EDISON

Jackpotjoy plc

Q2 financial statements

A third set of reassuring quarterly figures

Travel & leisure

Jackpotjoy plc (JPJ) has produced another set of robust quarterly earnings, with Q217 revenues increasing 17% to £75.2m and a 39.9% EBITDA margin. The core Jackpotjoy division grew 18% and is gaining market share. Q3 has started well, management has reiterated its expectations for FY17 and our forecasts remain unchanged. The stock trades at a significant discount to peers, with 2018e multiples of 7.2x EV/EBITDA, 6.1x P/E and 15.0% free cash flow yield. The balance sheet is simplifying following a major earn-out payment and, as the company continues to demonstrate its market dominance, we would expect a re-rating in the shares.

Year end	Revenue (£m)	EBITDA* (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/15	194.6	70.4	46.1	73.0	0.0	9.1	N/A
12/16	269.0	102.2	65.6	88.4	0.0	7.5	N/A
12/17e	294.8	105.7	70.9	93.8	0.0	7.1	N/A
12/18e	322.3	113.8	84.4	109.2	0.0	6.1	N/A
12/19e	345.3	116.4	93.0	118.0	0.0	5.6	N/A

Note: *EBITDA, PBT and EPS (fully diluted) are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. EPS is fully diluted.

Continued momentum, forecasts unchanged

Q2 revenues grew by 17% to £75.2m, primarily driven by an 18% increase in the core Jackpotjoy division. Mandalay has reversed the decline in Q117 and is up 10% sequentially. Benefiting from currency, Vera&John grew 30% vs Q216. Average LTM active customers increased 13% to 243,896 vs the prior year and average real money gaming (RMG) per month grew 16% to £21.8m. The Q2 adjusted EBITDA margin of 39.9% is expected to decline in H217, with the impact of higher gaming taxes as well as a significant marketing campaign. Our forecasts remain unchanged.

A simplifying balance sheet

Following the £94.2m earn-out payment to Gamesys, JPJ ended the quarter with an unrestricted cash balance of £24.0m and net debt of £325.3m. The most significant remaining obligation is a c £44m earn-out payment in June 2018 (for Botemania). Adjusted net debt/EBITDA remains high at 3.6x, but underlying cash conversion in Q217 was 99% and JPJ currently generates c £20-25m operating cash flow per quarter. We forecast net debt of £290.2m in 2018, with an adjusted net leverage of 2.7x, reaching the company's target of 2.0x during 2019.

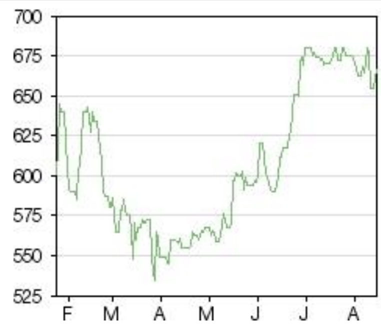
Valuation: 7.2x 2018e EV/EBITDA

Since its LSE listing, JPJ has produced three sets of robust quarterly reports. The stock trades at a meaningful discount to its peer group, at 7.2x EV/EBITDA, 6.1x P/E and 15.0% free cash flow yield for 2018. The valuation reflects legacy concerns over the Gamesys relationship, high leverage, the lack of dividend and low stock liquidity. In our view, cash generation should lead to demonstrable debt reduction from 2018 and we would expect a re-rating as the market regains confidence in the business.

15 August 2017

Price	**665p**
Market cap	**£492m**
	€1.1/£
Net debt (£m) at 30 June 2017	325
Shares in issue	74.1m
Free float	95%
Code	JPJ
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(0.5)	17.4	N/A
Rel (local)	(0.6)	18.5	N/A
52-week high/low		680.0p	534.0p

Business description

Jackpotjoy plc (JPJ) (formerly The Intertain Group) is a leading online gaming operator mainly focused on bingo-led gaming targeted towards female audiences. About 77% of revenues are generated in regulated markets. It moved its listing from the TSX to the LSE in January 2017.

Next events

Q3 financial statements	13/11/17

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Edison profile page

Jackpotjoy plc is a research client of Edison Investment Research Limited

Q217 results

Overview

Q217 revenue increased 17% to £75.2m, driven by an 18% growth in the core Jackpotjoy division, representing 5.3% sequential growth. At June 2017, average active customers grew 13% in the quarter to 243,896 vs the prior year and average RMG per month grew 16% to £21.8m, equating to £89 per customer.

The company reported an adjusted Q2 EBITDA margin of 39.9% vs 36.5% in the prior year. This compares to 40.9% in Q117, which also benefited from lower than average marketing costs. Our FY17 EBITDA margin forecast is 35.9%.

Q2 selling and marketing costs were 14.4% of revenues. Management has reiterated that these costs will rise during H2 with significant planned TV campaigns. Our full year selling and marketing estimate is 15.5% of revenues.

Excluding exceptional items, cash conversion was 99% and resulted in a quarterly operating cash flow of £22.3m. After the £94.2m earn-out payment to Gamesys in June, JPJ ended the quarter with an unrestricted cash balance of £24.0m and net debt of £325.3m.

Management has stated that trading into Q3 is solid and our forecasts remain unchanged.

Jackpotjoy (70% of revenues)

JPJ reported another strong quarter across all brands in the Jackpotjoy division, which grew 18% to £52.3m, with an adjusted EBITDA of £24.9m (47.6% margin). Jackpotjoy UK comprised 67% of divisional revenues vs 70% in the prior year. While Jackpotjoy UK and Jackpotjoy Sweden have demonstrated steady organic growth, the most significant increase is from Botemania (Spain) and Starspins, which now comprise 21% of divisional revenues.

Vera&John (23% of revenues)

Gaming revenue from Vera&John increased 30% to £17.4m in Q2 vs the prior year, due to £/€ currency movements. Adjusted EBITDA of £5.1m represents a margin of 29.3%. Due to higher marketing costs, this is lower than the 31.3% Q216 EBITDA margin.

Mandalay (7% of revenues)

Q217 revenues were flat at £5.5m vs the prior year but importantly have grown 10% sequentially. As discussed at Q1 results, management has focused on changing promotional spend to improve operational margins and deposit hold in future periods. Due to lower marketing spend, EBITDA was £2.4m vs £1.6m in Q216.

Exhibit 1: JPJ gaming revenue split*

£m	2016	2017e	2018e	2019e
Jackpotjoy	188.2	208.3	229.7	247.6
growth	55.3%	10.7%	10.3%	7.8%
Vera&John	57.0	64.7	70.6	75.5
growth	35.4%	13.6%	9.0%	7.0%
Mandalay	21.7	21.8	22.0	22.2
growth	1.2%	0.1%	1.0%	1.0%
Total gaming revenue	**266.9**	**294.8**	**322.3**	**345.3**
growth	38.2%	10.4%	9.3%	7.1%

Source: Jackpotjoy accounts, Edison Investment Research. Note: *Excludes other non-gaming income of £2.1m in 2016 (revenue guarantee and platform migration).

Gaming taxes and regulation

JPJ operates largely in regulated markets and Q217 gaming taxes were £8.5m, 11.3% of total revenues. Going forward, these taxes are expected to rise steadily. Notable increases include:

- **UK Point of Consumption Tax (POCT)**: The extension of POCT to include free bets in the UK is expected to be enforced from August 2017. Our forecasts indicate a c 3-4% impact to the UK businesses' EBITDA (Mandalay and Jackpotjoy UK).
- **Spain:** The 25% tax on Spanish gross gaming revenues will become more relevant as the Botemania revenues grow. We estimate that Botemania comprises c 10% of the Jackpotjoy division.
- **Sweden**: Our forecasts include the expected 18% gaming tax in Sweden from 2019. This will mostly have an impact on the Vera&John division, but we estimate that c 5-6% of the Jackpotjoy division is also derived from Sweden.

Cash flow and balance sheet

Following the £94.2m earn-out payment to Gamesys, JPJ ended the quarter with an unrestricted cash balance of £24.0m and net debt of £325.3m. Including the remaining earn-outs (c £44m to Botemania in June 2018), adjusted net debt/EBITDA ratio was 3.6x, from 4.0x in Q17.

Excluding exceptional items, cash conversion in Q2 was 99% and JPJ currently generates approximately £20-25m operating cash flow per quarter. The company is therefore comfortably positioned to pay its future earn-out obligations. We forecast net debt of £290.2m in 2018, with an adjusted net leverage of 2.7x, reaching the company's target of 2.0x during 2019.

Under the terms of its covenants, the group is permitted to pay dividends once adjusted leverage reaches 2.75x and the company has stated that it intends to begin paying dividends once the balance sheet is closer to sector average debt levels. We have not included dividends in our forecasts, but we believe cash returns could begin in 2019.

Exhibit 2: Financial summary

£m	2015	2016	2017e	2018e	2019e
Year end 31 December					
PROFIT & LOSS					
Revenue	194.6	269.0	294.8	322.3	345.3
Cost of Sales	(101.4)	(130.7)	(138.1)	(162.8)	(179.5)
Gross Profit	93.3	138.3	156.7	159.5	165.7
EBITDA	70.4	102.2	105.7	113.8	116.4
Operating Profit (before amort. and except.)	70.1	101.6	104.3	112.4	115.0
Intangible Amortisation	(50.6)	(55.5)	(55.0)	(55.0)	(55.0)
Exceptional and other items*	(109.7)	(52.5)	(9.7)	(5.2)	(4.9)
Share based payments	(2.9)	(2.3)	(2.1)	(2.5)	(2.5)
Operating Profit	(93.1)	(8.7)	37.5	49.6	52.5
Net Interest	(24.0)	(35.9)	(33.3)	(28.0)	(22.0)
Profit Before Tax (norm)	46.1	65.6	70.9	84.4	93.0
Profit Before Tax (FRS 3)	(114.2)	(40.7)	(1.0)	24.3	33.0
Tax	(0.5)	0.1	(0.7)	(2.5)	(4.5)
Profit After Tax (norm)	45.5	65.7	70.3	81.9	88.5
Profit After Tax (FRS 3)	(114.8)	(40.6)	(1.7)	21.8	28.5
Average Number of Shares Outstanding (m)	61.2	71.2	74.4	74.5	74.5
EPS - normalised (p)	74.4	92.2	94.4	109.9	118.8
EPS - normalised and fully diluted (p)	73.0	88.4	93.8	109.2	118.0
EPS - (IFRS) (p)	(187.5)	(57.1)	(2.3)	29.2	38.3
Dividend per share (p)	0.0	0.0	0.0	0.0	0.0
Gross Margin (%)	47.9	51.4	53.2	49.5	48.0
EBITDA Margin (%)	36.2	38.0	35.9	35.3	33.7
Operating Margin (before GW and except.) (%)	36.0	37.8	35.4	34.9	33.3
BALANCE SHEET					
Fixed Assets	674.3	652.3	598.4	545.9	494.5
Intangible Assets	668.8	648.8	593.8	538.8	483.8
Tangible Assets	0.2	0.9	1.9	4.5	8.0
Other long term assets	5.3	2.6	2.6	2.6	2.6
Current Assets	63.9	139.0	80.5	70.8	97.8
Stocks	0.0	0.0	0.0	0.0	0.0
Debtors (incl swaps)	25.6	62.0	35.0	37.0	37.0
Cash	31.8	68.5	36.5	23.8	49.8
Player balances	6.5	8.6	9.0	10.0	11.0
Current Liabilities	(54.3)	(154.9)	(118.7)	(64.4)	(60.7)
Creditors	(23.1)	(41.3)	(40.0)	(34.0)	(34.0)
Short term borrowings	(25.2)	(26.7)	(26.7)	(26.7)	(26.7)
Contingent consideration	(6.0)	(86.9)	(52.0)	(3.8)	0.0
Long Term Liabilities	(394.8)	(397.1)	(333.4)	(289.4)	(239.4)
Long term borrowings	(189.3)	(347.4)	(317.4)	(287.4)	(237.4)
Contingent consideration	(203.6)	(33.3)	0.0	0.0	0.0
Other long term liabilities	(2.0)	(16.4)	(16.0)	(2.0)	(2.0)
Net Assets	289.0	239.4	226.8	263.0	292.3
CASH FLOW					
Operating Cash Flow	23.3	83.0	98.7	108.8	114.5
Net Interest	(24.0)	(35.9)	(32.0)	(28.0)	(22.0)
Tax	(0.5)	(1.2)	(0.7)	(2.5)	(4.5)
Capex	(2.5)	(2.5)	(2.5)	(4.0)	(5.0)
Acquisitions (inc earn-outs)	(355.6)	(156.3)	(101.0)	(57.0)	(7.0)
Financing	203.7	(10.0)	35.5	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0
Net Cash Flow	(155.6)	(122.9)	(2.0)	17.3	76.0
Opening net debt/(cash)	27.1	182.7	305.6	307.5	290.2
HP finance leases initiated	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	(0.0)
Closing net debt/(cash)	182.7	305.6	307.5	290.2	214.2
NPV of outstanding earnouts/ other	209.5	140.7	70.0	18.0	10.0
Currency swaps	(4.7)	(38.2)	0.0	0.0	0.0
Adjusted net debt	387.5	408.1	377.5	308.2	224.2

Source: Jackpotjoy accounts, Edison Investment Research. Note: *Exceptional and other items include transaction-related costs, severance costs, fair value adjustments on contingent consideration and gain on cross-currency swap.

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