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RESEARCH

Gaming Realms

4th May 2021

Final results show full effect of licensing focus. Momentum carries on into Q1 and further US growth expected. Target price increased.

Gaming Realms is a creator and licensor of innovative games for mobile, operating in the UK, US, Italy and Canada. Flagship brand Slingo® is a popular and unique game genre combining elements of slots, bingo and table gameplay. These games are licensed by some of the world's biggest online gaming operators, including DraftKings, Sky Betting & Gaming and GVC, and distributed directly to operators or via global partners such as Scientific Games using the company's proprietary Remote Game Server platform.

■ 2020 a record year with a maiden adjusted EBITDA profit posted

The last financial year was a record one financially for Gaming Realms as its high margin licensing focused strategy really took off. Revenues increased by 66% to £11.4 million and at the adjusted EBITDA level a maiden profit of £2.9 million was posted from continuing operations, up from a loss of £0.255 million in 2019. Into the new financial year and strong momentum is said to have continued, with Licensing revenues increasing by 60% in Q1 2021 to £2.1 million.

■ More games, more partners, more players

Operational highlights of the year included the company's portfolio of proprietary games on its Remote Game Server growing from 34 to 44. During the year Slingo Originals content launched with 26 new partners including gambling industry giants such as 888casino.com, DraftKings, Paddy Power Betfair and Sky Betting & Gaming. That helped to increase the number of unique players by 140% to 2.28 million and see increased international demand for content.

■ Fast growing US markets offer further growth in 2021 and beyond

In the US, the trend of individual states opening up regulated and legal online gambling activities continues. Gaming Realms obtained a provisional supplier licence for Michigan in January, with launch in the state expected in May. In Pennsylvania a game content supplier licence was filed for last year, with receipt and a going live date expected in the first half of 2021.

■ Peer derived EV/EBITDA multiple valuation suggests significant upside

Our chosen peers trade on an average historic EV/EBITDA multiple of 45 times. Discounting this to 25 times and using our 2022 forecasts implies an equity valuation of £199.17 million. Discounted back to the present day at a rate of 12% and considering potential equity dilution from the company's convertible loan gives us a target price of 51p. We retain our stance of **Conviction Buy**.

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CONVICTION BUY

Price target – 51p

**GAMING
REALMS**
PLAYING A NEW GAME

Key data

EPIC	GMR
Share price	44p
52 week high/low	47p/7.74p
Listing	AIM/OTC
Shares in issue	288,169,339
Market Cap	£126.8m
Sector	Travel & Leisure

12 month share price chart



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2020 Full Year Results

P&L

The last financial year was a record one financially for Gaming Realms as its high margin licensing focused strategy really took off. At the top line revenues increased by 66% to £11.4 million, slightly ahead of the £11.2 million alluded to in the previous full year trading update. The performance came on the back of an 81% increase in revenues from the Licensing division to £7.5 million. There was also a good performance from the smaller Social Publishing division, where revenues rose by 41% to £3.9 million.

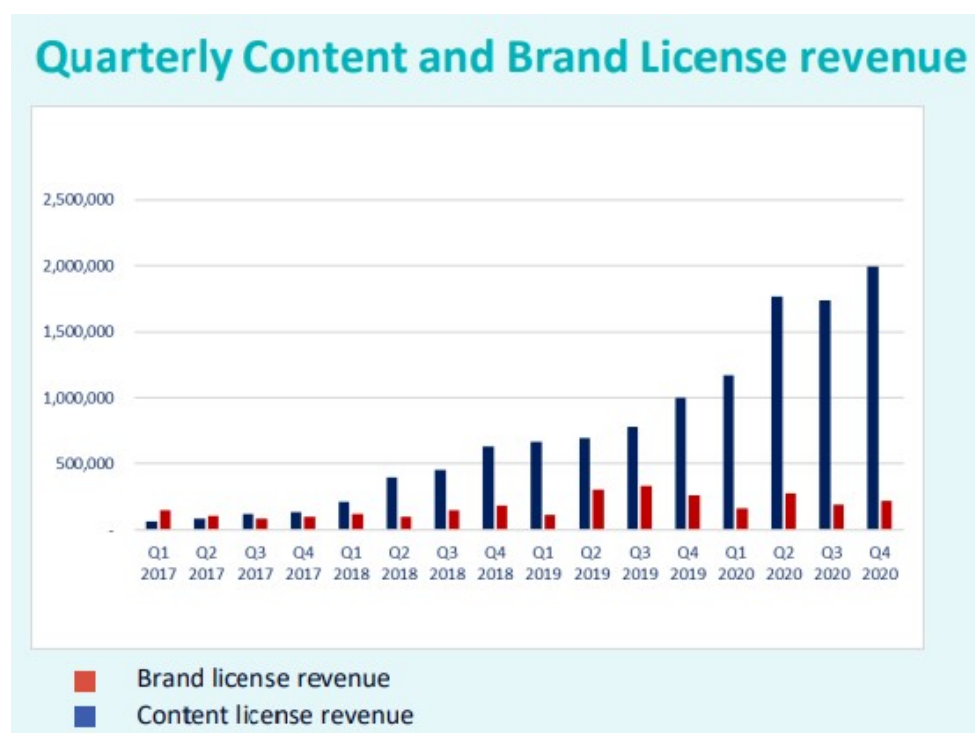
At the adjusted EBITDA level a maiden profit of £2.9 million was posted from continuing operations, up from a loss of £0.255 million in 2019. Along with the higher revenues, profits were helped by a £0.2 million fall in head office costs through ongoing cost control. The statutory loss meanwhile, which included £2.8 million of amortisation charges and £0.88 million of (non-cash) finance expenses, was cut from £4.63 million to £1.53 million.

Divisional performance

Licensing

Licensing segment revenues increased by 81% to £7.5 million as Gaming Realms continued to benefit from an increasing number of partnership deals, growth in existing partnerships and more game content. At the adjusted EBITDA level there was a £3.74 million profit, up from £1.39 million in 2019, for a margin of 50%. Notably, the company's full year investor presentation pointed out that quarterly compound growth of 23% has been seen since Q1 2018 in the Content Licensing segment of the division.

Licensing revenues from the fast growing US market, which is a key strategic focus for Gaming Realms (see page 6), increased to £2.4 million from £1.7 million in 2019. In the company's only live operating state at present, New Jersey, a c.3.5% market share from online slot products was maintained in a wider online casino market which grew by 102% over the period.



Source: Company

Social Publishing

The smaller Social Publishing division also had a good year, growing revenues by 41% to £3.9 million and reversing the falls of previous years. This was achieved by both publishing the Slingo Originals portfolio on the platform, along with the development of new tournament and promotional features. Impressively, the revenue growth was also achieved by increasing marketing spend by just £0.1 million to £0.2 million. Adjusted EBITDA grew to £1.4 million from £0.8 million, with the division producing a cash contribution to the group.

Balance Sheet & Cash Flow

Gaming Realms delivered a £2.02 million net cash inflow from operations over 2020 after the adding back of certain non-cash items including £2.82 million of amortisation charges, £0.22 million of depreciation and £0.88 million of finance charges. The total cash outflow for the year however was £0.53 million, with £2.44 million of development costs being capitalised. Cash at the period end stood at £2.1 million, with the other major balance sheet item being the company's £3.5 million convertible loan with Gamesys Group (previously JackpotJoy) arranged in December 2017. At the period end the total liability relating to this loan stood at £3.93 million. Additionally, since the period end Gaming Realms has received payment of £1 million from River Tech plc relating to deferred consideration for the July 2019 sale of its UK real money B2C assets.

Operating highlights

Operational highlights of the year included the company's portfolio of proprietary games on its Remote Game Server growing from 34 to 44. During the year Slingo Originals content launched with 26 new partners including gambling industry giants such as 888casino.com, DraftKings, Paddy Power Betfair and Sky Betting & Gaming. That helped to increase the number of unique players by 140% to 2.28 million and see increased international demand for content. Licensing deals were also signed with the likes of NetEnt, Playtech, Inspired Entertainment and King Show Games to build new innovative Slingo games. Outside of the UK, licence applications were submitted in order to enter the Pennsylvania and Michigan iGaming markets and the company prepared for launch in the Italian market.

Outlook

Into the new financial year and strong momentum is said to have continued, with Licensing revenues increasing by 60% in Q1 2021 to £2.1 million. Trading is said to be marginally ahead of Board expectations. The strategic focus in 2021 will continue to be on international expansion, securing additional partnerships and creating new Slingo games.

Gaming Realms successfully launched its Slingo content in the Italian regulated market in February, in collaboration with a number of top tier Italian gaming operators. Via partner SG Digital's Opening Gaming System (OGS) platform, the Slingo Portfolio is now live in the Italian market with iGaming operators Goldbet, Sisal Group and Lottomatica later.

In the US, the company obtained a provisional supplier licence in Michigan in January and expects to launch in the state (its second after New Jersey) in May. The licence allows Gaming Realms to provide its Slingo Originals game content to Michigan's licensed online casino operators. In preparation, the company has signed multi-state deals with BetMGM, Rush Street Interactive, DraftKings, BetMGM, Golden Nugget and Betfair/Fanduel, as well as two distribution deals with GAN for the US and European market. Meanwhile, a supplier licence is expected to be granted in Pennsylvania with launch set for the first half of the year. There are further planned launches in the US, Denmark, Spain, Canada and Portugal.

So far in 2021, nine new partners have been secured and new game Slingo Starburst has been launched in collaboration with NetEnt. This is said to have proven extremely popular with players and partners internationally, being the company's most successful launch to date in terms of unique player numbers and revenue generated in its first month.



Slingo Starburst. Source: Company

US Expansion Opportunities

Six months on from our last note on Gaming Realms, it's worth revisiting the growth opportunities in international markets, notably in the US. Here, the trend of individual states opening up regulated and legal online gambling activities continues, although perhaps at a slightly slower pace than expected. To date, twelve US states have legalised some form of online gambling.

According to Gaming Realms, the US online gaming market is expected to grow at a compound rate of 17.3% from 2020 to 2025, with gross gaming revenues forecast to rise to a value of \$6.1 billion by 2025. Meanwhile, a recent investor presentation from the company's US listed partner DraftKings suggested that the US iGaming market could be worth \$40 billion a year if all states legalised it.

In **Michigan**, The Michigan Gaming Control Board approved a number of operators to launch online betting and gaming from 22nd January this year. The market has already got off to a strong start, with online betting and gaming bringing in revenues of \$127.4 million in March, a 42.8% month-on-month increase in what was the second full month of online activity. Meanwhile, in the more mature **New Jersey** market, online gaming in March 2021 saw revenues of \$113.7 million, up by 75.4% from \$64.8 million in March 2020. The company maintaining its market share in 2020 along with the growth seen in New Jersey is testament to the quality of its games in our view.

At the time of the interim results last September Gaming Realms expected to be licensing its games in **Pennsylvania** by the start of 2021, subject to regulatory approvals, after it filed for a game content supplier licence during the first half. As noted in the recent full year results, the expectation is now for receipt of the supplier licence and a going live date in the first half of this year. Numbers for March 2021 released by the Pennsylvania Gaming Control Board showed a 293% increase in iGaming revenue in March 2021, compared to March 2020, to \$98 million (including online casino and poker but excluding sports betting).

Pennsylvania began legalising forms of online gambling in 2017 and in our view the state is a reference case for the push towards regulation. According to website www.playpennsylvania.com the state was attracted as it desperately needed a new source of tax revenue. The decision has quite literally paid off, with a total of just over \$864 million in state and local taxes having been raised up to 20th February 2021. That may even be enough incentive to encourage the ultra-strict state of Hawaii (but probably not Utah) to think again about their blanket gambling bans.

As mentioned above, Gaming Realms looks very well placed to take advantage of the move to regulation via its agreements with a range of leading US based operators. Some of them are very big and fast growing players. To take one, Rush Street Interactive is currently operating real-money gaming in nine US states and recently reported that revenues grew by 337% to \$287.5 million in 2020, with \$100 million earned in the final quarter alone. DraftKings meanwhile, while perhaps better known for its sports offering, had a 19% gross revenue market share in states where it was live with iGaming during Q4 2020. The NASDAQ listed company recently reported revenues up by 98% year-on-year to \$322 million for the three months to December.

Finally with regards to the US, in our last update note we suggested that a move to the NASDAQ market could see a higher valuation being awarded to Gaming Realms shares. While the company hasn't done that, it has recently listed its shares for trading on the OTCQX section of the US OTC Markets under the ticker PSDMF. At the end of April, management also made a presentation to investors to help boost the company's profile in the country.

Forecasts & Valuation Update

Investors have seen the recent operational and financial progress translate into positive share price movements. Gaming Realms shares recently hit 47p, the highest level since its reverse takeover IPO in July 2013. While the shares have slipped back to the current 44p they remain well ahead of lows of 4.45p seen at the depths of the coronavirus inspired sell off in March last year.



The 2020 results were slightly ahead of our previous expectations, with revenues £0.4 million ahead of our £11 million forecast and adjusted EBITDA £0.43 million ahead of our £2.47 million forecast. As such, we are revising our expectations for the current year and 2022. For valuation purposes, we retain EBITDA as the most appropriate measure of performance as Gaming Realms' has high non-cash charges associated with amortisation and interest.

As further partnership deals come on line and Gaming Realms expands in the US, for FY2021 we are now looking for revenues of £14.9 million, up from £13.8 million previously. The revival of the Social Publishing business also boosts our forecasts. Our adjusted EBITDA figure for the year goes to £5.4 million, up from £4 million. In FY2022 we expect trends to continue and are looking for £20.8 million of revenues, up from our previous forecast for £16 million, and adjusted EBITDA of £8 million, up from £5.81 million.

Peer derived valuation multiple

To illustrate what kind of valuation Gaming Realms could command if it meets our forecasts then we again look to several globally listed games licensing/development companies which provide similar services. Given the higher growth profile of the licensing sector compared to gambling, the sector to which Gaming Realms used to belong to before the disposal of its B2C assets, companies can command much higher valuations.

In our valuation table we include the details of three companies using current market data, down from five at the time of our last update in October 2020. Since then, Evolution Gaming completed its acquisition of rival NetEnt at a valuation of c.£1.7 billion and AIM listed Codemasters was acquired by Electronic Arts for c.£945 million in cash. To obtain a broader sample size for valuation purposes we also include the figures for these acquisitions into our table.

	Market Cap (£m)	Net cash (£m)	Historic EBITDA (£m)	EV/EBITDA
Evolution Gaming	30,536	283.0	288.4	104.9
Activision Blizzard	50,898	3,611	2,324	20.3
Electronic Arts	29,900	4,095	1,028	25.1
NetEnt - acquisition data used	1,677	-184.7	73.2	25.4
Codemasters - acquisition data used	945	50.1	18.2	49.1
AVERAGE				45.0

Gaming Realms peer analysis – share prices and exchange rates as at close on 29th April 2021.

Data sources: Sharepad, xe.com and individual company accounts

From our analysis we derive on average historic EV/EBITDA multiple of 45 times. This figure has largely been boosted by the share price performance of Evolution Gaming, which has more than doubled in value over the past six months. Given that Gaming Realms remains in the relatively early stages of its new licensing focused strategy, and considering its size, we feel a multiple of 25 times would be more appropriate and justifiable to use.

Applying this multiple to our 2022 forecasts for Gaming Realms, and using current net debt figures, implies an equity valuation of £199.17 million. Discounted back to the present day at a rate of 12% derives a value of £165 million, or a price per share of 57.26p.

To add a certain degree of caution to our valuation, we note the £3.5 million convertible loan due to Gamesys Group will be due for repayment in December 2022. Under the terms of the loan, Gamesys may elect to convert all or part of the principal amount into ordinary Gaming Realms shares at any time after the first year at a discount of 20% to the share price prevailing at the time of conversion. However, Gaming Realms may need to pay back part of the borrowings in cash if the price per share at conversion is lower than the nominal value of 10p, with the cash payment equal to the shortfall on the nominal value payable. But with the shares currently trading well above the nominal value a cash payment is looking increasingly unlikely. **The maximum dilution to shareholders under the loan terms will be c.11% assuming the loan is converted in full, which would effectively reduce our valuation to 51p, a figure we have chosen to adopt as our new target price.**

Conclusion

Gaming Realms is consistently showing that it can deliver quarter-on-quarter growth on the back of its content licensing focused strategy. With a relatively stable fixed cost based and a steady stream of new partnership deals coming through, we believe the company is very well positioned to continue strong growth throughout the rest of 2021 and beyond, especially as new US states are entered into. One near term catalyst for the shares in the expected granting of the supplier licence in Pennsylvania, which we believe could be achieved in the next few weeks. Speculating once again, given the growth being seen in the US markets, and considering the high levels of corporate activity in the sector, we believe Gaming Realms could be on the radar as a potential target for a larger player looking to expand its games portfolio and improve margins.

We update coverage of Gaming Realms with a target price of 51p and a stance of Conviction Buy.

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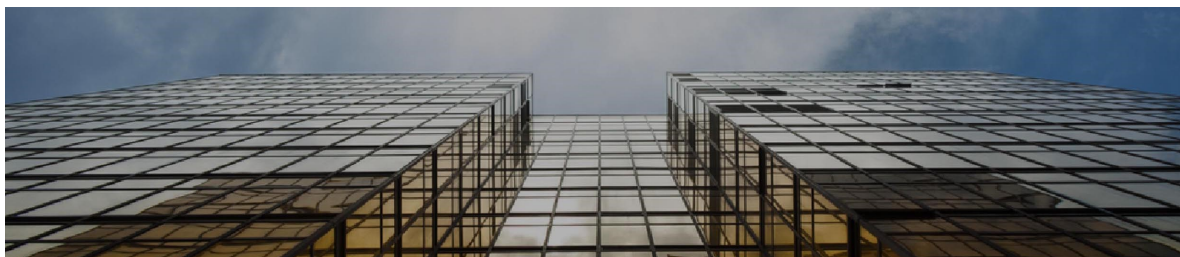
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