

8 June 2018

EML Payments Limited (EML)

BUY

Share Price: \$1.27

Crossing the Rubicon

Target Price: A\$1.91

EML has announced that its program with Caesars Entertainment has been launched. This is the first step in what may be a very significant contract for EML in time. Should the product evolve into Phase 2 it provides EML with access to Caesars 45m Total Rewards customers and a significant GDV pool. Timing around this product evolution remains uncertain, however, we view yesterday's announcement as an important first step in the process. We have made no changes to our forecasts and reiterate our Buy recommendation.

Caesars program launched

- EML announced yesterday that it has launched its payment card product with Caesars.
- The product allows Caesars Total Rewards members link payment sources (credit/debit cards) to their Total Rewards Payment Card, which allows them to earn up to 2x rewards credits on all purchases made with the payments cards.
- Given the innovative nature of the product and the early stage of its roll out, EML did not provide an estimate of potential GDV for this product.
- The conversion rate is expected to be in-line with other reloadable products in the US (~100bps).

Phase 2 may be a rewards redemption card

- Caesars Total Rewards customers convert reward credits into ~A\$1.3bn of vouchers each year, which are redeemed through paper vouchers.
- Should this process be migrated onto an EML card, we see significant upside to our forecasts
- Total potential EBITDA, assuming complete rollout and 100% penetration, is A\$12.0-14.0m.
- The success of this contract will depend on how quickly the rollout is completed and to what extent the card disrupts the current voucher based offering.
- The timing of this second phase of products evolution is unknown at this stage and given the length of time to launch Phase 1 we have not included it in our valuation. For further details, see our note *Vene, vidi, vici*, published in October 2016.

High conviction Buy

- We have made no changes to our forecasts or valuation and reiterate our Buy recommendation.
- 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.

Company Data

Shares – ordinary (M)	247.5
Dilution (M)	0.0
Total (fully diluted) (M)	247.5
Market capitalisation (\$M)	314.3
12 month low/high (\$)	1.05/ 2.26
Average monthly turnover (\$M)	19.3
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	32.5	24.1	16.4	13.6
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	18.8	15.3	13.2	10.7
Enterprise Value (\$M)	249.2	274.5	255.7	232.1	202.9
EV / EBITDA (x)	49.5	18.9	12.3	8.6	6.3
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



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Analysis

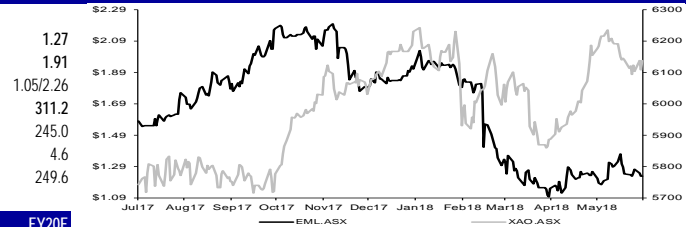
EML Payments Limited

Year end 30 June

MARKET DATA

Recommendation	
Price	\$ 1.27
Target price (12-month)	\$ 1.91
52 week low / high	\$ 1.05/2.26
Market capitalisation	\$m 311.2
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 100.4	32.5	24.1	16.4	13.6
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 285.9	18.8	15.3	13.2	10.7
FCF yield	% 0.3	5.3	6.5	7.6	9.3
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 271.3	271.3	252.5	228.9	199.8
EV/EBITDA	x 53.8	18.7	12.2	8.5	6.2
EV/EBIT	x 206.5	(303.8)	31.3	13.7	9.1
Price to book (NAV)	x 2.8	5.0	2.8	2.5	2.1
Price to NTA	x 5.5	4.8	4.1	3.1	2.3

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

Caesars launch EML product

Having announced in October 2016 that it had signed a contract with Caesars Entertainment Group to provide a payments card to its customers as part of the group's Total Rewards program, EML announced yesterday that the program has launched. We view this announcement as the first phase of what may be a significant program for EML.

Phase 1 – Total Rewards Payment Card

EML's product is a payments card that allows Caesars' Total Rewards program members (45m people) to earn reward credits while making purchases at participating Las Vegas merchants. Historically points are earned through spend on gaming and within the Caesars resorts (eg hotel rooms). This is facilitated by members downloading the "play by TR" app and linking their payment methods (credit/debit cards) to the Total Rewards Payment Card (Figure 1). Customers who like specific Total Rewards funding sources may receive 2x rewards credits on all purchases made with the payments card.

Figure 1: Total Rewards Payment Card and "play by TR" app



Source: trpayments.com

Impact to EML of Phase 1

As this product is a new offering, it is extremely difficult to estimate the potential GDV that EML may generate through this program. We expect that the conversion rate will be in-line with similar products that EML offers, implying ~100bps. As a result, we have made no changes to our forecasts or valuation.

The next phase of this program may provide substantial upside to EML

The Caesars program has the potential to provide substantial upside to EML as the product evolves from a payment card, generating points, into a product allowing points redemption. As outlined in our note *Veni, vidi, vici*, published on October 5 2016, should the program develop into a points redemption product it may result in substantial upgrades to EML.

However, as it has taken over 18 months to go from contract announcement to launch, we suggest that investors take a conservative view in relation to this potential upside.

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