrations from Sportingbet to the bwin platform to avoid losing customers in the process, but the COO in particular has considerable experience of this (ex Playtech).
- Dependence on key executives (but GVC now has a much broader management team).
- Fluctuating sports margins and casino margins.
- Competition: the group's markets are highly competitive and rapidly evolving and consolidating. Major competitors include Bet365, William Hill, Ladbrokes Coral, Betsson and Unibet, but there are also numerous smaller competitors in individual markets and products.
- Currency: GVC operates in international markets. Some 40-50% of earnings arise in euros (the reporting currency) while other relevant currencies are sterling, the Turkish lira and the Israeli shekel. Our forecasts allow for ongoing devaluation in the Turkish lira. Sterling devaluation since mid 2016 is a small positive as the group has cost centres in London and Gibraltar.
- Brexit: with local gambling licences and a network of offices worldwide we do not expect Brexit to have a material impact on the group.

Valuation

The most straightforward way to value GVC is via a peer group comparison. Exhibit 10 compares it to the leading UK online gambling operators, together with Sweden-listed Betsson and Kindred as they are both pure online sports-led operators. William Hill and Ladbrokes both have large low-growth land-based operations; analysts generally apply a much higher rating to online businesses.

Exhibit 10: Peer group comparison

	Price	Mkt Cap	EV/EBITDA (x)			P/E (x)		
	(p)	(£m)	2016e	2017e	2018e	2016e	2017e	2018e
GVC Holdings	**607.5**	**1,777**	**10.7**	**8.8**	**7.7**	**21.8**	**12.6**	**10.2**
888 Holdings	226	811	10.6	9.6	8.6	18.1	16.2	14.1
Betsson (BETS)	SEK 83.8	948	10.0	9.4	9.7	13.4	12.6	13.3
Kindred (Unibet) (KND)	SEK 79.2	1,687	14.9	12.3	12.8	19.8	16.0	16.8
Ladbrokes Coral (LCL)	125	2,383	13.4	8.9	8.0	17.3	12.3	9.8
Paddy Power Betfair (PPB)	8510	7,148	17.8	15.1	13.5	25.2	21.4	18.7
Playtech (PTEC)	824	2,638	9.2	7.7	6.9	14.1	11.5	10.2
William Hill (WMH)	284	2,443	8.7	8.4	8.0	13.0	11.6	10.6
Average			**12.1**	**10.2**	**9.6**	**17.3**	**14.5**	**13.4**
Average ex PPB			**11.2**	**9.4**	**9.0**	**15.9**	**13.4**	**12.5**

Source: Bloomberg, Edison Investment Research. Note: Share prices at 17 January.

GVC's share price increased by 38% in 2016 (ending at 641p) helped by encouraging KPIs, demonstration that the bwin acquisition is paying off, the move to a Premium Listing in August, entry to the FTSE 250 in September and increased analyst coverage. However, it ran into profit taking in Q416 and at 607.5p the 2017e EV/EBITDA of 8.8x is well below the sector average even if highly rated Paddy Power Betfair is excluded. The sector average itself has reduced over the last three months due to worries about the outcome of the government's triennial review, but the main adverse impact is expected to fall on betting shops (*Foxy* would be affected by any restrictions on daytime TV advertising but it is less than 5% of group revenue). With the rapid momentum the group has established, we consider that it could easily merit a premium rating, with Paddy Power Betfair's 2017e EV/EBITDA of 15.1x a target (albeit that PPB is 95% regulated). For example, a 2017e EV/EBITDA of 10.0-11.0x would imply a share price of 700-770p and a P/E of 14.5-16.0x.

We have also performed a DCF, running forecasts out to 2023, fading revenue growth from c 5% to 2.5% (terminal 2.0%) and EBITDA margins from 30% to 26% (terminal 25%). Using a WACC of 9.5% produces a value per diluted share of 779p; flexing the WACC between 9.0% and 10.0% gives a range of 735-827p. The model is also sensitive to forecast EBITDA margins; we have allowed for a reduction as more countries regulate and impose taxes but flexing the terminal margin by three points either way (22-28%) gives a value range of 710-848p (using the WACC of 9.5%). Overall we consider that our DCF comfortably supports the peer group derived 700-770p share price range.

Divisional performance and financials

GVC's 2016 reported results will include bwin from 1 February 2016, ie 11 months. To improve understanding of underlying trends management reports pro forma figure as if it had been owned for the full year, together with pro forma comparatives for 2015.Our estimates are prepared on this basis. Our forecasts (Exhibits 11 and 12) are unchanged from those published in our Update report dated 15 December 2016, when GVC announced an increased special dividend for 2016.

Sports labels – strong growth from cross-sell

GVC typically achieves just over 9% gross margin on sports wagers, although this varies by product and geography. It then cross-sells gaming products (casino, poker, etc). In H116 this cross-sell revenue was almost as much as that derived from sports: €157m versus €163m, a 96% ratio, up from 88% in H115. For modelling we assume around a 90% cross-sell ratio. Bwin has an industry-leading sports platform and GVC/Sportingbet excellent trading talent; combining the two, together with product improvements and mobile growth (mobile wagers up 55% in H116) has produced strong results. H116 pro forma net gaming revenue (NGR) rose 14% to €320.6m, with contribution up 19% to €177.7m. Q316 and Q416 (to 12 December) NGR grew by 12% and 19%, respectively. We allow for a weak end to the year due to punter-friendly results and forecast 11% NGR growth for 2016 followed by 3% in 2017 (no major football championship) and 5% in 2018. We believe that management would hope to do better than this.

Games labels – a new strategic roadmap for each business

Prior to acquisition, bwin's Games labels lacked focus, not helped by structural decline in the poker market and a competitive UK online bingo market (eg H115 NGR fell 14%). During 2016 GVC put in place a long-term strategic road map for each business, brought in new senior hires and worked on the product and user experience. Casino content has been much improved with deals with major providers such as Scientific Games, Microgaming, Blueprint (Gauselmann), Realistic Games and iSoftbet. Partypoker has partnered with the Dusk Till Dawn live poker venue in Nottingham and we believe this has helped turn around the poker business, with global live tournaments still a big opportunity for partypoker. CasinoClub has acquired its own platform (from BossMedia) and introduced live casino. Management hires during H216 include Adele Lawton as head of bingo (with 20 years' marketing experience, mainly in bingo, with brands including Gala, Skybet and Gamesys); Rob Fell (ex Lottoland) as head of casino product; Andrew Whitworth (ex Talarius/Tatts) as head of content and Oliver Bartlett (ex bgo.com and Grosvenor) as head of live casino.

H116 Games labels' NGR fell by 6% to €103.7m and contribution by 19% (partly due to the full impact of German and Austrian VAT). Our 2016e NGR forecasts implies flat revenues in H2 (which would be a very good performance) and we expect c 6% NGR growth in 2017 and 5% in 2018.

B2B/ Non-core

We expect B2B revenues and profits to grow steadily, particularly in the USA, although the segment remains small in a group context. Our forecast reduction in revenue from non-core operations in 2017 reflects the sale of the Kalixa payments business in December 2016 (it will continue to service GVC under an existing contract).

Exhibit 11: Pro forma* half-yearly results and estimates

€m	H115	2015	H116	H216e	2016e	2017e	2018e
Sports wagers (sports labels only)	2197.2	4312.6	2298.6	2136.4	4435.0	4656.7	4936.1
Sports margin	8.1%	9.1%	9.1%	9.6%	9.4%	9.1%	9.1%
Sports GGR	178.0	391.2	209.2	206.1	415.3	423.8	449.2
Sports bonuses	(29.1)	(86.6)	(45.8)	(34.0)	(79.7)	(75.0)	(80.0)
Sports NGR	148.9	304.5	163.4	172.1	335.5	348.8	369.2
Sports games cross-sell	131.5	271.1	157.2	148.1	305.3	317.4	332.3
Cross-sell % sports NGR	88%	89%	96%	86%	91%	91%	90%
Sports labels	**280.4**	**575.7**	**320.6**	**320.2**	**640.8**	**666.1**	**701.5**
Games labels	**110.7**	**211.7**	**103.7**	**103.8**	**207.5**	**220.0**	**230.8**
B2B	7.5	14.2	6.5	7.5	14.0	15.5	20.0
Total core	398.6	801.6	430.8	431.5	862.3	901.6	952.3
Non-core	9.9	20.5	11.1	11.6	22.7	7.4	7.7
Net gaming revenue (NGR)	**408.5**	**822.1**	**441.9**	**443.1**	**885.0**	**909.0**	**960.0**
VAT	(6.7)	(14.2)	(9.9)	(11.0)	(20.9)	(23.0)	(24.8)
Revenue	**401.8**	**807.9**	**432.0**	**432.1**	**864.1**	**886.0**	**935.2**
Contribution	**212.3**	**425.7**	**228.1**	**220.0**	**448.1**	**450.0**	**472.4**
Contribution margin % NGR	52.0%	51.8%	51.6%	49.6%	50.6%	49.5%	49.2%
Other operating costs	(138.8)	(262.2)	(123.7)	(119.9)	(243.6)	(200.0)	(187.4)
Other op costs ratio	34.5%	32.5%	28.6%	27.7%	28.2%	22.6%	20.0%
Normalised EBITDA	**73.5**	**163.5**	**104.4**	**100.1**	**204.5**	**250.0**	**285.0**
Clean EBITDA margin	18.3%	20.2%	24.2%	23.2%	23.7%	28.2%	30.5%
Depreciation	(0.4)	(31.9)	(10.4)	(14.6)	(25.0)	(25.0)	(25.0)
Amortisation of own work	(0.5)	(18.1)	(2.9)	(9.1)	(12.0)	(15.0)	(15.0)
Normalised EBIT	**72.6**	**113.5**	**91.1**	**76.4**	**167.5**	**210.0**	**245.0**
Share based payments	(0.2)	(33.4)	(6.5)	(8.5)	(15.0)	0.0	0.0
Net finance charges	(1.3)	(3.9)	(28.5)	(33.8)	(62.3)	(22.3)	(11.4)
Share of profit of associate	0.0	0.0	0.1	0.1	0.2	0.3	0.4
Normalised PBT	**71.1**	**76.2**	**62.7**	**42.6**	**105.3**	**188.0**	**234.0**
Restructuring charges	0.0	0.0	(5.1)	(19.9)	(25.0)	(5.0)	0.0
Other exceptional costs	(4.7)	(70.0)	(84.2)	(0.8)	(85.0)	(4.0)	0.0
Amortisation of acquired intangibles	(1.3)	(23.0)	(52.2)	(67.8)	(120.0)	(120.0)	(120.0)
Exceptional finance expenses	0.0	0.0	14.1	(14.1)	0.0	0.0	0.0
Reported PBT	**65.1**	**(16.8)**	**(64.7)**	**(60.0)**	**(124.7)**	**59.0**	**114.0**

Source: GVC accounts, Edison Investment Research. Note: *Assumes that bwin.party is owned throughout.

Our forecasts allow for rising gaming taxes

About 55% of GVC's revenues arise in regulated markets and a further 15-16% in markets that are yet to regulate but where it pays gaming tax and/or VAT (eg German casino, Czech Republic). It faces new gaming taxes when markets regulate (eg Romania and Bulgaria in 2016) and some tax increases in 2017 (UK 15% RGD applied to gross rather than net gaming revenue from August, Greek tax up from 30% to 35%). GVC expects 2018 taxes to be €50m higher than in 2014 (pro forma for the enlarged group) with around a €23m impact having arisen in 2015 (including VAT applied to gaming revenues in certain EU countries such as Germany and Poland) and about €10m in 2016. We have prudently allowed for over €30m of extra taxes in 2017 and 2018; our forecasts include gaming tax plus VAT of €127m in 2016 and €154m in 2018.

Contribution – higher taxes and marketing

GVC's 'contribution' is stated after betting taxes and duties, marketing and variable costs such as platform fees and payment processing. In 2015 and H116 the margin was fairly stable at 51.6-52.0% of NGR despite the increase in gaming taxes. Some of the bwin synergies come through in contribution but we assume most flow through the 'other operating costs' line. GVC's marketing spend was relatively low in H116 at c 21% of NGR (c €93m), with an 18% ratio in Sports and 33% in Games. During the half GVC exited low ROI (return on investment) marketing, eg bwin sponsorships, and worked to improve the CRM and business intelligence. Management guided to a

23-24% marketing ratio for H216 and we expect spend to run at a similar rate in 2017 and 2018. Hence we allow for a slight reduction in contribution margins over the forecast period.

bwin cost savings and synergies well on target

GVC identified €125m of cost synergies (off the 2014 cost base) before it acquired bwin. About €25m were secured in 2015 (before the deal completed, by a re-energised bwin management) and we expect c €30m in 2016, with a year-end exit run rate of €72.5m (58% of the €125m, as originally forecast). Most of the staff synergies have been secured and IT synergies are starting to come through. The first platform migration from Sportingbet to bwin was completed in September 2016 and we believe the main territories will be migrated by the end of Q217, probably towards or after the main football season. There is some execution risk but management is extremely experienced and we expect much of the 2017 target €55m of synergies to come from IT, with the run-rate reaching the full €125m pa by the end of 2017.

Exhibit 12: Synergy profile

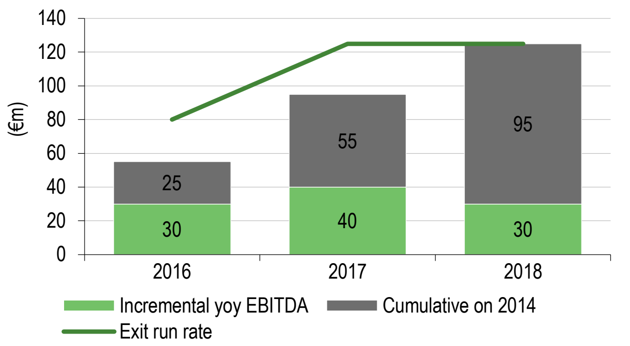
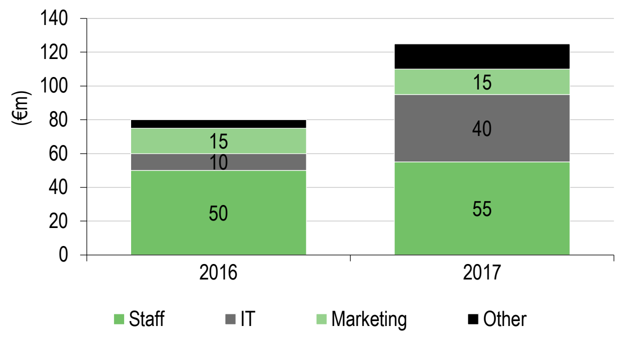


Exhibit 13: Exit run-rate



Source: GVC interims, Investor Presentation November 2016, Edison Investment Research

Normalised EBITDA and PBT growing strongly

The 'other operating costs' ratio is falling sharply as the synergies come through, from 34.5% in H215 to 28.6% in H216. We forecast a fall to 20% by 2018 and would then expect it to hold broadly steady at that level. Thus normalised EBITDA is growing much more rapidly than contribution, up 42% to €104.4m in H116 versus a 7% increase in contribution (to €228.1m). We forecast €204.5m of pro forma normalised EBITDA for 2016, which implies a slight reduction in H216 over H116 due to the increase in marketing and staff bonuses as expected results exceed original targets (eg in February 2016 our 2016 EBITDA forecast was €196.5m). For 2017 and 2018 we forecast 22% and 14% growth in EBITDA, to €250.0m and €285.0m, respectively.

Our 2016 normalised PBT estimate of €105.3m (up 38% on 2015) is after relatively high net finance charges of €62.3m on the Cerberus debt (€46.7m of interest at 12.5% and €15.6m of fees, although some analysts exclude the latter from their normalised PBT calculations). With the Cerberus debt being replaced by a Nomura loan before 2 February 2017 (initial interest rate only 2%), we expect financing charges to drop to €22.3m in 2017 and €11.4m in 2018. Hence we forecast 79% growth in normalised PBT in 2017 and 24% growth in 2018, which flows through to normalised EPS growth of 69% in 2017 and 23% in 2018, allowing for a slight rise in the tax rate from the expected 2016 level of 5%.

One-off costs to achieve the synergies

GVC expected to spend some €60m on one-off restructuring costs (excluding deal costs) to achieve the (recurring) €125m pa of synergies. P&L exceptional costs were €89m in H116 including deal costs and acquisition related expenditure of €55m, acceleration of amortisation on an onerous

IT contract of €12.5m and restructuring costs of €5m. We expect another €20m to be charged in H216, mainly restructuring costs. These charges, together with c €120m of amortisation of acquired intangibles, mean that we forecast a reported pre forma PBT loss of €124.7m. However, we expect exceptional items to fall to under €10m in 2017 and zero in 2018 paving the way for a strong uplift in reported profits to €114.0m in 2018.

Successful debt refinancing in August 2016...

GVC's €400m Cerberus loan was put in place at relatively short notice to part-fund the €1.51bn acquisition of bwin in February 2016 and, as such, it bears a 12.5% interest rate plus material fees. Our original forecast for the enlarged group assumed that it would be replaced by a new facility at c 7.5% from end Q117. In August 2016, however, GVC announced that it had successfully refinanced the Cerberus debt with a new €250m facility from Nomura with an initial interest rate of only 2% above Euribor and an extension period six or 12 months after the initial maturity date of September 2017. This will be drawn down shortly before 2 February 2017 (thus avoiding Cerberus anniversary fees). In our Update note of 4 August 2016 we viewed the announcement as "a big vote of confidence in GVC's early progress integrating its transformational bwin acquisition".

... paved the way for an early resumption in dividends

Aside from being high-cost, the Cerberus facility required GVC to take a dividend payment holiday in 2016. Its replacement with the Nomura facility has allowed it resume dividends earlier than planned. On 3 November GVC announced that it would pay a special dividend of 10c/share in respect of 2016 and on 15 December it announced that it would increase the planned pay-out by 49% to 14.9c per share (fixed at 12.5p/share) payable on 14 February 2017 (ie after the outstanding Cerberus loan has been repaid in full).

GVC has historically been a generous dividend payer. Its dividend policy for the enlarged group is to distribute 50% of annualised free cash flow from 2017 (absent of any significant investments and assuming appropriate capital ratios are maintained) and we believe management might choose to exceed this ratio. It has indicated that payments will be biannual with an approximate interim/final split of 40:60. GVC has also said that it will consider returning any future excess cash to shareholders in the form of special dividends and/or share buybacks, but in practice we expect that it is more likely to make at least one more sizeable accretive acquisition.

Strong positive cash flows and debt reduction

GVC's underlying business is highly cash generative with free cash flow typically exceeding 90% of normalised EBITDA.

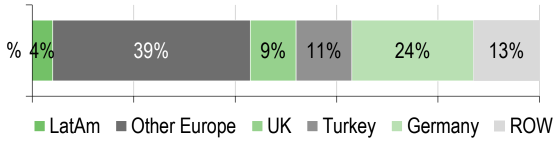
In 2016 the business bore most of the cash costs of the bwin deal and restructuring: we expect c €43m of cash restructuring costs, €104m of other exceptional cash costs and over €30m of working capital such that our €204.5m of 2016 normalised EBITDA (€190m including bwin for the actual 11 months) converts into €29m of operating cash flow. GVC reported net debt of €154m as at 24 July 2016 and we expect the December 2016 figure to be slightly below that at €145m despite many of the bwin-related costs having fallen in H216.

GVC has guided that 2017 will bear a further €25-30m of cash restructuring costs and that capex will run at c €40m pa. We expect the sale of the non-core Kalixa payments business to raise a net €15m (Edison Update note dated 19 December) and even allowing for €77m of dividend costs (14.9c special plus 10.4c interim) we expect 2017 year-end net debt to have fallen to €80m. By the end of 2018 we expect the group to be in a net cash position in the absence of further material acquisitions.

Exhibit 14: Financial summary

€m	2014	2015	2016p*	2017e	2018e
Year end 31 December	(IFRS)	(IFRS)	(IFRS)	(IFRS)	(IFRS)
PROFIT & LOSS					
Revenue	224.8	247.7	885.0	909.0	960.0
Cost of Sales	(101.5)	(112.4)	(436.9)	(459.0)	(487.6)
Gross Profit (contribution)	123.3	135.4	448.1	450.0	472.4
EBITDA	49.2	54.1	204.5	250.0	285.0
Depreciation and amortisation	(5.5)	(1.4)	(37.0)	(40.0)	(40.0)
Operating Profit (norm)	43.7	52.7	167.5	210.0	245.0
Amortisation of acquired intangibles	0.0	0.0	(120.0)	(120.0)	(120.0)
Exceptional/ one-off items	0.0	(24.5)	(115.0)	(9.0)	0.0
Share based payments	(0.7)	(0.4)	(15.0)	0.0	0.0
Operating Profit	42.9	27.7	(82.5)	81.0	125.0
Net finance charges (interest plus fees)	(0.1)	(2.2)	(62.3)	(22.3)	(11.4)
Other financial expense/ associates	(1.6)	0.0	0.2	0.3	0.4
Profit Before Tax (norm)	41.3	50.0	105.3	188.0	234.0
Profit Before Tax (FRS 3)	41.3	25.5	(144.7)	59.0	114.0
Tax	(0.7)	(0.8)	4.0	(15.0)	(21.1)
Profit After Tax (norm)	40.6	49.2	100.1	172.9	213.0
Profit After Tax (FRS 3)	40.6	24.7	(140.7)	43.9	93.0
Average Number of Shares Outstanding (m)	61.1	61.3	292.0	292.5	303.0
EPS – normalised fully diluted (c)	61.4	76.4	32.1	55.4	68.2
EPS – (IFRS) (c)	66.4	40.2	(48.2)	15.0	30.7
Dividend per share declared (c)	55.5	56.0	14.9	26.0	33.5
Dividend per share paid (c)	55.0	56.0	0.0	25.3	25.3
Gross (Contribution) Margin (%)	54.8	54.6	50.6	49.5	49.2
EBITDA Margin (%)	21.9	21.8	23.1	27.5	29.7
Operating Margin (before GW and except.) (%)	19.4	21.3	18.9	23.1	25.5
BALANCE SHEET					
Fixed Assets	159.2	159.2	1,686.5	1,572.5	1,477.5
Intangible Assets	154.3	155.2	1,660.0	1,541.0	1,441.0
Tangible Assets	1.1	1.4	25.0	30.0	35.0
Deferred tax asset	3.8	2.6	1.5	1.5	1.5
Current Assets	49.5	72.6	535.0	430.0	431.0
Stocks	0.0	3.8	0.0	0.0	0.0
Debtors	31.7	40.6	140.0	140.0	160.0
Cash	4.8	13.4	285.0	170.0	141.0
Customer balances	13.0	14.8	110.0	120.0	130.0
Current Liabilities	(50.4)	(81.0)	(320.0)	(440.0)	(385.0)
Creditors	(46.4)	(77.3)	(290.0)	(290.0)	(310.0)
Short term borrowings	(4.1)	(3.7)	(30.0)	(150.0)	(75.0)
Long Term Liabilities	(8.8)	(22.6)	(470.0)	(170.0)	(120.0)
Long term borrowings	(3.1)	(19.8)	(400.0)	(100.0)	(50.0)
Other long term liabilities	(5.7)	(2.8)	(70.0)	(70.0)	(70.0)
Net Assets	149.5	128.1	1,431.5	1,392.5	1,403.5
CASH FLOW					
Operating Cash Flow	48.5	62.5	29.2	207.5	268.9
Tax	(0.5)	(0.7)	(9.6)	(15.0)	(18.0)
Net Interest	(0.1)	0.0	(46.7)	(23.7)	(11.4)
Capex	(5.3)	(6.2)	(40.0)	(40.0)	(40.0)
Acquisitions/disposals **	(8.0)	(2.4)	(1,490.8)	15.0	0.0
Financing	0.9	(24.5)	1,423.1	(2.1)	(5.1)
Dividends	(33.6)	(34.3)	0.0	(76.7)	(98.5)
Net Cash Flow	1.9	(5.6)	(134.8)	65.0	96.0
Opening net debt/(cash)	4.3	2.4	10.2	145.0	80.0
HP finance leases initiated	(0.6)	(1.5)	0.0	0.0	0.0
FX/ Other	0.7	(0.7)	0.0	0.0	0.0
Closing net debt/(cash)	2.4	10.2	145.0	80.0	(16.0)

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). **2017 disposals is assumed net proceeds from the Kalixa sale: €29.0m agreed cash consideration is subject to completion account adjustments and as a payment processor these may be material; consideration is capped at €35.5m. There will also be a dividend for GVC before completion (free cash flow over and above €2.1m). We have conservatively assumed that the final cash impact of the disposal (net of expenses) is c €15m.

Contact details	Revenue by geography
32 Athol Street Douglas Isle of Man IM1 1JB +44 (0) 1624 652 559 www.gvc-plc.com	

Management team

Non executive chairman: Lee Feldman	CEO: Kenneth Alexander
Lee joined GVC in December 2004. He is the managing partner of Twin Lakes Capital, a US private equity firm focused on branded consumer products, media and business services. He is also the CEO and a board member of MacKenzie-Childs and Jay Strongwater, American luxury home furnishings and personal accessories companies.	Kenny has been chief executive of GVC (formerly Gaming VC Holdings) since March 2007. He was formerly finance director, then managing director, of the European operations of Sportingbet, which he joined in 2000. He is a member of the Institute of Chartered Accountants of Scotland and previously worked for Grant Thornton.
CFO: Richard Cooper, Paul Miles (designate)	**COO: Shay Segev**
Paul is joining the GVC board as CFO in February 2017, taking over from Richard Cooper who has been CFO since 2008. Paul was CFO of Wonga plc from late 2014 to February 2017. His previous roles include finance director of Capquest Group, group financial controller of RSA Group and acting group finance director of Phoenix Group.	Shay joined GVC in March 2016 and will be responsible for strategic and operational direction across the enlarged group and will lead the integration of the GVC and bwin.party technology platforms following completion of the recommended merger. He was formerly COO of Playtech and more recently chief strategy officer for Gala Coral Group.

Principal shareholders	(%)
Standard Life Investment Holdings	5.9
UBS Group AG	5.1
The Capital Group of Companies, Inc	5.0
Janus Capital Management	3.9
Majedie Asset Management	3.6
Directors and related parties	1.7

Companies named in this report

32Red (TTR), 888 Holdings (888), Betsson (BETS), Intertain (IT)/Jackpotjoy (JPJ), Kindred (Unibet) (KND), Ladbrokes Coral (LCL), Paddy Power Betfair (PPB), Playtech (PTEC), William Hill (WMH)