EDISON

GVC Holdings

Bigger and bolder

Trading update and historical pro-forma figures

Travel & leisure

Our updated pro-forma GVC forecasts reflect the increased LCL synergy targets (from £100m to £130m), as well as the new £2 FOBT stake limit. Overall, the investment thesis remains unchanged: GVC's enlarged business benefits from a highly scalable technology, strong brands and diversified revenue streams. We expect strong FCF to simultaneously drive down debt and return cash to shareholders. Additional upside should come from the opening of the US market, where we anticipate opportunistic expansion. The stock trades appropriately towards the top end of its peer group, at 10.8x EV/EBITDA and 14.2x P/E for FY18e.

Year end	Revenue (£m)	EBITDA (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16p	2,998.8	523.4	257.7	N/M	N/M	N/A	N/A
12/17p**	3,291.5	666.5	462.8	N/M	N/M	N/A	N/A
12/18e	3,435.1	734.9	518.2	74.6	30.0	14.2	2.8
12/19e	3,535.9	804.3	589.4	84.8	32.0	12.5	3.0
12/20e	3,454.0	739.9	534.6	76.7	34.0	13.8	3.2

Note: Pro forma results include LCL as if it has been included from 2016. *Normalised and diluted (EPS) excluding amortisation of acquired intangibles, exceptional items and share-based payments. **Continuing operations, excluding Turkey in 2017.

Strong Online trading and increased synergies

For the first 20 weeks into FY18, GVC reported 7% growth in net gaming revenues (NGR), driven by an impressive 17% increase in Online NGR. As expected, UK Retail declined by 5%, as a result of a 9% drop in sports wagers. GVC also increased its synergy targets from the LCL acquisition from £100m to £130m. As indicated previously, the vast majority of these synergies are technology-based and are expected to come to fruition in FY20 and FY21. Management will provide further details at the H118 results presentation in September.

£2 FOBT: Impact shifted to FY20

In addition to the new synergy targets, we have updated our forecasts to reflect the UK regulator's decision to reduce FOBT stakes to £2 (vs our previous £20 estimate). We now forecast c 1,000 shop closures at c £100k per shop and GVC has guided to an immediate EBITDA hit of £160m, eventually reducing to £120m post-mitigation. While the timing of implementation remains unclear, we expect the impact to begin in FY20 (rather than FY19). Altogether, we raise our FY19 EBITDA forecast from £743m to £804m, while our FY20 EBITDA forecast goes from £810m to £740m. Over this period, the steady growth in Online is therefore expected to fully offset the FOBT hit, with FY20 EBITDA broadly in line with our FY18 forecast.

Valuation: 10.8x EV/EBITDA for FY18

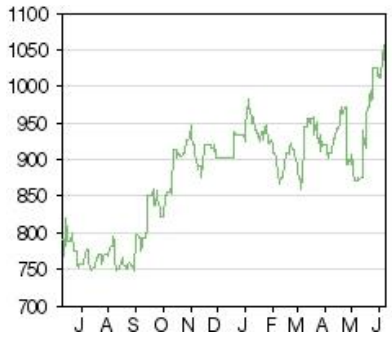
The LCL acquisition has cemented GVC's leading global position and the £130m+ cost savings are expected to contribute to significant EPS accretion. With net debt peaking at 2.45x in FY18, strong FCF should rapidly drive down leverage. There is additional potential upside from the US, which is not currently in our figures. The group trades at 10.8x EV/EBITDA and 14.2x P/E for FY18e, appropriately towards the top end of the peer group, in our view.

8 June 2018

Price	**1,056p**
Market cap	**£6,103m**

Net debt (£m) at March 2018	£1,860m
Shares in issue	578m
Free float	99%
Code	GVC
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	21.2	17.9	34.2
Rel (local)	18.8	9.8	29.2
52-week high/low		1056.0p	748.0p

Business description

GVC Holdings is a leading e-gaming operator in both the B2C and B2B markets. Following the acquisition of Ladbrokes Coral in 2018, it now has a market-leading position in UK retail betting. About 90% of revenues are derived from regulated and/or taxed markets.

Next events

Q2 trading update	July 2018
H2 results	September 2018

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Edison profile page

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Online growth offsets FOBT hit

Adjusting pro-forma forecasts for synergies and £2 FOBT

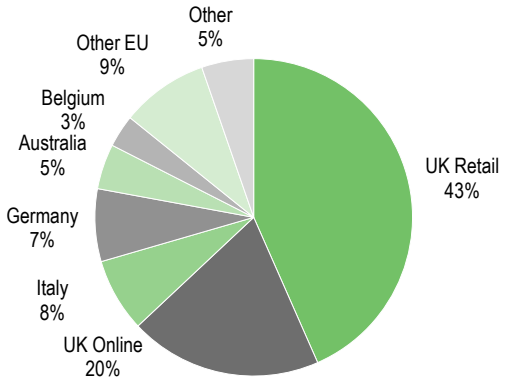
As detailed in our April 2018 update, GVC's acquisition of Ladbrokes Coral has created a global, multi-brand gaming business. The company has now provided FY17 headline pro-forma figures, with total FY17 pro-forma NGR of £3.29bn and EBITDA of £667m. Approximately 75% of total NGR was derived from the original LCL business and UK Retail comprised 42%.

We have updated our forecasts, which notably include new synergy targets (increased from £100m to £130m) as well as a £2 FOBT stake limit (vs our previous estimate of £20). Implementation of the stake limit is now expected in FY20, rather than FY19, and management expects the first full-year EBITDA to be reduced by approximately £160m (split roughly as a £180m hit to UK Retail and a £20m uplift in Online).

Altogether, we forecast 4.4% NGR growth in FY18 and 2.9% in FY19, driven by continued momentum in Online. Reflecting the impact of FOBT implementation, we forecast NGR decline of 2.3% in FY20. At this point, UK Retail is expected to comprise 30% of revenue and 10% of EBITDA, vs 42% and 38% in FY17.

As shown in Exhibit 2, we believe that the steady growth in Online NGR, combined with integration synergies, will fully offset the negative impact from the recent FOBT regulatory changes.

Exhibit 1: Geographical revenue* split



Source: GVC. Note: * Reported revenues include VAT and internal revenues ie slightly different from NGR.

Online: 49% of NGR

Pro-forma FY17 Online NGR grew 24% to £1.60bn and for the first 20 weeks of 2018, GVC reported pro-forma NGR growth of 17% (18% in constant currency). Sports Brands increased by 16%, with a sports margin of 10.4%, in line with the group's long-term margin target of 10%. Games Brands also increased by 16%, helped by a 41% increase in partypoker's NGR.

Geographically, highlights in this division included a 23% NGR increase in Germany (bwin) and a 75% increase in the newly acquired Crystalbet in Georgia. The Italian and Australian businesses are also gaining market share, delivering 18% and 44% NGR growth, respectively. In the UK, Gala and Coral grew above their peers at 8% and 15%, respectively, although Ladbrokes.com grew by only 6%, which is marginally below the market. Management's goal is to return Ladbrokes.com to market growth, which is estimated at high single-digit.

Looking forward, we forecast continued momentum in Online, with FY18 NGR increasing 12% to £1.80bn and FY19 NGR increasing 8% to £1.94bn. As this division continues to scale its proprietary

technology and efficiently manage its cost base, management has reiterated that growth in Online EBITDA will ultimately offset the anticipated reduction in UK Retail.

- **PASPA: significant upside possibilities in USA**

Following the repealing of PASPA in the US and the gradual state-by-state opening of sports-betting, there is significant upside potential in the US. GVC believes it has a substantial technological advantage (proprietary technology in gaming and sports), helped by an existing B2B platform in Nevada (Stadium Technology Group) and a casino partnership in New Jersey. Management has stated that it remains open to pursuing expansion opportunities but, while we expect further news over the next year, we have not included any significant upside into our forecasts.

- **Potential rise in UK remote gaming duty would affect Online EBITDA by c 5%**

The UK regulator has stated its intention to raise the remote gaming duty (RGD) at the next Budget, in order to offset the loss of other gaming taxes (specifically from the fixed-odds betting terminals). Currently, industry views are that the RGD will be increased from 15% to 20%, which we believe would affect EBITDA by £20–25m (c 5% of total Online EBITDA). Given the high degree of uncertainty, the possible duty increase is not currently in our forecasts.

UK Retail: 42% of NGR

The structural decline in UK Retail is well documented, with lower footfall contributing to a 9% decline in FY17 UK Retail NGR. Continuing this trend, the trading update into FY18 showed a 5% like-for-like NGR decline, with OTC net revenue 8% behind. During this period, a 9% decline in sports wagers was partially attributed to poor weather, which resulted in a 12% cancellation of all planned horse racing fixtures. Machine revenues were down 2%, which is likely to have been caused by the negative press surrounding FOBTs.

- **FOBT impact moved to FY20**

The Triennial Review has now concluded, with B2 machine stakes cut to £2 (from £100 previously) and GVC has guided to an immediate EBITDA hit of £160m (c 20% of FY18e EBITDA). The timing for implementation remains unclear, although industry speculation suggests end-FY19 or the beginning of FY20. In our model, we assume a full impact in FY20, with FOBT-related shop closures commencing that year. In this scenario, we assume a total of 1,000 shop closures (one-third of the estate) at a cost of £100k per shop (of which £50k is cash). Our forecasts include 600 shop closures in FY20, with the remaining 400 spread over the next two years. GVC estimates that post-mitigation, the ultimate impact on EBITDA will be £120m, with an expected adverse impact of c £145m in UK Retail and positive impact of c £25m in Online.

European Retail: 7% of NGR

European Retail NGR grew 14% to £240.9m in FY17, with growth accelerating to 32% into 2018 (28% constant currency), boosted by an exceptional 53% NGR increase in Eurobet (Italy). Overall, wagers increased by 4% and the sports margin improved by 3.8bp to 18.1%, due to favourable results in Italy.

We expect growth to moderate from this point, with NGR increasing by 8% in FY18 and c 5% thereafter.

We summarise our divisional forecasts in Exhibit 2 below.

Exhibit 2: Divisional summary

Pro-forma P&L	2016	2017	2018e	2019e	2020e
Online	1,296.3	1,602.8	1,799.4	1,939.8	2,090.1
UK Retail	1,431.1	1,391.1	1,331.7	1,280.5	1,033.6
European Retail	212.0	240.9	259.7	270.4	284.2
Other	59.4	56.7	44.3	45.2	46.1
Total NGR	**2,998.8**	**3,291.5**	**3,435.1**	**3,535.9**	**3,454.0**
Growth	*0.0%*	*9.8%*	*4.4%*	*2.9%*	*(2.3%)*
Online	606.8	717.9	806.1	878.1	944.3
UK Retail	1,016.3	997.6	952.2	915.5	718.3
European Retail	109.7	120.8	129.9	135.2	142.1
Other	32.2	36.5	33.2	33.9	34.6
Total contribution	**1,765.0**	**1,872.8**	**1,921.4**	**1,962.7**	**1,839.3**
Contribution margin	*58.9%*	*56.9%*	*55.9%*	*55.5%*	*53.3%*
Online	286.2	406.9	469.6	532.8	589.0
UK Retail	253.3	256.6	246.4	236.9	77.5
European Retail	41.5	48.6	51.9	54.1	56.8
Other	(12.6)	(0.3)	4.4	4.5	4.6
Corporate	(45.0)	(45.3)	(42.0)	(44.0)	(46.0)
Synergies	0.0	0.0	4.5	20.0	58.0
Total EBITDA	**523.4**	**666.5**	**734.9**	**804.3**	**739.9**
EBITDA margin	*17.5%*	*20.2%*	*21.4%*	*22.7%*	*21.4%*

Source: GVC and Edison Investment Research

Synergies update

As shown in Exhibit 3, GVC has updated its guidance relating to the synergies from the deal, from £100m to at least £130m, with improvements coming from across the company. Over time, we continue to expect management to exceed these targets, given both GVC's and LCL's impressive track record of managing complex integrations. The cost of achieving these synergies has also increased from £100m to £130m.

As detailed in our April update, we believe there are further revenue and capex synergy opportunities, although these are not factored into our estimates. Management has stated that it will be providing further details at the H118 results presentation in September.

Exhibit 3: GVC's updated synergy timetable

Originally announced (cumulative)				Updated guidance (cumulative)			Integration Costs (In Year)
Year post acq.	Exit Run Rate	Financial Year	Exit Run Rate	Increase (Run Rate)	New Exit Run Rate	Realised in Year	
Year 1	£7m	2018	£5m	£2m	£7m	£4m-£5m	£17m
Year 2	£33m	2019	£27m	£8m	£35m	£16m-£26m	£39m
Year 3	£56m	2020	£50m	£28m	£78m	£52m-£62m	£43m
Year 4	£100m	2021	£100m	£30m	£130m	£104m-£114m	£31m
Year 5	£100m	2022	£100m	£30m	£130m	£130m	-

- Synergies split: c£125m of synergies to be delivered in Online and c£5m in Corporate

Source: GVC

Estimate changes

As discussed above, we have updated our forecasts to reflect the strong trading update, the new regulatory environment, as well as increased synergy targets. The introduction of a £2 stake is expected to depress EBITDA by £160m vs our original estimate of £60m (which had been based on a £20 stake limit), but the impact will now likely occur in FY20 rather than FY19.

Exhibit 4: Estimate changes

	Revenue			EBITDA			EPS		
	Old	New	% chg	Old	New	% chg	Old	New	% chg
2018e	3,402.0	3,435.1	1.0	747.5	734.9	(1.7)	76.2	74.6	(2.0)
2019e	3,413.6	3,535.9	3.6	743.4	804.3	8.2	73.3	84.8	15.7
2020e	3,537.6	3,454.0	(2.3)	810.9	739.9	(8.8)	84.2	76.7	(9.1)

Source: Edison Investment Research

Exhibit 5: Pro-forma financial summary

(£m)	2016	2017	2018e	2019e	2020e
31-December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT					
Revenue (NGR)	2,998.8	3,291.5	3,435.1	3,535.9	3,454.0
Cost of Sales	(1,233.8)	(1,418.7)	(1,513.7)	(1,573.2)	(1,614.7)
Gross Profit	1,765.0	1,872.8	1,921.4	1,962.7	1,839.3
EBITDA	523.4	666.5	734.9	804.3	739.9
Normalised operating profit	376.4	529.5	597.9	667.3	602.9
Amortisation of acquired intangibles	(200.0)	(380.0)	(380.0)	(380.0)	(380.0)
Exceptionals	(534.3)	(59.5)	(235.7)	(39.0)	(103.0)
Share-based payments	(31.8)	(20.7)	(15.0)	(15.0)	(15.0)
Reported operating profit	(389.7)	69.3	(32.8)	233.3	104.9
Net Interest	(124.6)	(72.0)	(85.0)	(84.2)	(76.0)
Joint ventures & associates (post tax)	5.9	5.3	5.3	6.4	7.6
Profit Before Tax (norm)	257.7	462.8	518.2	589.4	534.6
Profit Before Tax (reported)	(508.5)	2.5	(112.5)	155.4	36.6
Reported tax	23.6	(9.9)	(67.4)	(76.6)	(69.5)
Profit After Tax (norm)	257.7	462.8	518.2	589.4	534.6
Profit After Tax (reported)	(508.5)	2.5	(112.5)	155.4	36.6
Minority interests	0.0	0.0	(5.0)	(5.8)	(6.3)
Discontinued operations	28.4	(13.2)	0.0	0.0	0.0
Net income (normalised)	222.1	402.6	445.8	507.0	458.8
Net income (reported)	(456.5)	(20.6)	(184.9)	73.0	(39.2)
Basic average number of shares outstanding (m)	NM	NM	578	578	578
EPS - basic normalised (p)	NM	NM	77.13	87.72	79.37
EPS - diluted normalised (p)	NM	NM	74.55	84.78	76.72
EPS - basic reported (p)	NM	NM	(31.99)	12.63	(6.79)
Dividend (p)	NM	NM	30.00	32.00	34.00
Revenue growth (%)	NM	10%	4%	3%	-2%
Gross Margin (%)	58.9	56.9	55.9	55.5	53.3
EBITDA Margin (%)	17.5	20.2	21.4	22.7	21.4
Normalised Operating Margin	12.6	16.1	17.4	18.9	17.5
BALANCE SHEET					
Fixed Assets	6,040.7	6,082.0	5,761.3	5,404.3	5,175.3
Intangible Assets	5,605.3	5,607.0	5,286.6	4,944.6	4,602.6
Tangible Assets	245.0	264.4	254.8	239.8	352.8
Investments & other	190.4	210.7	220.0	220.0	220.0
Current Assets	792.0	773.8	893.6	922.8	909.7
Stocks	1.6	2.0	2.0	2.0	2.0
Debtors	342.6	258.7	280.0	300.0	320.0
Cash & cash equivalents	272.2	328.8	411.6	400.8	347.7
Other	175.6	184.3	200.0	220.0	240.0
Current Liabilities	(1,583.1)	(1,121.0)	(1,095.0)	(1,095.0)	(1,095.0)
Creditors	(699.9)	(594.1)	(600.0)	(600.0)	(600.0)
Tax and social security	(67.7)	(253.8)	(250.0)	(250.0)	(250.0)
Short term borrowings	(742.4)	(200.0)	(200.0)	(200.0)	(200.0)
Other	(73.1)	(73.1)	(45.0)	(45.0)	(45.0)
Long Term Liabilities	(1,052.8)	(1,513.9)	(2,392.1)	(2,180.0)	(1,980.0)
Long term borrowings	(749.6)	(1,212.1)	(2,012.1)	(1,800.0)	(1,600.0)
Other long term liabilities	(303.2)	(301.8)	(380.0)	(380.0)	(380.0)
Net Assets	4,196.9	4,220.9	3,167.8	3,052.1	3,010.0
Minority interests	0.0	0.0	0.0	0.0	0.0
Shareholders' equity	4,196.9	4,220.9	3,167.8	3,052.1	3,010.0
CASH FLOW					
Op Cash Flow before WC and tax	558.6	701.2	734.9	804.3	739.9
Working capital	3.8	(29.1)	(25.0)	(25.0)	(25.0)
Exceptional & other	(534.3)	(59.5)	(235.7)	(39.0)	(73.0)
Tax	(6.5)	(14.9)	(52.4)	(76.6)	(69.5)
Net operating cash flow	21.7	597.7	421.8	663.6	572.4
Capex	(58.2)	(205.8)	(187.0)	(160.0)	(160.0)
Acquisitions/disposals	(1,032.4)	(6.0)	(3,157.0)	0.0	0.0
Net interest	(71.1)	(101.3)	(70.0)	(84.2)	(76.0)
Equity financing	158.8	47.0	2,497.0	0.0	0.0
Dividends	(30.4)	(200.1)	(192.0)	(178.0)	(189.6)
Other	109.3	0.0	(30.0)	(40.0)	0.0
Net Cash Flow	(902.4)	131.5	(717.2)	201.4	146.9
Opening net debt/(cash)	312.7	1,215.1	1,083.5	1,800.7	1,599.3
FX	0.0	0.0	0.0	0.0	0.0
Other non-cash movements	0.0	0.0	0.0	0.0	0.0
Closing net debt/(cash)	1,215.1	1,083.5	1,800.7	1,599.3	1,452.5

Source: GVC, Edison Investment Research. Note: pro-forma accounts for GVC-LCL.

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