EDISON

GVC Holdings

FY16 results

Integration paying dividends

Travel & leisure

With the successful integration of bwin, GVC's FY16 pro forma results delivered strong 9% net gaming revenue (NGR) growth and high underlying cash flow generation. 2017 has started well: group NGR is up 15% ytd, €125m cost synergies are on track and GVC has announced a second special dividend (15.1c). The group's combined scale and diversification has significantly reduced risk, with 69% of revenues derived from regulated and/or taxed markets. The stock trades at 10.5x EV/EBITDA and 14.7x P/E for 2017e, at the top end of its broader peer group.

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	14.0	6.5
12/15	247.7	54.1	50.0	76.4	56.0	11.2	6.5
12/16p**	894.6	205.7	121.2	41.5	30.0	20.7	3.5
12/17e	936.9	251.6	202.6	58.5	33.0	14.7	3.8
12/18e	992.4	287.9	240.9	68.8	38.0	12.5	4.4

Note: *Normalised and diluted (EPS) excluding amortisation of acquired intangibles, exceptional items and share-based payments. **Pro forma results include bwin.party as if it were included from 1 January 2016.

bwin bedded down

The acquisition of bwin in February 2016 marked a step change in scale and diversification, creating a top four global online gambling company. 55% of total net gaming revenues (NGR) is now derived from regulated markets and 2016 results confirmed the successful integration of the two businesses. Cost synergies of €55m were achieved by year-end 2016 and the run rate of €125m is expected by Q417. In addition, with bwin's well-invested platform and strong brands, there is significant scope for continued revenue synergies in the form of cross-sell.

2016 results: Strong revenue with margin expansion

GVC's pro forma 2016 revenues (€894.6m) and adjusted EBITDA (€205.7m) were at the top end of market expectations. Driven by the turnaround in bwin, sports labels were particularly strong (+14%), with a sports win margin of 9.6% (from 8.6%). Our 2017 and 2018 revenue and EBITDA forecasts remain largely unchanged, with an adjusted EBITDA margin of 26.9% and 29.0%. Our forecasts allow for synergy benefits, which offset expected rises in gaming taxes. The company has renegotiated its debt, reducing future finance costs. The underlying business is highly cash generative and, despite the second special dividend and progressive minimum 50% pay-out policy, we expect net debt of €131.5m to decline slightly in 2017. We forecast net cash in 2019, subject to M&A or further special dividends.

Valuation: 10.5x 2017 EV/EBITDA

GVC has an excellent track record and strong organic growth prospects, which may continue to be augmented by M&A at some stage. The stock has performed well and now trades at the top end of its broader peer group, at 10.5x EV/EBITDA and 14.7x P/E for 2017e. The Capital Markets Day in May and successful platform migrations during 2017 are key catalysts. An 8.1% FCF yield in 2018 is attractive, enabling the potential for further special dividends (not included in our forecasts).

3 April 2017

Price	**733.50p**
Market cap	**£2,158m**
	€/£1.17
Net debt (€m) at 31 December 2016	132
Shares in issue	294.2m
Free float	94%
Code	GVC
Primary exchange	LSE (Premium Segment)
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	5.5	14.2	45.3
Rel (local)	4.6	10.8	23.6
52-week high/low		769.0p	512.0p

Business description

GVC Holdings is a leading e-gaming operator in both B2C and B2B markets with four main product verticals (sports, casino, poker and bingo). About 69% of revenues come from regulated and/or taxed markets. GVC acquired bwin.party digital entertainment (bwin) on 1 February 2016 for €1.51bn.

Next events

Trading update	April 2017
Capital Markets Day	25 May 2017
H1 trading update	July 2017

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Strong 2016 performance with integration on track

9% pro forma revenue growth with margin expansion

As previously announced in February, GVC reported pro forma NGR of €894.6m. This represents a 9% increase (12% on constant currency) and compares to reported revenues of €247.7m in 2015. Within pro forma revenue, sports labels accounted for 73%, games labels for 23% and other for 4%. By geography, we estimate that the largest market (Germany) accounts for 25% and the largest unregulated market is Turkey, at 11% of revenues. The enlarged group has a very broad geographic spread elsewhere including the UK, Greece, Italy, Spain, France, Brazil and various East European markets.

Pro forma 2016 adjusted EBITDA was €205.7m, representing a margin of 23%. This was above our estimate of €204.5m and compares to a pro forma EBITDA of €163.2m (a 20.2% margin) in the previous year. The contribution margin of 52% was lower than the previous year (54%), largely due to higher VAT and gaming taxes.

On a reported basis, clean EBITDA was €193.5m compared to €54.1m in the previous year, while normalised PBT grew 102% to €93.8m. A statutory loss before tax of €138.6m reflects one-off costs of €117.8m, largely due to the acquisition of bwin.party, finance expenses of €65.3m and depreciation and amortisation charges (including acquired intangibles) of €136.5m.

Sports labels: bwin a key driver

All core sports labels delivered growth in 2016, with overall sports wagers increasing by 4% to €4,488m. An improvement in gross win (9.6% from 8.6%) contributed to a 9% growth in sports NGR, from €304.5m to €333.2m.

The higher gross win was particularly due to improved risk management in bwin sports. During the year the value of first-time deposits across the acquired bwin sports labels rose 37%, while improved products and more effective cross-sell saw games revenues from sports customers increase by 26%.

As a deliberate measure to exit poor ROI marketing in acquired businesses, sports labels marketing was only c 17% of NGR in 2016. This is expected to rise to more normal levels of 23-25% of NGR.

Trading in 2017 has continued the strong trajectory, with total sports labels NGR up 18% ytd (19% in constant currency).

Games labels: H2 returning to growth

The games labels in the bwin business have historically been the most challenged and pro forma games labels NGR declined to €203.5m from €211.8m (flat in constant currency). Pro forma contribution declined to €89.0m from €109.6m, partly due to higher gaming taxes/VAT, as well as increased investment (from a low base) in *partypoker*.

Following the enhancements during the year, the *partypoker* franchise grew 16% in H2 vs the previous year and overall games labels NGR has returned to a 4% growth in H2, with a contribution margin of 45% in H2 (vs 41% in H1).

Trading in 2017 has started well, with games labels NGR up 6% ytd (8% on a constant currency basis).

bwin integration fully on track

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 69% including taxed and soon-to-regulate). It spent much of 2016 integrating bwin (€55m of synergies achieved by year-end) and the assimilation has progressed positively and ahead of initial expectations.

The preparatory work to migrate the *Sportingbet* and associated brands onto the bwin platform has largely been completed, with three countries already switched over. The migration of the larger territories is expected to commence once the relevant football seasons have finished.

The synergy target of €125m is on track and continued momentum in cross-selling is a key opportunity. To achieve this, GVC has stated that marketing spend will increase to 23-25% of NGR vs 20% in 2016.

Finance charges

In March 2017, GVC secured a €320m senior secured term and revolving facility, comprising a €250m term loan (3.25% above Euribor) and a €70m revolving credit facility (2.75% above Euribor). GVC has no plans to draw on the revolving credit facility at this time.

The new long-term debt structure fully replaces the previous short-term financing from Nomura and represents the company's first entry into the syndicated debt market. The €250m loan from Nomura was itself a replacement of the more restrictive €400m Cerberus loan, which had originally enabled the February 2016 bwin acquisition.

Rapidly declining net debt

Year-end net debt of €132m was lower than our forecast of €145m. GVC reported material exceptional cash costs in 2016, fully offsetting the group's natural underlying cash generation. The company has guided to restructuring cash costs of €25-35m in 2017, but after this we expect the one-off restructuring and deal costs to fall away, while the cumulative synergies should continue to grow to the forecast €125m. As a result, we expect net debt to decline and our forecasts indicate net debt of €21.4m by year end 2018, depending on the dividend payout and before any potential acquisitions.

Forecast changes

Our 2017 and 2018 revenue and EBITDA forecasts remain largely unchanged. The reported strong start to the year is expected to be slightly offset by the lack of major football tournaments this summer.

Our forecasts allow for rising gaming taxes as markets regulate, but despite this we forecast normalised PBT growth of 67% and 19% in 2017 and 2018, respectively, driven by synergies and falling interest charges.

The refinancing of the original Cerberus loan has enabled the company to resume its dividend policy and the company has announced two special dividends this year, totalling 30c. Thereafter, our forecasts allow for a c 50% dividend pay-out ratio from 2017. We forecast net debt of €124.3m in 2017 and €21.4m in 2018.

Given the company's high FCF yield (5.4% and 8.1% in 2017 and 2018), there is also clear potential for additional special dividends in the future.

The reduction in net finance charges has a positive impact on our EPS estimates, which change from 55.4c to 58.5c in 2017.

Exhibit 1: Estimate changes

	Revenue (€m)			EBITDA (€m)			EPS (c)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2016	894.0*	894.6	0.1	204.5	205.7	0.6	32.1	41.5	29.4
2017e	935.2	936.9	0.2	250.0	251.6	0.6	55.4	58.5	5.6
2018e	995.0	992.4	(0.3)	285.0	287.9	1.0	68.2	68.8	0.9

Source: Edison Investment Research. Note: *As announced on 2 February 2017.

Valuation

The most straightforward way to value GVC is via a peer group comparison. The stock currently trades at 10.5x 2017e EV/EBITDA and 14.7x 2017e P/E, at the top end of its larger peer group.

Exhibit 2 compares GVC with 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.

GVC's share price has performed well over the past year, helped by encouraging KPIs, demonstration that the bwin acquisition is paying off, entry into the FTSE 250 last September and increased analyst coverage.

With the rapid momentum the group has established, we consider that it could easily merit a further premium rating to the peer group. For example, a 2017e EV/EBITDA of 11x would imply a share price of 767p and a P/E of 15.3x.

This is supported by our DCF (WACC 9.6%), which produces a value of 787p. Flexing the WACC and terminal EBITDA margins by 5% gives a range of 716-874p per share.

Exhibit 2: Peer group comparison

	Price	Market cap	EV/EBITDA (x)			P/E (x)		
	(p)	(£m)	2016e	2017e	2018e	2016e	2017e	2018e
GVC Holdings	**728**	**2,142**	**11.9**	**10.5**	**9.4**	**20.7**	**14.7**	**12.5**
888 Holdings	265	949	12.8	10.5	9.5	21.9	18.1	16.2
Betsson (BETS)	SEK 78	SEK11,285	11.6	9.7	10.1	12.9	12.1	13.0
Kindred (Unibet) (KND)	SEK 95	SEK 21770	24.6	12.7	13.2	33.9	17.4	18.5
Ladbrokes Coral (LCL)	129	2,470	NA	8.4	7.6	13.8	11.7	9.4
Paddy Power Betfair (PPB)	8,500	7,145	26.8	15.3	13.5	NA	21.8	19.3
Playtech (PTEC)	932	2,961	13.7	8.9	8.0	22.3	13.1	11.9
William Hill (WMH)	288	2,469	9.6	8.4	7.9	13.7	12.0	11.1
Average			**15.9**	**10.6**	**9.9**	**19.9**	**15.1**	**14.0**
Average ex PPB			**12.0**	**9.9**	**9.4**	**19.9**	**14.1**	**13.2**

Source: Bloomberg, Edison Investment Research. Note: Share prices at 03 April 2017.

Exhibit 3 Financial summary

€m	2014	2015	2016	2017e	2018e
Year end 31 December	(IFRS)	(IFRS)	(IFRS)	(IFRS)	(IFRS)
PROFIT & LOSS					
Revenue	224.8	247.7	894.6	936.9	992.4
Cost of Sales	(101.5)	(112.4)	(430.6)	(485.4)	(517.1)
Gross Profit (contribution)	123.3	135.4	464.0	451.6	475.3
EBITDA	49.2	54.1	205.7	251.6	287.9
Depreciation and amortisation	(5.5)	(1.4)	(27.0)	(34.0)	(37.0)
Operating Profit (norm)	43.7	52.7	178.7	217.6	250.9
Amortisation of acquired intangibles	0.0	0.0	(109.5)	(120.0)	(120.0)
Exceptional/ one-off items	0.0	(24.5)	(104.4)	(30.0)	0.0
Share based payments	(0.7)	(0.4)	(31.1)	(15.0)	(10.0)
Operating Profit	42.9	27.7	(66.3)	52.6	120.9
Net finance charges (interest plus fees)	(0.1)	(2.2)	(60.8)	(15.0)	(10.0)
Other financial expense/ associates	(1.6)	0.0	3.3	0.0	0.0
Profit Before Tax (norm)	41.3	50.0	121.2	202.6	240.9
Profit Before Tax (FRS 3)	41.3	25.5	(123.8)	37.6	110.9
Tax	(0.7)	(0.8)	0.0	(18.2)	(24.1)
Profit After Tax (norm)	40.6	49.2	116.0	184.4	216.8
Profit After Tax (FRS 3)	40.6	24.7	(123.8)	19.4	86.8
Average Number of Shares Outstanding (m)	61.1	61.3	271.8	295.0	303.0
EPS - normalised fully diluted (c)	61.4	76.4	41.5	58.5	68.8
EPS - (IFRS) (c)	66.4	40.2	(45.5)	6.6	28.6
Dividend per share declared (c)	55.5	56.0	30.0	33.0	38.0
Dividend per share paid (c)	55.0	56.0	0.0	43.2	35.0
Gross Margin (%)	54.8	54.6	51.9	48.2	47.9
EBITDA Margin (%)	21.9	21.8	23.0	26.9	29.0
Operating Margin (before GW and except.) (%)	19.4	21.3	20.0	23.2	25.3
BALANCE SHEET					
Fixed Assets	159.2	159.2	1,637.7	1,529.0	1,434.0
Intangible Assets	154.3	155.2	1,609.4	1,490.4	1,390.4
Tangible Assets	1.1	1.4	19.7	30.0	35.0
Deferred tax asset	3.8	2.6	8.6	8.6	8.6
Current Assets	49.5	72.6	478.0	370.7	498.6
Stocks	0.0	3.8	0.0	0.0	0.0
Debtors	31.7	40.6	123.2	125.0	140.0
Cash	4.8	13.4	242.8	125.7	228.6
Customer balances	13.0	14.8	112.0	120.0	130.0
Current Liabilities	(50.4)	(81.0)	(641.5)	(240.0)	(260.0)
Creditors	(46.4)	(77.3)	(238.0)	(240.0)	(260.0)
Short term borrowings	(4.1)	(3.7)	(403.5)	0.0	0.0
Long Term Liabilities	(8.8)	(22.6)	(76.9)	(320.0)	(320.0)
Long term borrowings	(3.1)	(19.8)	0.0	(250.0)	(250.0)
Other long term liabilities	(5.7)	(2.8)	(76.9)	(70.0)	(70.0)
Net Assets	149.5	128.1	1,397.3	1,339.7	1,352.6
CASH FLOW					
Operating Cash Flow	48.5	62.5	34.0	196.6	266.9
Tax	(0.5)	(0.7)	(7.9)	(15.0)	(18.0)
Net Interest	(0.1)	0.0	(47.7)	(15.0)	(10.0)
Capex	(5.3)	(6.2)	(34.8)	(30.0)	(30.0)
Acquisitions/disposals	(8.0)	(2.4)	(1,491.5)	5.0	0.0
Financing	0.9	(24.5)	1,426.6	(3.5)	0.0
Dividends	(33.6)	(34.3)	0.0	(130.9)	(106.1)
Net Cash Flow	1.9	(5.6)	(121.3)	7.2	102.8
Opening net debt/(cash)	4.3	2.4	10.2	131.5	124.3
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	131.5	124.3	21.4

Source: Company accounts, Edison Investment Research. Note: *2016 are pro forma as if bwin were included from 1 January 2016.

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