

21 May 2018

**EML Payments Limited (EML) BUY Share Price: \$1.30**

**Favourable gaming regulation changes in key markets Target Price: A\$1.91**

The potential value of EML's strong relationships with leading global bookmakers increased significantly last week due to major industry changes in the US and UK. This further increases our confidence regarding EML's long-term growth opportunities in the Gaming market globally. We reiterate our Buy recommendation and A\$1.91 target price.

#### Major regulation changes favourable for Gaming

- Early in the week, the US Supreme Court ruled that legislation, known as PASPA, which prevented individual states legalising Sportsbetting was unconstitutional. As a result, any US state that now wishes to legalise Sportsbetting is free to do so.
- This was followed by the UK Government reducing the maximum stake on Fixed Odds Betting Terminals (FOBTs) from GBP100 to GBP2.

#### Opening of US market

- The US gaming market offers significant potential upside to EML, with the current illegal market estimated to generate ~US\$150bn in turnover p.a.
- Over twenty states, prior to the ruling, expressed an interest in regulating should PASPA be overturned.
- Paddy Power Betfair (PPB), which owns Sportsbet, EML's largest Gaming client, wasted no time in strategically positioning itself for the US market, announcing that it is in merger talks with leading fantasy sports operator, FanDuel (6m+ active US customers).
- We expect that Bet365, PPB, William Hill and Ladbrokes (all EML customers) will follow suit, acquiring databases and brands.
- We see substantial potential upside to EML from the US Sportsbetting market, which is ~3x larger than the UK and ~200x larger than Australia.

#### Financial Summary

- In the UK, the reduction of the maximum FOBT stake is expected to result in ~50% of UK betting shops closing.
- As these shops were used as quasi-banks for online gaming customers of the larger multichannel operators, we see this as a substantial opportunity for EML to win large customers in the UK, particularly William Hill and Ladbrokes (already customers in the UK).

#### High conviction Buy

- EML is trading at a significant discount to its payment peers, which given its impressive track record, strong organic growth potential and balance sheet strength is completely unwarranted in our view.
- We have high conviction in our Buy recommendation.

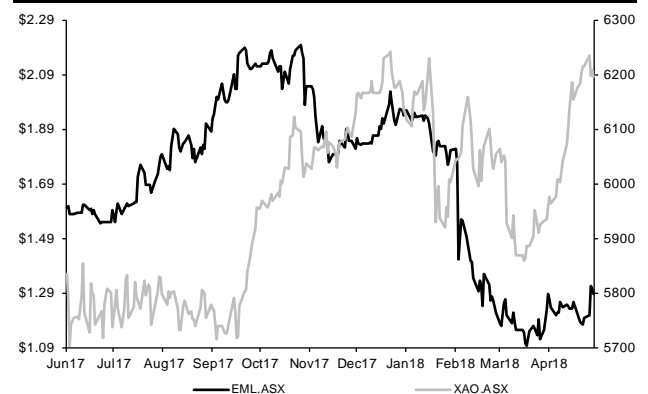
#### Company Data

|                                |                  |
|--------------------------------|------------------|
| Shares – ordinary (M)          | 245.0            |
| Dilution (M)                   | 4.6              |
| Total (fully diluted) (M)      | 249.6            |
| Market capitalisation (\$M)    | 318.5            |
| 12 month low/high (\$)         | 1.05/ 2.26       |
| Average monthly turnover (\$M) | 14               |
| Index                          | All Ords         |
| GICS Industry                  | Consumer Finance |

#### Financial Summary (fully diluted/normalised)

| Year end June          | 2016A | 2017A | 2018F | 2019F | 2020F |
|------------------------|-------|-------|-------|-------|-------|
| Revenue (\$M)          | 23.3  | 58.0  | 64.8  | 71.7  | 77.3  |
| Costs (\$M)            | -18.3 | -43.5 | -44.1 | -44.8 | -45.2 |
| EBITDA (\$M)           | 5.0   | 14.5  | 20.7  | 26.9  | 32.1  |
| NPAT (\$M)             | 2.5   | 9.7   | 13.2  | 19.4  | 23.3  |
| EPS (¢ps)              | 1.3   | 3.9   | 5.3   | 7.8   | 9.3   |
| EPS Growth (%)         | 35    | 208   | 35    | 47    | 20    |
| PER (x)                | 93.3  | 33.3  | 24.7  | 16.7  | 13.9  |
| Free Cashflow (\$M)    | 0.9   | 16.6  | 20.4  | 23.6  | 29.1  |
| FCFPS (¢ps)            | 0.4   | 6.6   | 8.2   | 9.5   | 11.7  |
| PFCFPS (x)             | 265.6 | 19.3  | 15.7  | 13.5  | 11.0  |
| Enterprise Value (\$M) | 249.2 | 278.6 | 259.9 | 236.2 | 207.1 |
| EV / EBITDA (x)        | 49.5  | 19.2  | 12.5  | 8.8   | 6.5   |
| Payout ratio (%)       | n/m   | n/m   | n/m   | n/m   | n/m   |
| Dividends (¢ps)        | n/m   | n/m   | n/m   | n/m   | n/m   |
| Yield (%)              | n/m   | n/m   | n/m   | n/m   | n/m   |
| Franking (%)           | n/m   | n/m   | n/m   | n/m   | n/m   |

#### EML – performance over one year



#### Disclosure and Disclaimer

This report must be read with the disclosure and disclaimer on the final page of this document.

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## Analysis

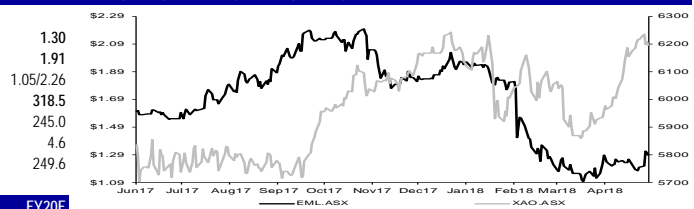
### EML Payments Limited

Year end 30 June

#### MARKET DATA

|                           |     |           |
|---------------------------|-----|-----------|
| Recommendation            |     |           |
| Price                     | \$  | 1.30      |
| Target price (12-month)   | \$  | 1.91      |
| 52 week low / high        | \$  | 1.05/2.26 |
| Market capitalisation     | \$m | 318.5     |
| Shares on issue (basic)   | no. | 245.0     |
| Options                   | no. | 4.6       |
| Shares on issue (diluted) | no. | 249.6     |

#### 12-MONTH SHARE PRICE PERFORMANCE



#### INVESTMENT FUNDAMENTALS

|                                   | FY16A | FY17A | FY18F   | FY19F | FY20F |       |
|-----------------------------------|-------|-------|---------|-------|-------|-------|
| Reported NPAT                     | \$m   | 0.1   | 0.0     | 6.0   | 12.5  | 16.4  |
| NPAT normalised                   | \$m   | 2.5   | 9.7     | 13.2  | 19.4  | 23.3  |
| Reported EPS (undiluted)          | ¢     | 0.0   | 0.0     | 2.4   | 5.0   | 6.6   |
| EPS normalised (undiluted)        | ¢     | 1.3   | 3.9     | 5.3   | 7.8   | 9.3   |
| ....Growth                        | %     | 35%   | 208%    | 35%   | 47%   | 20%   |
| PER normalised                    | x     | 102.8 | 33.3    | 24.7  | 16.7  | 13.9  |
| Operating cash flow per share     | ¢     | 0.9   | 7.8     | 9.5   | 10.8  | 13.1  |
| Free cash flow per share          | ¢     | 0.4   | 6.7     | 8.3   | 9.6   | 11.9  |
| Price to free cash flow per share | x     | 292.6 | 19.3    | 15.7  | 13.5  | 11.0  |
| FCF yield                         | %     | 0.3   | 5.2     | 6.4   | 7.4   | 9.1   |
| Dividend                          | ¢     | 0.0   | 0.0     | 0.0   | 0.0   | 0.0   |
| Payout                            | %     | 0.0   | 0.0     | 0.0   | 0.0   | 0.0   |
| Yield                             | %     | 0.0   | 0.0     | 0.0   | 0.0   | 0.0   |
| Franking                          | %     | n/a   | n/a     | n/a   | n/a   | n/a   |
| Enterprise value                  | \$m   | 278.6 | 278.6   | 259.9 | 236.2 | 207.1 |
| EV/EBITDA                         | x     | 55.3  | 19.2    | 12.5  | 8.8   | 6.5   |
| EV/EBIT                           | x     | 212.0 | (312.0) | 32.2  | 14.1  | 9.5   |
| Price to book (NAV)               | x     | 2.9   | 5.2     | 2.9   | 2.5   | 2.1   |
| Price to NTA                      | x     | 5.6   | 4.9     | 4.2   | 3.2   | 2.4   |

#### KEY RATIOS

|               | FY16A | FY17A | FY18F | FY19F | FY20F |      |
|---------------|-------|-------|-------|-------|-------|------|
| EBITDA margin | %     | 21.6  | 25.0  | 32.0  | 37.5  | 41.5 |
| EBIT margin   | %     | 5.6   | (1.5) | 12.5  | 23.3  | 28.3 |
| NPAT margin   | %     | 0.4   | 0.0   | 9.3   | 17.5  | 21.3 |
| ROE           | %     | 0.1   | 0.0   | 5.4   | 9.8   | 11.0 |
| ROA           | %     | 0.1   | 0.0   | 4.3   | 7.9   | 8.9  |

|   |     |        |        |        |        |         |
|---|-----|--------|--------|--------|--------|---------|
| Net debt / (cash)                         | \$m | (26.9) | (39.9) | (58.6) | (82.3) | (111.4) |
| Interest cover (EBIT / net interest)      | x   | n/a    | n/a    | n/a    | n/a    | n/a     |
| Gearing (net debt / EBITDA)               | x   | n/a    | n/a    | n/a    | n/a    | n/a     |
| Leverage (net debt / (net debt + equity)) | x   | n/a    | n/a    | n/a    | n/a    | n/a     |

#### DUPONT ANALYSIS

|                    | FY16A | FY17A | FY18F | FY19F | FY20F |      |
|--------------------|-------|-------|-------|-------|-------|------|
| Net Profit Margin  | %     | 0.4   | 0.0   | 9.3   | 17.5  | 21.3 |
| Asset Turnover     | x     | 0.2   | 0.5   | 0.5   | 0.5   | 0.4  |
| Return on Assets   | %     | 0.1   | 0.0   | 4.3   | 7.9   | 8.9  |
| Financial Leverage | x     | 1.3   | 2.0   | 1.3   | 1.2   | 1.2  |
| Return on Equity   | %     | 0.1   | 0.0   | 5.4   | 9.8   | 11.0 |

#### GROWTH PROFILE

|                   | FY16A | FY17A  | FY18F   | FY19F     | FY20F |      |
|-------------------|-------|--------|---------|-----------|-------|------|
| Operating revenue | %     | 62.8   | 148.6   | 11.8      | 10.7  | 7.8  |
| EBITDA            | %     | 100.6  | 187.7   | 42.8      | 29.8  | 19.3 |
| EBIT              | %     | n/m    | (168.0) | (1,003.2) | 107.2 | 31.1 |
| Operating NPAT    | %     | (98.9) | (89.8)  | n/m       | 107.2 | 31.1 |
| Normalised EPS    | %     | 35.3   | 208.5   | 35.1      | 47.2  | 20.1 |
| DPS               | %     | n/a    | n/a     | n/a       | n/a   | n/a  |

#### PROFIT AND LOSS (PRO FORMA)

|                                  | FY16A | FY17A | FY18F  | FY19F  | FY20F  |        |
|----------------------------------|-------|-------|--------|--------|--------|--------|
| Total revenue                    | \$m   | 23.3  | 58.0   | 64.8   | 71.7   | 77.3   |
| EBITDA                           | \$m   | 5.0   | 14.5   | 20.7   | 26.9   | 32.1   |
| Depreciation, Amortisation & SBP | \$m   | (3.7) | (15.4) | (12.6) | (10.2) | (10.2) |
| EBIT                             | \$m   | 1.3   | (0.9)  | 8.1    | 16.7   | 21.9   |
| Net interest                     | \$m   | 0.0   | 0.0    | 0.0    | 0.0    | 0.0    |
| Non-operating income             | \$m   | 0.0   | 0.0    | 0.0    | 0.0    | 1.0    |
| Pretax Profit                    | \$m   | (0.8) | (0.9)  | 8.1    | 16.7   | 21.9   |
| Tax expense                      | \$m   | 0.8   | 0.9    | (2.0)  | (4.2)  | (5.5)  |
| Minorities                       | \$m   | 0.0   | 0.0    | 0.0    | 0.0    | 1.0    |
| Operating NPAT                   | \$m   | 0.1   | 0.0    | 6.0    | 12.5   | 16.4   |
| Intangible Add Back              | \$m   | 1.4   | 9.7    | 7.1    | 6.8    | 6.8    |
| Normalised NPAT                  | \$m   | 2.5   | 9.7    | 13.2   | 19.4   | 23.3   |
| Significant items                | \$m   | 0.0   | 0.0    | 0.0    | 0.0    | 1.0    |
| Reported NPAT                    | \$m   | 0.1   | 0.0    | 6.0    | 12.5   | 16.4   |

#### BALANCE SHEET

|                      | FY16A | FY17A | FY18F | FY19F | FY20F |       |
|----------------------|-------|-------|-------|-------|-------|-------|
| Cash                 | \$m   | 26.9  | 39.9  | 58.6  | 82.3  | 111.4 |
| Receivables          | \$m   | 5.2   | 6.4   | 10.4  | 11.5  | 12.4  |
| Inventory            | \$m   | 0.0   | 0.0   | 0.0   | 0.0   | 0.0   |
| Other                | \$m   | 10.4  | 16.2  | 1.0   | 1.0   | 2.0   |
| Current              | \$m   | 42.6  | 62.4  | 70.0  | 94.7  | 125.8 |
| Prop, plant & equip  | \$m   | 2.2   | 2.8   | 5.6   | 6.6   | 7.6   |
| Intangibles          | \$m   | 71.4  | 60.1  | 63.8  | 56.9  | 50.1  |
| Other                | \$m   | 0.0   | 0.0   | 0.0   | 0.0   | 1.0   |
| Non current          | \$m   | 73.6  | 63.0  | 69.4  | 63.5  | 58.7  |
| Total assets         | \$m   | 116.2 | 125.4 | 139.4 | 158.3 | 184.5 |
| Accounts Payable     | \$m   | 8.8   | 23.8  | 26.6  | 29.4  | 31.7  |
| Borrowings           | \$m   | 0.0   | 0.0   | 0.0   | 0.0   | 1.0   |
| Other                | \$m   | 19.2  | 39.7  | 1.5   | 1.5   | 2.5   |
| Total liabilities    | \$m   | 28.0  | 63.4  | 28.0  | 30.9  | 35.2  |
| Shareholder's equity | \$m   | 88.3  | 62.0  | 111.3 | 127.4 | 149.3 |

#### CASH FLOW

|                                     | FY16A | FY17A  | FY18F | FY19F | FY20F |       |
|-------------------------------------|-------|--------|-------|-------|-------|-------|
| EBITDA                              | \$m   | 5.0    | 14.5  | 20.7  | 26.9  | 32.1  |
| Change in provisions                | \$m   | 0.0    | 0.0   | 0.0   | 0.0   | 1.0   |
| Change in working capital           | \$m   | (5.2)  | 3.3   | 1.2   | (1.7) | (1.4) |
| Net interest                        | \$m   | 0.9    | 0.8   | 0.8   | 0.8   | 0.8   |
| Tax paid                            | \$m   | 1.0    | 0.7   | 0.7   | 0.7   | 0.7   |
| Other                               | \$m   | 0.0    | 0.0   | 0.0   | 0.0   | 0.0   |
| Operating cash flow                 | \$m   | 1.7    | 19.3  | 23.4  | 26.6  | 32.1  |
| Capex                               | \$m   | (0.9)  | (2.7) | (3.0) | (3.0) | (3.0) |
| Acquisitions                        | \$m   | (33.9) | (3.8) | (1.6) | 0.0   | 0.0   |
| Disposals                           | \$m   | 0.0    | 0.0   | 0.0   | 0.0   | 0.0   |
| Investing cash flow                 | \$m   | (34.8) | (6.5) | (4.6) | (3.0) | (3.0) |
| Equity                              | \$m   | 55.4   | 0.2   | 0.0   | 0.0   | 0.0   |
| Increase / (decrease) in borrowings | \$m   | 0.0    | 0.0   | 0.0   | 0.0   | 0.0   |
| Dividend/other                      | \$m   | 0.0    | 0.0   | 0.0   | 0.0   | 0.0   |
| Financing cash flow                 | \$m   | 55.4   | 0.2   | 0.0   | 0.0   | 0.0   |
| Free cash flow                      | \$m   | 0.9    | 16.6  | 20.4  | 23.6  | 29.1  |

Source: Petra Capital

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