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Raketech Group Holding plc (RAKE.SE)

Q3 2018 Earnings Call

CORPORATE PARTICIPANTS

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

Andreas Kovacs

Chief Financial Officer, Raketech Group Holding plc

OTHER PARTICIPANTS

Sharish Aziz

Analyst, Danske Bank A/S (Sweden)

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Raketech Q3 Report. Today, I'm pleased to present CEO, Michael Holmberg. For the first part of the call, all participants will be in listen-only mode. And afterwards, there'll be a question-and-answer session. Mr. Holmberg, please begin.

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

Thank you, operator. Good morning, everyone, and welcome to this audiocast where we will be presenting the Raketech Q3 2018 report. My name is Michael Holmberg and I'm the CEO of Raketech. With me today is CFO Andreas Kovacs, and we look forward to taking you through the presentation.

Next slide, please. Today, we have the following chapters on the agenda. I will be giving you the key highlights during Q3. I will talk about who we are and what we do. Andreas will be giving you the financials for the quarter. Then I will go over to a market outlook followed by key takeaways from where we are, and then finalizing with a Q&A session.

Next slide, please. The quarter highlights. It was a very strong quarter with overall solid growth on our main KPIs, €7 million in revenue. Here, I'm particularly proud about our quarter-on-quarter growth of 16.4% when Q2 was a strong quarter in itself where an extra push also came from the World Cup. Looking at year-on-year growth of 42.3% and 28.6% organic, that cannot be classified as anything else than a smashing growth in light of that Q3 2017 was our strongest quarter to-date at that time where we also had very strong growth from Q2 to Q3 in 2017.

EBITDA is close to 46.5% higher than the same quarter last year. And also here, we record a substantial quarter-on-quarter increase, delivering €4.5 million. The EBITDA margin was 58.7%.

Looking at the new depositing customers, NDCs, Raketech's view is that it is a KPI we are measuring, one of many, but it's not always the most important one. I do, however, note that close to 27 (sic) [27,000] (00:02:30) NDCs during the quarter is an all-time high for us, and it's a quarterly increase of more than 30%.

Next slide, please. So, let's spend a minute on going over our business model, what is it that Raketech does? We match the players' needs with the right gaming company. Consumers interested in sports and gaming come to one of our products via search, in many cases via Google, or by finding our products in social media or in the App Store or Google Play. And they download our app. You want to see what the latest game releases are, the latest gambling news, what the current campaigns are, what offers is out there, where you find the highest odds on the match or which TV channel that shows the game. And we offer products where you find all of these, and Raketech is a market leader in our field.

This is a service just like PriceRunner for a consumer that wants to buy a new pair of headphones or a coffee machine or a service like Booking.com if you're looking for a hotel room or renting a car. So, we offer high-ranking quality products like Casinoguide.se, Casinobonusar.nu, Odds.dk, Betting.se, BetXpert.com or TVmatchen.nu and many, many more. And when the player finds what he is looking for at one of our sites, he clicks on to the gaming company where he or she will be able to play casino or place a bet on sports. Once that happens we get paid, that means a new depositing customer. So, we are the link between the players and the gaming operator. And on the other side of the value chain, you have the game suppliers who in turn provide the games or platforms to the operators.

How we do business is all performance-driven. Compare that to traditional marketing where you pay a fee for a radio spot, a TV commercial or printed ad, you cannot track that in the same way as online marketing. This is the beauty of where we are. So, the operators pay for what they get and they get back to us, meaning that we do this well. We deliver players with high lifetime value because the operators can calculate in detail how much revenue each player delivers and where that player came from. And if the player came from Raketech, they will want to continue working with us which we have seen since the company was founded, which takes us to the next slide. So, the next slide, please.

We're a leading affiliate company with revenue primarily from the Nordic markets today. But we have also established ourselves in the UK, Germany, and Spain. We are exploring new markets and we're launching global products. We focus on 20 [ph] top test (00:05:02) products today and we work with basically all the gaming operators in the markets where we're active. With 21 acquisitions over the years, we are M&A-driven and we have over 60% of our traffic coming from mobile devices. The next slide, please.

How do we grow, what's our strategy? It's three pillars. It's core, lab and M&A, in that order. Core is what by far most of our business is, both in company focus and revenue. We have a diversified product strategy with four types of products, SEO search, communities, guides, and social media. An example of an old search product which now performs at an all-time high level is the Finnish sports and casino guide TurtleBet.com. And I want to stress that in Q3 a lot of our focus has been on optimizing on our current assets in core which is the explanation for delivering quarter-on-quarter organic growth of close to 29%.

Looking at the lab, this is where product innovation comes from. We are an innovative tech company that takes being entrepreneurs seriously and that means that you can expect us to always deliver new products. This can be in terms of technology, in terms of partnerships, in terms of finding the next big thing in our area of business. This is a strong commitment we have internally to never stop being curious people and innovating and it's also defined in the very foundation of the company, in our values where one is being open-minded and another one is being hungry.

The other values are teamwork, focused, and taking ownership, all underlining where we are coming from. A great example of a product recently launched from the lab is the Esportsguide which I will talk more about in a minute.

And then finally, the third pillar, M&A, has historically been playing a key part in our growth story and in our Q2 presentation I discussed more in detail how we work with M&A. We've done 21 acquisitions over the years and the recent example from H1 this year is Casinofeber.se, a leading Swedish casino guide for anyone interested in online casino. So this is how we grow. It's clearly defined in our company strategy and in our business plan and it works very well.

Can I have the next slide, please? So, lab, core and M&A, let's go a step further into what it means in reality. Let's look at the Esportsguide.com case study, our most recent launch from the Lab from last week. So, the platform we use is TVMatchen.nu, a product that was launched back in 2004. Raketech acquired it in Q1 last year. It's Sweden's largest TV sports guide.

The team, in-house team, product team, development team, content team, design studio team, and the sales team, they're working together on this product. The innovation, it's an in-house product idea. Many of our employees have a huge passion for esports and that is where this product is coming from.

So, what is the market for this product? So, esports is a global market. Today over 200 million fans of gamers, it's forecasted to go over 300 million by 2022. It's a booming market. And how does it make sense for Raketech? Well, many of our partners, the betting companies, offer betting on esports.

And why we're launching it now? Well, we have the resources. We have the competencies in esports. We have the tech know-how, the sales contacts and we see a gap in the market. There is no such product out there today.

What's our ambition then with the product? It's to build the user base to get the attention from the gamers community. We launch mainly via social media. This will potentially be a second screen product for the global gaming audience who are then playing their video games and then following others on Twitch, which is a [ph] fee that is (00:09:15) then implemented into this product.

So, when do we monetize on the products, I might ask. Well, I say now we're focused on the products. That's our goal right now, to build the best product in this field. We're building long-term. If we do that well, revenue will come. But we will continue to launch new products in the lab, and the Esportsguide is a very good example of how that works in reality for Raketech. Next slide, please. Which is the financial block, so I'll hand over to you now, Andreas.

Andreas Kovacs

Chief Financial Officer, Raketech Group Holding plc

Thank you very much, Michael. So please go to the slide number 10 here. If we look into the historical revenue development, there we can see really strong development during the last two years. We have a compound average growth rate of 49.4%, and we can also see a really strong increase between Q2 and Q3 of 16.4% and we are especially proud as we grew actually with 23% between Q1 and Q2 which is a significant growth and we will continue on this pattern. Please also note that there has not been an acquisition completed during Q3 which makes this KPI even stronger.

Please go to the next slide. If you look at our revenue split, there we could see first of all that we have a really strong evolution from our casino segment. We've seen great potential here. We can see that out of total revenue, 81.6% relate to the casino segment in Q3. We have seen a slightly slowdown in our sports segment driven mainly by that we have the World Cup in Q2 which has been slowing down now.

And also we can see in the other vertical which mainly relates to our financial vertical that we internally have seen great improvements and we see really a big potential and [ph] we'll be – well, we'll (00:11:29) see how we can scale this up.

If we look at the overall year-on-year revenue growth, we can note a revenue growth of 42.3%. Out of this, 28.6% was organic growth. And if you break down our revenues – revenue growth during the different streams, we can see that we have a bigger portion of rev share compared to Q2 and we have also a bigger portion of CPA compared to Q2.

We have around 44% both on rev share and CPA, which is taken partly from the flat fee evolution. That has been explained by the World Cup during Q2 where the operators has been really eager to expose even more. So, this is something that we expected.

If we look at the next slide and we look at the EBITDA evolution, there we could see a strong EBITDA development. We could see an EBITDA margin growth by 5% between Q2 and Q3. This is explained if we try to break our [ph] costs driven down (00:12:53). There we could see that increased direct costs has been – the direct cost has been increasing by 2.6% compared to revenue, and this is in line with our strategy where we really want to build the scale of our business model where we can rely more on external assets, not only on internal employees. And there we really see it as a winning concept going forward.

If you look at the employees and personnel costs, there we could see a decrease of 5.3% compared to our revenue, and that is – goes also hand in hand with the increase of direct cost. We see that to gain efficiency and that to continue on our strategy we're able to operate this business more with the external assets and not only internal.

If you look at the other operating expenses which has decreased with 2.4% compared to revenue, that is explained mainly by the lower consultancy cost post-IPO but also some kind of seasonality effect. We can see a slightly lower activity from our suppliers, mostly during the summer months, July and August.

Just to also point it out, I think here at the EBITDA margin improvement, you can also see which scalable model we have. I mean, we have a really strong revenue involvement, and there we can show that we have actually on the same FX cost base where we can gain higher margins with strong revenue growth.

If you go to the next slide, please, and we look into the statement of financial position. There, we can see that our total asset base amount to €92 million, of which the absolute majority relate to fixed assets of €66.4 million. These assets mainly comprise intangible assets in form of website domains and player databases. During Q3, we have renegotiated the earn-out with one of the latest acquisition related to Casinofeber leading to an increased recognized value of these assets and the main driver just to understand related to a prolonged earn-out period. This has also led to an increased portion of assets which will be amortized going forward, so you can expect slightly increased amortizations going forward.

Goodwill, that relates to the acquisition of Shogun which we completed in Q2. This is a long-term strategic investment which we until now had a limited revenue effect. Cash and cash equivalents related to €20.5 million at end of Q3. Equity amounted to €57 million as of 30th of September. And if you look further down in our balance sheet then you can see that amounts committed related to earn-out payments amounts to €9.8 million as of the end of September.

Borrowings which relate to our credit facility towards Ares Management amounted to €21.9 million as at last of September 2018. And that relates our current credit facility of a total credit line of €70 million. We made an earlier payment during the quarter to these creditors of €15 million in July which also resulted in non-cash effect affecting our finance cost of €0.7 million as we unwind the capitalized transaction cost earlier than expected.

As of 3rd of October, we made another early payment repayment of additional €15.5 million and you can expect the similar effects related to our finance expenses without any cash effects during Q4. Other payables relate mainly to our short-term payables.

If we can take the next slide, so if we look into our cash flow then we can see that our cash conversion EBITDA against net cash flow amounted to 0.6 times EBITDA. However, I want to highlight that out of this, we had also the annual tax payment related to historical profits of €0.8 million. And of this, we have actually received during Q4 as a refund €0.7 million. So, this is more or less timing effect that hits our cash flow during Q3. With that said, if we adjust for this then our [ph] cost of cash (00:17:58) conversion during Q3 results in 0.74 times EBITDA.

If we look in the cash flow bridge and we go to the elements, there we could see a net cash from operations excluded from this tax payment amounting to €3.1 million. You could see earn-out play payments and payments to acquisitions of €5 million during the quarter. And then you can also see the €36.3 million of received funds in relation to the IPO. These are the funds that was received actually in the first days of Q3 as we went public during the last days of Q2.

And then we have the repayments on borrowings of €15.5 million during the quarter which was explained before. The paid interest of €1.8 million relates to longer period only this quarter and as we have prolonged credit terms related to our interest expenses. And then we come to the total cash and cash equivalents of €20.5 million at the end of the quarter.

So, please go to next slide and I will leave it to Michael once again.

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

Thank you, Andreas. So, let's take the market outlook. What are the key trends if we flip to slide number 16, please. So it's key to understand the player behavior and catch new search trends early. What news are coming to the market? This can be new products, can be new technology or new payment methods like Pay N Play. It can be new gaming companies. In order to be a market leader also in the future, we need to be on our toes and we are that by working with the best people on the market, our employees and our partners are key and we also do it by investing in BI and data analysis.

This is an area where we have spent a lot of time and effort over the past couple of years to build the platform and the intelligence to be a powerhouse also in the future. So, what the players are asking for is what we deliver on. This is also exactly what Google prioritizes, produce quality content, that's the Google [ph] advice (00:20:20) since some 10 years back and it is really only advice that you need that counts for all our products. This is what we do since it makes sense for the end user.

Let's discuss a bit about consolidation. We foresee consolidation on the market, driven by regulation and compliance. However, what has happened over the past six months is that consolidation climate in general has slowed down. We have always been and we are a consolidator of the affiliate industry. We focus on finding the right assets for future growth.

Looking at SEO communities and scalable tech products like our sports TV guides, we haven't acquired in Q3, we only acquire when it makes sense, when the product quality and the price is right. We don't compromise on that and we are very selective, I would say, picky.

We get proposals, companies coming to us to sell on a weekly basis. We are actively approaching companies we are interested in. But we only acquire when it is right for long-term company growth. This is very important, and we feel no stress in this area. We focus a lot on building our current assets and it's paying off. We do this in-house and we do it in partnerships. We're working where we are very strong.

Geography, comment on that. The market trend we see, with regards to geography, is that our partners, the operators, actively request growth for markets where they are investing. This means that the business model of course is highly attractive, that the operators have growth via affiliates high on their agenda. And if you work with a strong partner like Raketech, which sends players with high lifetime value and a clear agenda for compliance, you want to invest in that relation.

So, today we primarily have revenue from the Nordics and the UK, but we have a big domain park for traffic from other regions, too, like most of the regulated European countries, North America, New Zealand. We also get many requests from our partners in the Nordics for traffic from other markets. This is something we are exploring mid to long term. One of Raketech's core strengths is our relation with the gaming operators. And logically, we will expand into regions that are relevant to them, win-win partnership.

Can I have the next slide, please? Focus Sweden, preparing for regulation. What is the update from Q3 and the focus for Q4? Raketech has experienced from the regulated markets, Denmark and the UK the benefits [ph] since (00:23:15) we are in Sweden now. In our view, regulation comes into effect from the 1st of January 2019 and it will be a period of transition for all the players in the market. We have been discussing the commercials for 2019 with all our main partners and then intensify that work in Q3 and we are where we want to be here in Q4.

Some operators have a clear view on 2019, whereas others are adopting their strategy now. I can conclude that there is a big demand for our services also in a regulated Swedish market. It's a big demand from the established operators, from new operators and from some of the companies that have been regulated in Sweden for years already. The market opens up for paid media advertising, a service that we are ready to provide.

Regarding search trends, they will not be changing overnight. We've invested in analyzing this. Regulation allows one bonus [ph] per player (00:24:19) per operator. Search on bonuses will still be high in 2019. Trends are also that the players want the best product, the best user experience. I feel we are heavily focusing on by data analysis of player behavior. With the new products also comes new opportunities. One example is In-Banner Pay N Play where we recently entered a partnership with player provider Trustly as the first affiliate company.

So I feel confident that we will continue to run a successful business in Sweden post-regulation given our market-leading position, tight relation with the operators and product innovation. To-date, almost 200 gaming brands have applied for a Swedish license. So it's exciting times ahead for the Swedish market.

The next slide, please. Sustainability update, we continue with high focus on sustainability as we also see this as a key market driver into regulations. During the quarter, we have become a member of SPER, Spelbranschens Riksorganisation is a first affiliate company and we have implemented a policy in line with the directives from Lotteriinspektionen and Konsumentverket. This is also an area where we are a forerunner in the industry.

Next slide, please. So, to slide number 20, please. So, to conclude on the quarter, we record strong performance in the quarter with revenue growth of 42%. We had a lot of focus on growth from core lab. This will continue also from here on. We are well-prepared for the Swedish regulation in closing our commercial partnerships for 2019 progress according to plan.

A comment on Q4 performance is that we see continued solid growth in line with our expectations. And at this point, we are on track to deliver on our full-year goals. So now let's move over to questions. Operator, please.

Operator: Thank you. [Operator Instruction] Our first question comes from the line of Sharish Aziz of Danske. Please go ahead, your line is open.

Sharish Aziz

Analyst, Danske Bank A/S (Sweden)

Q

Thank you, operator. I have a question on the geographical distribution of the revenues? You're stating in the report that 96% is coming from the Nordic region. Would you care to give more, a slightly more detailed distribution [ph] for Sweden (00:27:29), Norway, Denmark, please?

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

A

Yes. Hello, Sharish, and that is correct and what we can comment on is that we were performing well in the Swedish market but definitely also, so, in Finland and in Denmark, Norway also progressing according to plan. The geographical split is also in line with the prospectus, so from H1, so there are no dramatical changes from that then. And then, we will continue to be growing into new markets according to our plans.

Sharish Aziz

Analyst, Danske Bank A/S (Sweden)

Q

That helps a lot. Second follow-up question though. What about the U.S. market, any specific plans on entering, on going into New Jersey, for instance, or any other states? What are your views on the American regulation which is evolving?

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

A

Today, we already have traffic from the U.S., we're not capitalizing on it today. We launched the Esportsguide last week, which is a global product that has good potential for the U.S. market where obviously esports is very, very big and booming.

We are looking at when the time is right to start capitalizing on our online assets. We have the competency. We have contacts to move into the U.S. market. So, it's definitely a market that is very interesting for the future.

Sharish Aziz

Analyst, Danske Bank A/S (Sweden)

Q

Thank you. And then just one last question from me. In terms of – I guess any seasonality into Q4 on casino or sports vertical which we should take into consideration? Yeah.

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

A

Thank you, Sharish.

Andreas Kovacs

Chief Financial Officer, Raketech Group Holding plc

A

Yes. I mean, what you have seen and what we also seen is more or less that our casino assets really performing really, really well, and the only guidance we can give is more or less that in line with Q3 we foresee similar trends.

Sharish Aziz

Analyst, Danske Bank A/S (Sweden)

Q

Thank you very much, Andreas. That's helpful. That's all.

Operator: Thank you. [Operator Instructions] As there are no further questions at this time, I'll hand back to our speakers for the closing comments.

Michael Holmberg

Chief Executive Officer, Raketech Group Holding plc

Thank you all for joining the call this morning. It was a pleasure to take you through our Q3 performance, and we look forward to continuing delivering as per our business plan and come back to you with the Q4 report when the time is coming for that. Thank you very much.

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