

Paysafe Group

H117 results

Growth normalises

Paysafe's H117 results show that organic constant currency growth is moderating to low double-digit rates, after an exceptional period of growth in 2016. Profitability was strong during the period, helped by the strong growth and margins of the Asia Gateway business. The sale of Asia Gateway and the acquisition of MCPS will both help reduce the group's exposure to online gambling, and MCPS will strengthen the group's position in bricks and mortar payment processing.

Year end	Revenue (\$m)	EBITDA* (\$m)	EPS* (c)	DPS (c)	P/E (x)	EV/EBITDA (x)
12/13	253.4	53.1	15.1	0.0	50.2	74.2
12/14	365.0	82.9	22.0	0.0	34.5	47.5
12/15	613.4	152.6	25.6	0.0	29.7	25.8
12/16	1,000.3	300.8	42.1	0.0	18.0	13.1

Note: *EBITDA and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments

Growth moderates in H117

Paysafe saw growth moderating across all divisions, with reported revenue growth of 11% and organic constant currency growth of 12% (H116: 20%, H216: 21%). Once the major merchant is excluded, this moderated to 10%. The company achieved an EBITDA margin of 31.4%, better than the company's (pre-bid) guidance for a margin of at least 30.1%. The tax rate has trended up, as expected, as more revenues were generated in higher tax regions. Adjusted EPS increased 23% y-o-y to 25c. The company ended H117 with net debt (including deferred financing fees) of \$259.9m.

Pro forma financials show potential impact of deals

Paysafe has provided pro-forma financials to show the financial performance of the Asia Gateway business (due to be sold when the takeover of Paysafe completes) and Merchants' Choice Payment Solutions (MCPS - in the process of being acquired by Paysafe) during H117. The Asia Gateway business grew faster than the rest of the Payment Processing division, achieved a higher EBITDA margin (39.5%) and net margin (38.2%) than the Paysafe group and contributed 23% of group earnings in H117. MCPS showed 3% revenue growth, achieved a 15.0% EBITDA margin and 3.6% net margin, and if owned for the whole of H117, would have added 5% to H1 earnings before synergies.

Valuation: Reflects active payments M&A market

The formal offer of 590p is at a 9% premium to the closing price on 20 July but at a 34% premium to the volume weighted average price over the six months to 30 June, just prior to the start of sector M&A activity. Prior to 21 July (when the potential bid was announced), the stock had gained 46% year to date.

Software & comp services

11 August 2017
Price **583.50p**
Market cap **£2,830m**

€1.1/US\$1.3/£

Net debt (\$m) at end H117, including deferred financing fees 259.9

Shares in issue 484.9m

Free float 98.7

Code PAYS

Primary exchange LSE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 11.46 23.28 40.53

Rel (local) 10.82 23.35 29.48

52-week high/low 595.0p 305.7p

Business description

Paysafe Group is a global payment solutions specialist operating in three areas: payment processing, digital wallets and prepaid services.

Next events

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Review of H117 results

Exhibit 1: Financial highlights			
\$000	H117	H116	y-o-y
Revenues	538,656	486,739	10.7%
Gross margin	56.0%	53.5%	2.4pp
Adjusted EBITDA	169,242	144,180	17.4%
EBITDA margin	31.4%	29.6%	1.8pp
Adjusted EBIT	152,048	129,244	17.6%
EBIT	99,601	89,702	11.0%
Net interest expense	(10,554)	(15,151)	-30.3%
Adjusted PBT	141,494	114,093	24.0%
PBT	89,047	74,551	19.4%
Tax	(15,340)	(10,012)	53.2%
Adjusted net income	124,054	101,381	22.4%
Net income	73,707	64,539	14.2%
Normalised EPS (c)	24.7	20.1	23.0%
EPS (c)	15.2	13.4	13.2%

Source: Paysafe

Paysafe reported H117 revenue growth of 10.7% y-o-y (+12% organic, constant currency) and an increase in gross margin of 2.4pp. Adjusted EBITDA increased by 17.4% generating an EBITDA margin of 31.4%, up 1.8pp from a year ago and 1.3pp from FY16.

Exceptional items totalled \$21.9m in H117, including acquisition-related costs of \$1.4m, foreign exchange losses totalling \$7.0m and adjustments related to contingent consideration. In H117, the share-based contingent consideration owing to Meritus resulted in a fair value loss of \$12.8m. During the period, the FANS consideration was renegotiated for certain vendors, with a cash payment of \$3.3m agreed in place of share-based consideration that would have resulted in the issue of 790,908 shares over a three-year period. This resulted in an exceptional loss of \$1.2m. Paysafe also recognised an exceptional gain of \$0.7m due to MeritCard not hitting all of its post-acquisition targets.

The reported tax rate was 17.2% for the period, up from 13.4% in H116 but essentially flat compared to H216. The adjusted tax rate of 12.3% was higher than the 11.1% in H116 but lower than H216's 12.7% rate. Intellectual property was transferred from the Isle of Man to the UK during H117 and this had a one-off positive impact on the rate – without that the rate would have been c 14%. The company switched its tax residence from the Isle of Man to the UK on 1 August 2017.

The company ended H117 with a net debt position (including deferred financing fees) of \$259.9m, down from \$279.8m at the end of FY16. This resulted in a net debt/LTM adjusted EBITDA ratio of 0.8x at the end of H117, down from 0.9x at the end of FY16. Adjusted cash conversion (adjusted free cash flow as a percentage of adjusted EBIT) was 98% in H117 (H116: 74%). Before payments working capital, cash conversion was 77% (H116: 78%).

The largest customer made up 19% of group revenues, down from 20% in H116 and FY16. Excluding Asia Gateway revenues, the group grew revenues 10% on an organic, constant currency basis.

Exhibit 2: Divisional performance

	H115	H215	H116	H216	H117
Payment processing					
Reported revenue growth	47%	28%	34%	17%	14%
Pro forma constant currency revenue growth	7%	25%	28%	15%	16%
Pro forma constant currency revenue growth excl. major merchant	24%	33%	32%	10%	11%
Reported gross margin	37%	37%	39%	42%	42%
Digital Wallet					
Reported revenue growth	20%	127%	195%	50%	8%
Pro forma constant currency revenue growth	20%	14%	28%	33%	9%
Reported gross margin	73%	73%	76%	74%	81%
Prepaid					
Reported revenue growth	N/A	N/A	N/A	42%	5%
Pro forma constant currency revenue growth	12%	10%	11%	19%	9%
Pro-forma/reported gross margin	50%	51%	52%	53%	52%
Group					
Reported revenue growth	40%	90%	118%	32%	11%
Pro forma constant currency revenue growth	12%	14%	20%	21%	12%
Reported gross margin	45%	50%	54%	55%	56%
Source: Paysafe					

Payment Processing

Payment Processing showed strong constant currency organic growth of 16% in H117. Excluding the major merchant, growth was 11%, moderating from the 32% achieved in H116 but similar to the 10% reported in H216. Volumes processed of \$12.4bn were 10.7% higher than a year ago; the take rate of 2.1% was flat year-on-year. Gross margin increased year-on-year but was flat versus H216.

Digital Wallets

Digital Wallets also saw a moderating growth rate: in H117 constant currency organic growth fell to 9% from 28% in H116 and 33% in H216. Several factors reduced the growth rate: a) the company withdrew from servicing online gambling in Japan for regulatory reasons; b) the issuance of pre-paid cards was restricted in non-SEPA countries; and c) more rigorous KYC measures were enforced. In addition, 2016 saw the benefit of the UEFA championships and volume growth from the addition of new territories and payment methods. Volumes processed in H117 of \$10.7bn were 6% lower than a year ago, although the take rate increased to 1.5% from 1.3% as a result of fee increases enacted over the last 12 months. Additionally, revenues from Income Access (acquired September 2016) and card issuing do not generate transaction volumes. Gross margin saw a significant uptick (81% vs 76% in H116 and 74% in H216), helped by the termination of lower-margin business and lower bad debts.

Prepaid

The Prepaid division achieved organic constant currency revenue growth of 9% in H117, down from 11% in H116 (once the impact of discontinued Ukash business is excluded). Volumes transacted were flat year-on-year at \$1.4bn, with the take rate increasing marginally to 7.7% from 7.6% a year ago. Gross margin was substantially unchanged compared to H116 and H216.

Pro-forma financials

The company also provided pro-forma financials for H117 for the Asia Gateway (due to be sold at the same time as the takeover) and Merchants' Choice Payment Solutions (MCPS – agreement to acquire announced 21 July).

Exhibit 3: Pro-forma financials for H117

\$m	Paysafe	Asia Gateway	MCPS	Pro-forma group*
Revenues	538.7	76	167	629.7
Adjusted EBITDA	169.2	30	25	164.2
Adjusted EBITDA margin	31.4%	39.5%	15.0%	26.1%
Adjusted EBIT	152.0	29	18	141
Adjusted EBIT margin	28.2%	38.2%	10.8%	22.4%
Adjusted net income	124.1	29	6	101.1
Adjusted net margin	23.0%	38.2%	3.6%	16.1%

Source: Paysafe. Note: *Paysafe plus MCPS minus Asia Gateway.

The Asia Gateway grew revenues 20% y-o-y in H117 and generated an EBITDA margin of 39.5%, which implies that the remaining Paysafe business generated an EBITDA margin of 30.0% in H117. The Asia Gateway business paid no tax so generated a strong net margin of 38.2% compared to the group net margin of 23.0%.

MCPS saw growth in pro-forma revenues of 3% y-o-y in H117 and generated an EBITDA margin of 15%. MCPS incurs a higher tax charge than Paysafe as it is US-based. As previously stated, Paysafe is targeting annualised cost synergies of \$7.5m by the end of FY18. This acquisition will substantially increase the proportion of Payment Processing revenues from bricks and mortar stores.

Exhibit 4: Financial summary

	\$'000s	2013	2014	2015	2016
Year end 31 December		IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue		253,367	364,954	613,392	1,000,282
Cost of Sales		(121,484)	(187,298)	(316,922)	(457,420)
Gross Profit		131,883	177,656	296,470	542,862
EBITDA		53,106	82,946	152,620	300,825
Company EBITDA		52,213	85,965	152,563	300,825
Operating Profit (before amort acq intang, SBP and except.)		42,888	71,257	133,201	268,251
Amortisation of acquired intangibles		(3,300)	(9,200)	(31,900)	(51,900)
Exceptionals		(1,368)	7,219	(60,986)	(8,249)
Share-based payments		(4,512)	(8,274)	(14,089)	(13,726)
Operating Profit		33,708	61,002	26,226	194,376
Net Interest		(995)	(2,024)	(14,418)	(26,383)
Profit Before Tax (norm)		41,893	69,233	118,783	241,868
Profit Before Tax (FRS 3)		32,713	58,978	11,808	167,993
Tax		(1,235)	(1,303)	(4,405)	(25,972)
Profit After Tax (norm)		40,311	67,703	108,686	212,968
Profit After Tax (FRS3)		31,478	57,675	7,403	142,021
Average Number of Shares Outstanding (m)		252.2	277.7	399.8	483.6
EPS - normalised (c)		15.1	22.0	25.6	42.1
EPS - FRS 3 (c)		12.5	20.8	1.9	29.4
DPS (c)		0.00	0.00	0.00	0.00
Gross Margin (%)		52.1%	48.7%	48.3%	54.3%
EBITDA Margin (%)		21.0%	22.7%	24.9%	30.1%
Company EBITDA Margin (%)		20.6%	23.6%	24.9%	30.1%
Operating Margin (before am and except.) (%)		16.9%	19.5%	21.7%	26.8%
BALANCE SHEET					
Fixed Assets		65,551	295,955	1,569,269	1,552,326
Intangible Assets		53,231	284,723	1,548,253	1,518,445
Tangible Assets		12,320	10,114	18,492	23,452
Other Fixed Assets		0	1,118	2,524	10,429
Current Assets		184,490	177,275	259,045	420,313
Cash & cash equivalents		164,379	109,893	117,875	231,157
Restricted NETELLER cash		6,198	8,777	29,070	31,854
Cash held as reserves & settlement assets		0	38,607	66,341	100,459
Receivable from Members & Merchants		0	0	0	0
Trade and other debtors		13,913	19,998	45,759	56,843
Current Liabilities		117,634	114,410	170,943	232,617
Creditors		107,524	58,240	121,070	175,464
Payable to Members/Merchant liability		0	30,591	16,758	18,547
Short term borrowings		10,110	25,579	33,115	38,606
Long Term Liabilities		801	150,498	582,804	521,788
Long term borrowings		801	107,205	494,410	456,570
Other long term liabilities		0	43,293	88,394	65,218
Net Assets		131,606	208,322	1,074,567	1,218,234
CASH FLOW					
Operating Cash Flow		94,542	42,699	91,711	278,487
Net Interest		(158)	(1,873)	(8,403)	(12,459)
Tax		(1,191)	(1,564)	(4,929)	(10,186)
Capex		(13,567)	(11,094)	(23,721)	(53,698)
Acquisitions/disposals		(5,281)	(169,192)	(1,102,070)	(43,827)
Financing		1,188	(4,939)	670,173	(13,482)
Dividends		0	0	0	0
Net Cash Flow		75,533	(145,963)	(377,239)	144,835
Opening net (debt)/cash		85,829	118,389*	(22,891)	(409,650)
HP finance leases initiated		0	0	0	0
Other		(1,697)	4,683	(9,520)	796
Closing net (debt)/cash		159,665*	(22,891)	(409,650)	(264,019)

Source: Paysafe. Note: *Does not match as method of reporting was changed.

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