Nexi – SIA, the newborn Italian champion in the payments industry

Nexi (BIT:NEXI) – market cap as of 30th October 2020: €8.41bn
SIA Group – Private Company

Introduction

On the 5th of October 2020, Nexi SpA and SIA SpA, two Italian financial companies specialising in payment solutions, announced a €15bn all-share merger, creating an Italian PayTech champion. The merged group will have €1.8bn pro-forma aggregated revenue and €1.0bn EBITDA and will be the largest group in Continental Europe in terms of merchant servicing. As a result of the deal, Nexi's shareholders will own 70% of the combined entity, while SIA's investors will hold the remaining 30%, with CDP (development bank controlled by the Italian government) owning the largest stake of 25%. The deal was a result of months long negotiations, which intensified this year after French payments operator Worldline agreed to acquire Ingenico for €7.8bn, becoming the largest payment provider in Europe.

The merger confirms the consolidation trend in the payment services industry and further increases pressure on Europe's payment providers to consolidate in order to accelerate growth and step-up in size as online purchases intensify during the pandemic and consumers move further away from using physical cash.

About Nexi

Nexi SpA is Italy's largest payment-service company, operating in merchant servicing, card payments and digital solutions. Founded in 1939 and then known as ICBPI, Nexi in the present state is the result of a series of acquisitions as well as a rebranding conducted in 2017. Today it can be considered a market leader in certain sectors of the payment industry in Italy.

In December 2015, a majority stake in Nexi (then ICBPI) was bought out by Mercury Italy (a private equity investment vehicle owned by Advent International, Bain Capital and Clessidra SGR). In April 2019, Nexi held an IPO on the Milan stock exchange and raised ~€2.0bn, effectively becoming the largest European IPO of 2019. Prior to the merger announcement, top holders of Nexi were Mercury UK (20.1%) and Intesa Sanpaolo (10.5%), strategic corporate investors, resulting in the free float of 69.4%.

Nexi's main lines of business are: Merchant Services and Solutions, Cards & Digital Payments, and Digital Banking Solutions.

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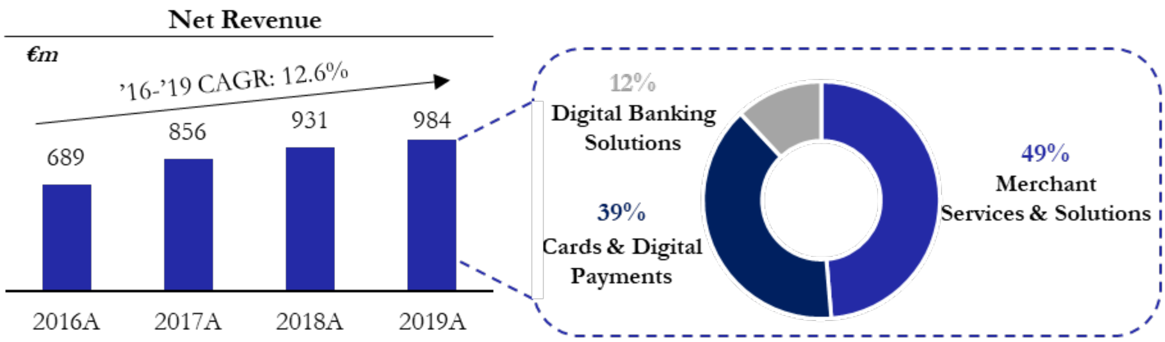
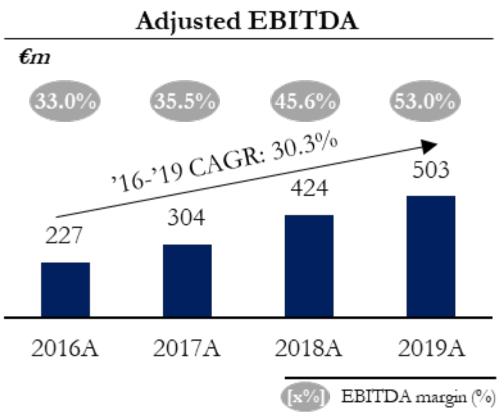
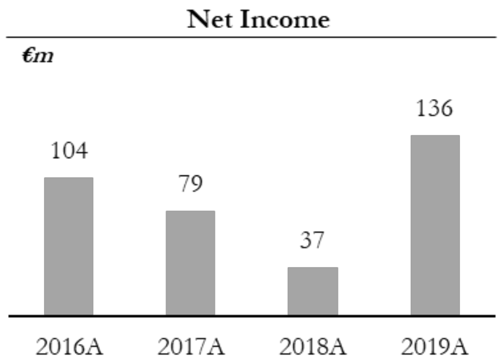
41.6m Payment Cards Managed	**900k** Merchants Served	**~13k** ATMs Served
6.1bn Transactions Processed Annually	**€463bn** Value of Annual Processed Transactions	**469k** Corporate Banking Workstations

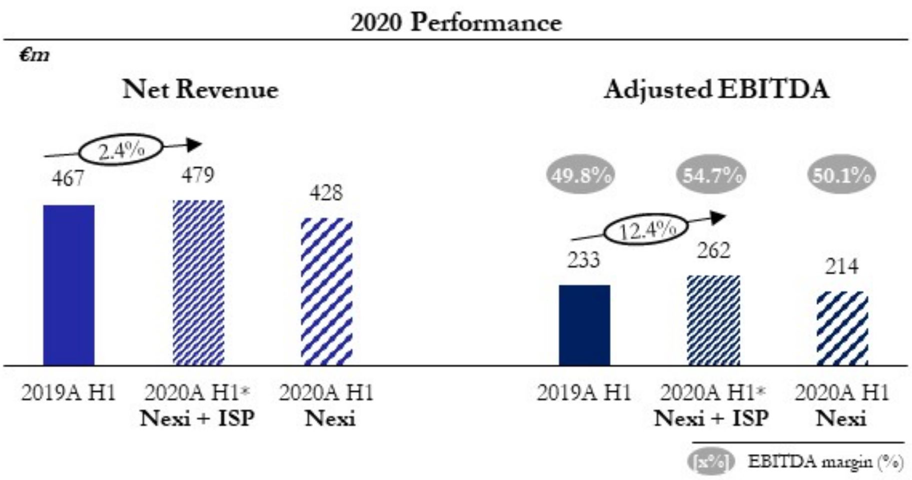
In terms of financial performance, Nexi has demonstrated stable revenue growth and in 2019 outperformed its IPO guidance. Merchant Services & Solutions, the main revenue contributor, remains the fastest growing business line, especially accelerated by e-commerce growth.



At the same time, Nexi has successfully introduced programmes aimed at cost-containment and operational efficiency improvements, resulting in EBITDA growth outpacing revenue growth and a consistently improving EBITDA margin. Improvement of EBITDA profitability in 2019 was also supported by early impacts from implementation of IT strategy and ahead-of-plan realisation of synergies from the integration of acquired businesses.

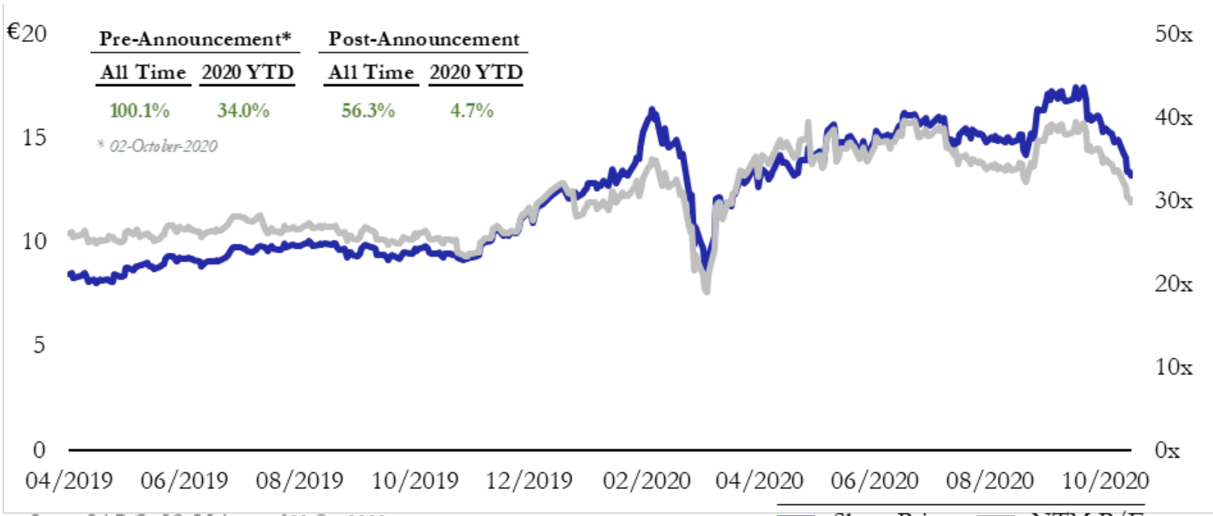






While financial performance in H1 2020 was negatively affected by the COVID-19 pandemic, the successful closing of €1.0bn acquisition of Merchant Acquiring Business of Intesa Sanpaolo (ISP) in June 2020 offset the absolute drop in financial metrics and even improved EBITDA profitability compared to Nexi standalone. Pandemic negative effect on Nexi (standalone) was also partially mitigated by Nexi's nature of business, with revenues falling by only 8.5% and EBITDA by 8.0%.

Nexi has demonstrated strong trading performance since the IPO. Growing share price and strong valuation would justify the all-share merger and allow Nexi to benefit from the deal structure. Even though the market received positively the deal announcement, recently the share price has been negatively affected by the 2nd wave of COVID-19 (FTSE Italia All-Share fell by 8% in 5-28th October period).



Source: S&P CapIQ. Values as of 30-Oct-2020.

About SIA

The SIA Group is the European leader in the design, construction and management of infrastructure and technological services in the card & merchant solutions, digital payment solutions and capital markets & network solution segments. SIA provides services in 50 countries, with activities in Italy representing approximately 68% of the revenues. Founded in 1977, SIA (then Società Interbancaria per l'Automazione) throughout its history played a significant role in the Italian payment systems sector and today remains a core Italian market player.

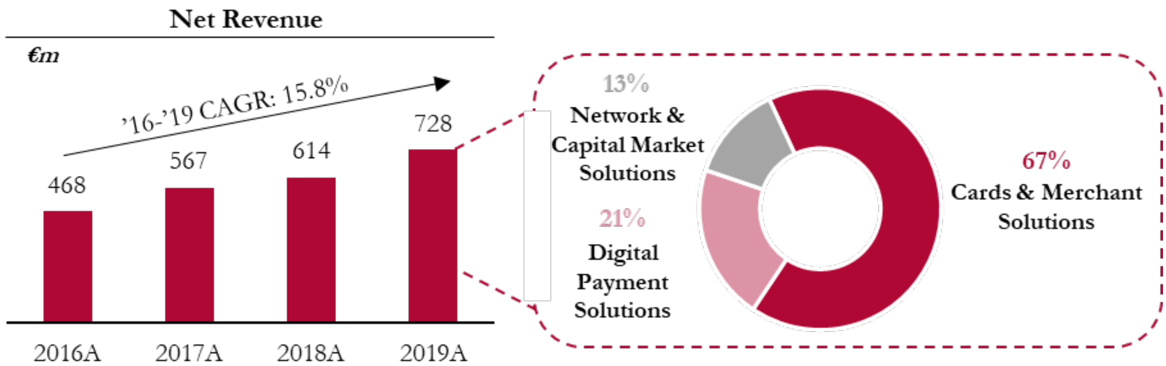
At the beginning of 2020, SIA announced the start of preparations to go public, with expected floating in summer 2020. However, COVID-19 adverse effect on markets might have affected listing intention, increasing SIA's enthusiasm regarding the merger with Nexi.

Prior to the merger, SIA was a private company, majority-owned by an arm of the Italian government represented by FSIA Investment (57.4% stake) and CDP equity (25.7% stake).

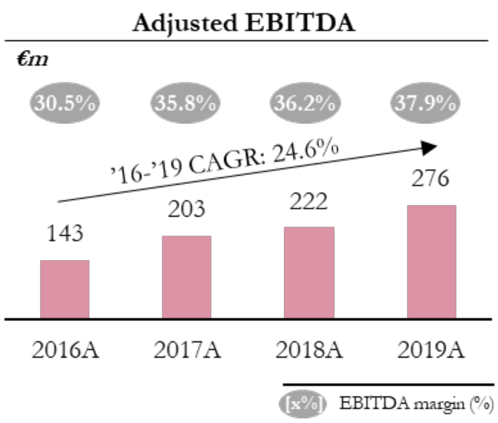
SIA's main lines of business are: Card & Merchant Solutions, Digital Payment Solutions, and Network & Capital Market Solutions.

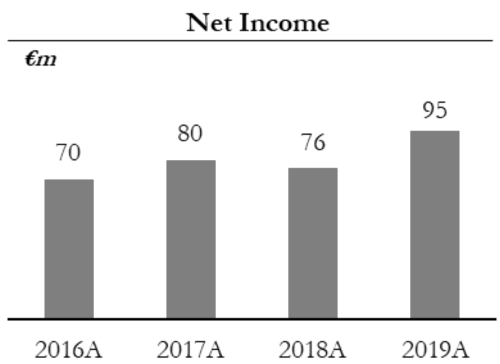
#1	#1	#2
Card Processor in Italy	In cross-border transactions in Europe	Card Processor in EU
84m+	**~16bn**	**~840k**
Payment Card Managed	Payment Card's Transactions Processed Annually	Points of Sale

In terms of its financial performance, SIA has been demonstrating solid revenue growth during the last several years with Cards & Merchant Solutions being the main contributor. Recent gain in revenues was caused by the stable contribution of Italian business, improving performance of businesses acquired in Central and South-Eastern Europe as well as considerable growth in car-based electronic payment transactions and traffic volumes processed through SIA network.



Despite gradually growing operating costs related to the increase in business volumes and implementation of new initiatives, SIA managed to offset costs growth thanks to the growing contribution and performance improvement of international operations.





Industry Analysis

Digital disruption impacting the financial services' industry is not unheard of in 2020. What is still being defined is the new industry structure and its competitive dynamics, which are going to include new players and, as a consequence, new winners, and new losers.

The new imperative of "intelligent digital mesh", that is changing the way people interact and what they expect from their favorite brands, is beginning to affect also the financial industry. The focus is all on the intense customization of the services required by the customer, which is leading to the large spread of personalized insurance programs, financial robot-advisors, social trading platforms, and many more. What the customer is really seeking is the opportunity to utilize interconnected services that are not excessively expensive in terms of commissions to financial intermediaries. This is especially true in two market areas: investment management and payments/money transfers. At the same time, the possibility to easily compare the various financial service providers makes the customer more powerful to choose and the switching costs way lower.

As a consequence, the required digitalization and the need to be ahead of the competitive game are leading to prosperous deal activity in the fintech industry, where the bigger players are acquiring the small ones to access new technology, eliminate competitors and offer to the customers the demanded "interconnected services". Three areas appear more likely to experience this trend: credit capabilities, open data, distribution collaboration, and payments. On top of that, the pandemic made many of the traditional manual processes not possible anymore (like paying with cash or credit cards if not contactless), creating a need for new approaches. Most of the deals of the last months have the rationale of offering a more complete service to customers. This is the reason behind the joint venture of FundingXchange and Experian, or behind the acquisition of RateSetter by Metrobank.

The payments industry is the perfect example of this innovation trend, including the digitalization of the whole value chain across all industries and size of companies, with new standards for e-commerce solutions, B2B payments, mobile payments, card management, and open banking. In addition, the change in the European regulatory environment regarding PayTech companies will create a safe environment to compete for the market disruptors. The new directives are based on two pillars: the definition of better market rules in order to have a clear understanding of which organizations are allowed to provide payment services, and the construction of new regulations about data management in order to define the obligations of users and service providers. The focus on data management and its proper regulation is driving the large international players to improve their capabilities in this area through strategic acquisitions (e.g. Visa's acquisition of Plaid and Mastercard's acquisition of Finicity) but it is also creating new opportunities for smaller players. In fact, the main effects of the Payment Services Directive 2 (PSD2) in the European Economic Area is to allow PayTech companies to operate on a pan-European level also while being based in a smaller country. This radically changed the strategic perspective of the main market players, who are now looking for a leadership position at the European level rather than at the national one, like in the case of UK-based bank Tide partnering with Hokodo to conquer Europe, or Swedish iZettle working together with the British competitor Stuart to expand their services abroad.

According to Invyo, a global supplier of fintech analysis, among the 50 most disruptive European companies in the financial industry, four ventures out of the five ones with highest market capitalization are focused on the payment services: Ayden (Netherlands), Nexi (Italy), Klarna (Sweden), and Transferwise (UK). With these companies setting the new competitive rules, the European payments market is expected to hit a value of $802bn in digital transactions only by the end of this year. However, 50% of retail payment transactions in Europe are still cash-based, showing a large space for growth. Credit cards may appear as the most logic candidate to substitute cash payments, but the fast-growing digital payment industry highlights that customers are more likely to choose digital solutions.

The Italian payments landscape follows the European trends in terms of innovation, but it demonstrates to be particularly underpenetrated by card payments, although the CAGR from 2015 to 2018 stands at 9.7%. The card penetration rate in Italy is only around 26%, which offers the opportunity to attract the people who did not opt for the "credit card world" because of its complexity. For these customers, the digital payments alternative looks easier and less expensive, which will constitute a competitive advantage of the new Paytech ventures as compared to the companies offering cards in the past years. Plus, the last months of Covid-19 accelerated the process by making online payments the prominent solution.

Deal structure

According to the settled memorandum of understanding, the equity transaction will be constituted by the transfer to Sia's shareholder of 1.5761 Nexi's shares for each Sia's share. This will lead to an equity slit of the new resulting enterprise constituted by 30% of equity in the hands of current Sia's shareholder, while 70% of it will be held by current Nexi's shareholder. According to the current market capitalization, the new group will be valued more than €15bn, becoming one of the ten largest companies active on the Italian market in terms of capitalization. The floating capital will constitute around 40% of the total equity value, confirming the strong ambition of the two companies to constitute a source of public value, mainly because the 25% of the new entity will be owned by CDP, a public organization controlled by the Italian Minister of Finance.

The new company will be led by the current board of directors of Nexi with the confirmation of Michaela Castelli as president. At the closing step of the deal, 5 or 6 new board members designed by Cdpe and Fsia will join the board, with three of them being independent, one of them as vice-president and the final one as not independent. At the same time, Cdpe, Fsia and Mercury signed a side agreement which will be legally effective at the moment of the closing and will define the relationship between those three major shareholders. The current CEO of Nexi, Paolo Bertoluzzo will be confirmed CEO of the new company, while the current Sia's CEO, Nicola Cardone, will have a support function until the transaction is concluded, in order to later leave the company to continue his career is another organization.

Deal Rationale

The combination of Nexi and SIA creates a national champion in the attractive Italian payment market, with a 70% market share according to Jefferies' estimates. Indeed, the new group will be the first merchant acquirer and the first card processor in Italy, an economy that is still cash driven, with card payment penetration of only 24%, but with strong and resilient growth.

This deal was long-awaited by market participants, since Nexi and SIA have been in merger talks for a year-and-a-half to resolve governance and valuation differences.

A key sticking point in determining SIA valuation was the accord to keep Italian lender UniCredit as one of its main clients, that will be finalized in the first months of 2021 according to the two companies. SIA was valued at a 2019 EV/EBITDA multiple of 13.6x including run-rate synergies, with a €4.6bn Equity Value implied at Nexi current share price.

The new group will have a deeper value chain coverage, combining SIA focus on the technological platform, including data centres and processing capabilities, with Nexi focus on operations and merchants' solutions.

Significant synergies will derive from the combination. Nexi estimated total recurring cash synergies of about €150m, of which cost synergies of ~€100m, revenue synergies of ~€35m, recurring capex synergies of ~€15m, and additional one-off capex synergies of ~€65m. The acquisition is estimated to be 15-20% Cash EPS Accretive at anticipated full run-rate synergies.

Nexi-SIA will be a leader in Europe, handling payments for roughly 2 million merchants, managing 120 million cards and processing more than 21 billion transactions a year. The new group will generate €1.8bn in revenues, almost double the €984.1m revenues generated by Nexi in 2019, with estimated €1bn EBITDA and €0.8bn Operating Cash Flow. Furthermore, the new Group will combine Nexi dominant position in the Italian market with SIA international presence in more than 50 countries, that will contribute to €0.2bn to group revenues.

The acquisition of SIA is in line with the expansive strategy of Nexi that aims to become the biggest European payments provider. Indeed, the new group will be better positioned to capture multiple growth avenues, both organic and inorganic. For example, being the dominant player in the Italian market, it will particularly benefit from the national agenda towards a cashless society; Nexi-Sia will achieve organic growth also through a broad portfolio of products across all business segments, and through further margin expansion, driven by the evolution of technology platforms and by increased operating leverage. The new entity could grow also inorganically: local M&A opportunities include further acquisition of merchant acquiring business units and of tech companies that may enhance Nexi-SIA's capabilities; internationally the group is a potential actor in pan-European consolidation and it could expand through bolt-on acquisitions in countries where it is already present.

Market Reaction

Nexi shares gained around 3.08% on Borsa Italiana, the Italian Stock Exchange, on the day of the announcement, rising to €17.41. All the analysts at major broker houses expressed a positive opinion on the impact of this deal on Nexi.

Equita SIM appreciated the strategic rationale of the deal, as Nexi will strengthen its competitive position and it will diversify its clients both by type and by geography. Furthermore, according to its analysts, the acquisition will be 11-14% adjusted EPS accretive in 2022-2023. Equita SIM maintained a rating "hold", but it increased its target price from €15 to €16.2.

The highest target price is provided by Jefferies, standing at €20 with a rating "buy", claiming that this acquisition is strategically important for Nexi as it can accelerate pan-European consolidation. Goldman Sachs is also bullish on Nexi with a target price of €19 and a rating "buy", as the combined group could expand internationally and possibly become a consolidator in the European payments market.

Kepler Cheuvreux approves the deal with SIA and it expects greater synergies than the ones initially forecasted. The broker has a rating "buy" and a target price of €18 on Nexi.

Financial Advisors

Bank of America, HSBC and Mediobanca are serving as financial advisors, while Legance – Avvocati Associati as legal counsel to Nexi.

SIA is being advised by J.P. Morgan as the sole financial advisor and is supported by Rothschild & Co on specific activities in the context of the transaction and by Gianni, Origoni, Grippo, Cappelli & Partners as legal counsel.

TAGS: Nexi, Sia, Italy, Payments, Banking, Financial Services