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Kambi Group Plc (KAMBI.SE)

Q2 2014 Earnings Call

CORPORATE PARTICIPANTS

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Kambi Q2 Report 2014. Today, I'm pleased to present Kristian Nylén, CEO; and David Kenyon, CFO. For the first part of this call, all participants will be in listen-only mode and afterwards there'll be a question-and-answer session.

Speakers, please begin.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

Good morning and welcome to Kambi's second results presentation. Turning to slide 2, you can see the outline of our presentation. I will start with highlights of the quarter and discuss our trading during Q2. David will give the financial updates and then I will cover the World Cup, the events of the second quarter; our product development, and the market. After the conclusion of our presentation, we will open up for questions.

Let me start by giving a brief introduction of Kambia on slide 3. Kambi is a premium turnkey sports betting service, offering multiple channels such as Web, mobile and retail. Our service is managed from in-house developed platform that has been continuously developed during the last decade. The platform, together with our highly skilled staff, forms the foundation of our service.

Our business model is scalable and we don't ambition any significant extra costs for acquiring new customers. We currently offer our fixed cost service to 11 customers amongst of them are outperforming the market. Our quarterly highlights are shown on slide 4.

The second quarter showed continued growth. Our revenue is increasing by 97% compared to last year. Year-to-date's revenues are up by 84%. As you all know, revenues were posted World Cup and I will cover that further later on.

During the second quarter, Kambi signed contracts with two new operators. 32Red, a UK-focused operator with the main focus on the casino verticals, they chose Kambi to upgrade its product and we now hopefully also gain market share in the sports betting.

Georgian-based operator, Iveribet is part of a larger conglomerate. It's entering into the online gaming industry with good marketing capabilities and strong potential for future. Both of these companies went live just before World Cup.

NagaWorld, the casino resort in Phnom Penh that we started during Q1, was launched in April, with Kambi taking its first bet on OTC terminals. I will come back to this product development later on.

Another positive note is that Kambi was accepted as a member of the European Lotteries Association in June. This will have a positive impact on our chances to acquire customers in the lottery segment. The World Cup was, of course, the highlight of the quarter. We saw new records in operator turnover and transactions during the event.

What I'm especially pleased with from the World Cup was how well our system copes with a massive load. This is the ultimate stress test but the traffic is up significantly and is centered around a few matches per day.

I am very proud to say that we did not have any downtime during the tournament. I'm also very pleased with our fantastic offering during the tournament, and I will come back to that later in the presentation. I firmly believe that we gave our customers an excellent opportunity to gain market share.

An analysis of our trading activities is shown on slide 5. Since the operator turnover can be considered commercially sensitive, we have decided to create an index to illustrate the growth. The first quarter of 2014 is indexed 100. As we can see in the graph, turnover has grown by 65% year-on-year. Of course, the World Cup had a significant impact on this figure. 18% of the total turnover for the quarter was generated from events.

New customers that were not operating with Kambi last year also have quite an impact. 888, for instance, went live in late May 2013. But most importantly, our current customer base is showing very strong growth in the sports betting vertical. The betting margin for the quarter was 7.3%, which is slightly below the average for the last 18 months.

However, as we can see, it's higher margin than a year ago, and therefore impact their revenues positively in comparison to last year. The World Cup had an even larger effect on results than it had on the turnover because of a higher betting margin. There were enough good results in the matches and a larger proportion of a turnover than in general was generated from pre-match.

The World Cup started really badly, I must admit, and we were a bit nervous for a while about presumably our first quarter report. The most popular teams were winning. Very many goals were scored often later on which is especially [ph] bad with (06:20) live betting. And on top of that, it was the stars such as Messi [indiscernible] (06:25) scoring the goals. Sounds good to any soccer fan but not to a bookmaker.

The turning point was the first match in the second round, Brazil [ph] drawing (06:36) Mexico, and after that the surprising results started to happen more frequently. Two teams we are especially grateful to are Algeria, who surprised in a positive way, and Spain, who surprised in a not so positive way.

I will now hand over to David for more bit details of results.

David Richard Kenyon

Chief Financial Officer, Kambi Group Plc

Thank you, Kristian. Good morning, everyone. First, I'm going to talk you through our headline results on slide 6. Then I will take you behind those numbers and show you the impact of a period of strong operational performance.

Revenue for Q2 2014 was €9.5 million, up 97% from last year. This brings the revenue for the first half of the year to €17.2 million, up 84%. For the first time, we showed an operating profit in the quarter of €0.8 million. This compares to an operating loss of €3.5 million in Q2 2013. Both of these figures were impacted by exceptional items, namely the listings this year and the write-off in 2013 of certain intangible assets.

Excluding these items, the operating results was €1.4 million in Q2 2014 compared to minus €2 million last year, and €1.3 million for the first half compared to minus €4.2 million.

I would like to note that we're choosing to focus in this and future reports on our operating results rather than EBITDA. As a technology-based business, we capitalize significant developments expenditure on the balance sheet, and we take the amortization over three years. These charges make operating results for EBIT a more meaningful financial measure for our business although you will find out EBITDA disclosed in the Quarterly Report.

EBITDA was €2.4 million for Q2 2014, compared to minus €0.3 million last year, and €3.9 million for the first half year, compared to minus €1.1 million. Our cash flow from operating and investing activities, excluding movement in working capital, was €1 million for Q2 2014, compared to minus €1.9 million last year. The same measure for the first half is €1 million, compared to minus €4.4 million.

I will talk you through the Q2 cash flow later as there have been some significant changes to our balance sheet during the quarter, which I'd like to explain. So let's now look at the income statements in some more detail, turning to slide 7. This slide sets out the main components of our income statement. Revenue for the quarter was €9.5 million, up from €4.8 million last year for the reasons previously given by Kristian. Operating expenses increased to €8.1 million in Q2 from €6.8 million. The increase in cost is principally driven by an increase in head count, as we continue to expand the range of our offering and improve the products from a technical perspective. As you see, there is a figure of €0.6 million related to the cost of listing the company. In addition, we have offset €0.2 million against share premium on the balance sheet and these costs relating to the issue of equity during the quarter. There's €0.8 million in total representing five transaction costs for Kambi, but they will not be additional costs in future quarters.

In summary, an operating profit for the first half reflects our strong operational performance in the quarter and the growing strength of our customer base.

So let's move on to the cash flow on slide 8. [indiscernible] (10:33) slide for the major components which impacted our cash position during the quarter. Our opening cash balance was €2.1 million. The operating cash outflow in the quarter was €3.5 million. This may be lower than one might expect. The main reason is a [indiscernible] (10:50) now impact the trade debt to balance as opposed to [indiscernible] (10:55) financing figures. This classification change took place upon the separation of the groups. Furthermore, each period end is likely to reflect two months of invoices from those operators due to the timing of the issue of our invoices at the end of each month.

Capital expenditure in the quarter was €1.4 million, which is principally related to the capitalized development costs on our system automation, front end, and retail projects. Three items formed the prelisting refinancing. First of all, there was a new issuer of equity whereby both Unibet and the existing employee shareholders purchased new shares in the company.

I'm pleased to report that there was a 97% take-up of this rights issue by the employee shareholders. Overall, the equity issue raised €23.8 million. Using these funds, Kambi repaid its outstanding loans to Unibet which were €9.7

million at the end of Q1. And finally, Unibet issued a convertible loan to Kambi for €7.5 million. As a result of these transactions, our closing cash balance was €18.5 million which we believe puts our balance sheet in a very strong position.

So let me summarize on slide 9. A strong operational performance helped by Football World Cup, earnings growth as our existing customers succeed and we take on new operators, and a robust balance sheet which gives us a solid base for the future.

So now let me pass you back to Kristian.

Kristian Nylén

Chief Executive Officer, Kambi Group Plc

Thank you, David. Let me talk about the World Cup a little bit more on slide 10. As I mentioned earlier, I'm very proud about our World Cup offering, and I want to take the opportunity to show you a few things that made our operators stand out during the World Cup. Firstly, we had a betting offer in place on which team would get the next [indiscernible] (13:01).

I believe we were the unique offer in these markets. It may seem strange but this offer generate an important part of live betting turnover. The second example is when a penalty was given. Most of our operators sustain in-play betting while our customers could still offer market on the outcome of a penalty. This is the kind of detail that makes successful operators able to retain their customers and acquire new ones.

I'll talk a bit about what we're expecting during the third quarter turning to slide 11. The sports calendar is generally not that exciting year-on-year like in August. And that, of course, has a negative impact on the betting activities.

However, this year the World Cup continues to be a strong revenue driver also in July with the last 10 matches played. Traffic picks up again in the mid to late August with a major European Football League starting. And events such as the World Championships in basketball will also boost the betting activity slightly.

As 888 stated yesterday, their sports betting will soon be launched in Spain. The impact of these remains to be seen of course, but 888 are one of the leading brands for both casino and poker in Spain.

Details of our most recent product development are shown on slide 12. Our development process is generally a continuous improvement of existing products and back office tools. However, we do also launch new and exciting things.

This quarter we launched our first version of an over-the-counter terminal. The OTC terminal allows shop clerks to place bets for players and administrate [indiscernible] (15:20). The product is operational with NagaWorld shown in the picture and Iveriabet.

The addition of the OTC terminals strengthens our position as the leading multichannel supplier, the potential prospect [indiscernible] (15:41) such as lotteries and land-based gaming groups.

On slide 13, we would like to show you how our core market, European online sports betting, is expecting to develop. As you can see, the expected growth for 2014 is around 20%. Most of our customers are expected to outperform that figure handsomely. The five-year average growth is expected to be around 10% with a lower growth in the odd years and a higher growth in the even years. The reason is, of course, the major football championships are head in the even years. Kambi's short-term study is to continue to grow in its home market,

Europe. But as you can see with NagaWorld, we may take on customers outside Europe on an opportunistic basis.

Turning to page 14. Re-regulation in Europe is continuing and this year the UK will be re-regulated. The Netherlands is expected to follow by mid-2015 at the earliest. In the UK, betting [indiscernible] (17:11) will be collected from December and will have a negative impact on any commission from UK-based payers.

We don't foresee any major impact in IT complexity. Unfortunately, we do not see any positive impact from re-regulation in the UK, but they already have an open gaming market. In the Netherlands, however, we expect the same type of development of the [indiscernible] (17:42) Spain where we have been successful acquiring new entrants to the market. All in all, we have currently new known information. We expect the Dutch regulation to be positive for Kambi.

To sum it up on slide 15, Kambi had seen a record a quarter, our first as a listed company. The strong revenue was boosted by the World Cup and also driven by a very strong performance from our customers. Two new customers were signed during the quarter, and 3 out of our 11 customers went live.

We are confident that we have positioned ourselves well as a premium supplier of sports betting services. We have a top class product offering and very successful customers as references.

David and I would like to thank you for your interest in Kambi. And now we open up for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] There no one in the queue. [Operator Instructions] I have a question for Mr. [indiscernible] (19:23) Please go ahead.

Q

Yes. Hello, Kristian and David. How are you today?

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

Q

Very good. Thank you.

Q

Can you hear me? Okay. Good. So my question is – you're supposed to provide the answer – how do you view your possibilities to sign up government sort of state on the operators? Is that something that will be aided by your enter into the European Lotteries Association? And how about W, the World Lottery Association?

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

A

Thank you very much. I think if we start in the end of the question, the World Lottery Association, they haven't had a board meeting since we became separate entity. So we believe we have a good chance to become a member there as well. But that remains to be seen.

In general, I would say that we are very positive to signing up state lotteries in the future. However, this is usually a very, very long process and there is – yeah, it will take time. There is not that many out there and I can't tell you the timing of it. But as I said before, this is one of our absolute core focus, and I'm confident that we will find somebody else in the future.

Q

Okay. And the two newly signed operators, when will they – when do you think you will go live with them?

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

A

They are live. They went live just before World Cup.

Q

So there are no further customers that you have signed and not going live with? Everyone is live?

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

A

Exactly. I think in that World Cup was such a compelling event. I think everybody we are talking to on the spring, for them it was more or less a requirement to go live before World Cup. What will go live for sure during the autumn then is, of course, 888 in Spain, which you can see almost like in new customers, of course.

Q

Okay, okay. Well, thank you. That was all the questions I had.

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

A

Thank you.

Operator: [Operator Instructions] There are no further questions registered on the telephone. I hand over to you, speakers.

Kristian Nylén
Chief Executive Officer, Kambi Group Plc

Okay. Then thank you for your questions and for listening in. We look forward to updating you on the 29th of October when we release our third quarter report.

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