

Feeling lucky? Gambling company Lottomatica to go public at the end of the month

Introduction

On April 13th Lottomatica announced plans to go public via an IPO seeking a valuation of up to €2.67bn. The gambling company, owned by the alternative asset manager Apollo Global Management [NYSE: APO], intends to list its shares on the Borsa Italiana by the end of April at a price per share between €9 and €11. The firm will be selling both existing shares as well as new ones issued in a capital raise of up to €425m. Apollo announced that they expect to cut their stake in the firm down to 75% and intend to use part of the proceeds of up to €600m to repay €250m of debt. This is the underlying rationale behind going public; to improve the company's financial position by reducing leverage and injecting liquidity to fund further expansion and cement their position in the Italian gambling industry. This IPO comes during an all-time low of IPO activity due to macroeconomic uncertainty and interest rate hikes, which saw a tumble of 94% in money raised between 2021 and 2022. Onlooking companies hope that a successful float will pave the way for a long-awaited recovery in equity markets and IPO markets.

About Lottomatica

One of the biggest players in Europe, Lottomatica was the first Italian operator in the legal gambling business to be approved by the Customs and Monopoly Agency. With over 3,000 points of sale in sports betting and over 1,400 in gaming halls, the firm operates the largest spread gambling network in Italy. Lottomatica's business is composed of three main streams: online betting, sports betting, and gaming. In Italy, Lottomatica is the industry leader in the online gaming industry operating under the brands Lottomatica, Better, Goldbet, and Betflag. The extensive and cutting-edge portfolio of online gaming products that Lottomatica offers can be accessed both over the web and through mobile apps for smartphones and tablets. Sports betting is covered by three popular brands Better, GoldBet and Intralot which are all accessible in betting shops and corners. Betting shops are entirely devoted to providing gambling services to customers, whilst corners are in smaller spaces within other stores such as a bar or tobacconist but look to provide the same service and experience. Meanwhile, the term "gaming" refers to a variety of independent machines that are placed in public spaces and rival gaming establishments across the nation. Lottomatica operates two main kinds of gaming machines: Amusement with Prize (AWPs) and Video Lottery Terminals (VLTs). AWPs are connected to the concessionaire's computer network for control purposes and are installed in public establishments such as cafes. Meanwhile, VLTs can be controlled in real time from remote locations and are only installed in dedicated gaming halls which are subject to security as access is denied to minors under 18 years of age.

Lottomatica generates revenue by taking commissions, known as vigorish or vig. The term originates from Yiddish slang and simply means the fee that bookmakers charge for accepting a gambler's wage. A better's advertised odds include the vig, which is also paid as a processing fee for the wager. A typical house edge is also used to generate income from the gaming devices and applications run by Lottomatica. All Lottomatica's products include advertising and partnerships that generate further revenue for the business. In 2022, the firm provided over €22.8bn worth of bets from which they generated just under €1.4bn of revenue, representing revenue growth of over 70% since 2021. This growth in revenue was primarily driven by a 93.3% increase in gaming and a 122.5% increase in sports betting, with a predictably more modest growth of 17.5% growth in online betting. Lottomatica is currently wholly owned by Apollo Global Management, who bought out the company from International Game Technology (IGT) [NYSE: IGT] in May 2021 for €950m.

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Industry overview

According to the European Gaming and Betting Association, the European gambling market amassed gross gaming revenues of €108.5bn in 2022, an 8% increase on pre-pandemic levels and a 23% increase on 2021. This growth has been spurred predominantly by the re-opening of gambling venues following the pandemic, with land-based revenue increasing 34% and accounting for 65% of total gambling revenues. Over the last decade or so, we have seen the emergence and growth in popularity of online gambling, and this is a sector that analysts forecast to see the most growth in. Within online gambling, casino gambling made up 39% of revenue in 2022, closely followed by sports betting. Another trend that we have witnessed is the growing proportion of online bets placed via mobile phone devices over desktops and laptops. In 2019, only 46% of online gaming revenue was attributed to mobile devices, compared to the 51% in 2021 and the forecasted 64% by 2026. The growth in both online gambling and betting on mobile devices in Europe can be attributed to the increasingly digitalized world we live in, where more people have access to mobile devices, internet connectivity and streaming technology. The wider European gambling industry is dominated not by local players, but by multinational operators such as Bet365 and Flutter Entertainment [LON: FLTR] who run brands such as Sky Bet and Sky Vegas. The dominating players have focused on mergers over the past few years to increase their market stake and improve profit margins. For instance, Paddy Power PLC and Betfair PLC merged to form Paddy Power Betfair PLC and Flutter Entertainment merged with The Stars Group to become one of the biggest players worldwide. Many online gambling companies rely on third-party companies, such as Playtech, for backend software solutions for their products. More recently however, we have seen an increasing number of firms deciding to backwards integrate with technology providers. 888poker [LON: 888] have invested heavily in developing its own proprietary software and gaming technology and similarly William Hill acquired Grand Parade, a software development company. Overall, the European gambling industry is still highly fragmented, with new players entering the market

As one of the biggest European gambling markets generating over €20bn in revenue and second only to the United Kingdom, the Italian gambling industry is regulated by the Agenzia delle dogane e dei monopoli (ADM), which is responsible for granting licenses to operators, monitoring compliance with regulations, and collecting taxes on gambling revenue. Lottomatica's competitors comprise of mainly British companies operating in the Italian market. Firms such as Flutter, Entain, Playtech and 888 Holding all have much more international exposure on a global scale than Lottomatica, but Lottomatica still leads the domestic market revenue taking up 19.6% of the market. Sisal, which was bought out by Flutter in 2021 comes in at second place with 9.44% and Snai, an Italian owned and run company, at third with 8.05% of the market.

IPO Rationale

The main rationale behind Lottomatica's IPO is to improve the company's financial position and gain liquidity to fund more acquisitions, consolidating its position in the Italian gambling market even further.

Through the IPO, Lottomatica will issue €425m worth of new shares, which will be mainly used to repay a €250m intercompany loan from Gamma BondCo SARL and pay back in advance some of its senior notes maturing in 2025. The reduction of financial debt, combined with the capital increase, will help lower the financial leverage of the company, reaching a Net Financial Position / EBITDA pro-forma of 2.4x, a significant improvement from the pandemic period.

The company's leverage has been increasing over the years due to several acquisitions financed through debt. The acquisition of Betflag in November 2022 for €310m, with an additional earn-out of €50m to be paid in 2024 based on the financial performance of the newly acquired company, was only the latest in a series of takeovers, aimed at gaining market share in the Italian gambling market. In 2018, the company acquired Goldbet for €273m,

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incorporating another major player in the gambling industry, and over the years it has acquired majority stakes in other companies such as Giocaonline SRL, Ares SRL, Marim SRL, and others, whose businesses span from online gambling to Video Lottery Terminal (VLT) systems.

Following the IPO, Lottomatica will have more liquidity at its disposal to finance new acquisitions and continue with its strategy, sealing its leadership in the Italian gambling market. Integrating more competitors in the group will allow the company to achieve new cost synergies, improving margins even more and gaining more market share in an industry that has historically been fragmented.

Gamma TopCo, the parent company of Lottomatica Group, will also sell a portion of its shares in the offering, using proceeds to repay a €150m loan from Gamma BondCo. Together with the repayment of the €250m loan to Lottomatica Group, Gamma BondCo will use the funds to repay a €400m PIK bond maturing in 2026, which was issued in 2021 to pay a special dividend to shareholders.

Deal Structure

The price for the IPO will be between €9 and €11 per share, as announced by Lottomatica on April 20. Apollo Global Management, the owner of the group, significantly lowered the target proceeds from the offering, which decreased from €1bn, as announced in January, to a maximum target of €600m. This would imply a significant discount, especially when compared to competitors such as Entain, but may still not be enough for investors, which are still sceptical after the only two IPOs that Europe has seen so far in 2023, IONOS [ETR: IOS] and Eurogroup Laminations [BIT: EGLA], have delivered losses. The implied EV from the offering, around €4.3bn, is considerably lower than the one announced in March, which amounted to €5bn. The IPO will be reserved for institutional investors. Part of the offer will be comprised of new shares, following a capital increase of €425m, while the remaining shares being offered will be sold by Gamma TopCo, the parent company. Accounting for the capital increase, Lottomatica's market cap post-IPO will fall between €2.265bn and €2.67bn, depending on the final price accepted by the market.

A pool of banks, among which Barclays, Deutsche Bank, Goldman Sachs, JP Morgan, UniCredit, Mediobanca, BNP Paribas, and Banco BPM will provide bridge financing for a total of €1.1bn, which will provide the company with short-term liquidity to pay for the listing process. The deal will also include a green shoe option, which will allow the underwriters to purchase up to 10m additional shares at a fixed price of €9, the lower bound of the offer, and an additional 8m shares at €9, the upper bound of the offer, with a cap at 15% of the total shares offered in the IPO.

Outlook for the market reaction

With the IPO set to take place at the end of April, the outlook seems bleak when comparing Lottomatica to the other 2 European IPOs of 2023. EuroGroup Laminations [BIT: EGLA] debuted on Euronext Milan at the start of February and has since seen its market capitalization fall by more than 10%. Similarly, German web hosting company IONOS [ETR: IOS] went public on the Frankfurt Stock Exchange at a similar time and has seen its shares slip 5% on the opening day, after being initially priced at the bottom of the company's target range, at €18.50 per share. The stock has since fallen by 23%. The latter listing was seen as an icebreaker to the otherwise dry European IPO market, which, before Ionos, had not seen a major listing since Porsche's debut in September 2022.

Combine these 2 stories with a Q1 2023 that has seen an 8% drop in global IPO volume and a 61% fall in proceeds from IPOs YoY and the chances of an unsuccessful IPO seem high. Nevertheless, the IPO market has been dry for a while due to uncertain macroeconomic conditions and banking turmoil dampening investors' appetite. It is

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by time that IPO activity picks up and it could be Lottomatica's ambitious plans of aggressive expansion in Italy that gets investors interested again. Apollo has also taken steps to ensure that its story goes differently from those of EuroGroup Laminations and Ionos, through taking a significant cut in its target proceeds, from €1bn to €600m and thus boosting its chances of a successful listing.

Advisors

The consortium of global coordinators is formed by Barclays, Deutsche Bank, Goldman Sachs, JP Morgan and UniCredit. Equite SIM acts as co-manager, while Credit Suisse is the financial adviser and Apollo Capital Solutions, Banca Akros and BNP Paribas are the joint bookrunners for the IPO.

TAGS: IPO, Borsa Italiana, Apollo Global Management, Lottomatica

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