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Moody's INVESTORS SERVICE

Print

Rating Action: **Moody's downgrades Intralot to Caa1; outlook negative**

08 Mar 2019

London, 08 March 2019 -- Moody's Investors Service ("Moody's") has today downgraded Intralot S.A.'s ("Intralot" or "the company") corporate family rating (CFR) to Caa1 from B3 and probability of default rating (PDR) to Caa1-PD from B3-PD. Concurrently, Moody's has downgraded to Caa1 from B3 the instrument ratings on the EUR250 million Senior Notes due 2021 and EUR500 million Senior Notes due 2024, both issued by Intralot Capital Luxembourg S.A. The outlook is negative.

RATINGS RATIONALE

The downgrade of Intralot's CFR to Caa1 was primarily prompted by the loss of the SporToto tender for managing the IDDAA sports-betting licence currently held by its 45% subsidiary Inteltek in Turkey. The existing contract will expire on 28/08/2019. This contract represents EUR21.3 million (15%) of consolidated EBITDA based on LTM Q3 2018 and its loss will weaken credit metrics including leverage and cash flow. Moody's expects consolidated leverage to increase to 5.9x in 2019 from 4.8x at LTM September 2018, and proportional leverage (Debt/(EBITDA less net dividend outflow)) to increase to 7.4x from 6.4x, leading to a potentially unsustainable capital structure unless contract wins are sufficient in the next 12-18 months to enable a timely refinancing of the company's EUR250 million senior notes due in 2021. The contract loss will also further weaken liquidity by reducing future cash flow as well as impeding the company's ability to renegotiate the revolving credit facilities (RCFs) which is necessary as the existing covenants cannot currently be achieved. The situation has also been aggravated by the sudden departure of the CEO.

Intralot's rating is also constrained by (1) potential deleveraging and/or improvement in liquidity being predominantly dependent on asset disposals (eg its 20% stake in Gamenet) in an increasingly subdued market; (2) the existence of significant minority interests which results in pro-rata leverage being materially higher than reported (fully consolidated) leverage, as well as substantial cash leakage through dividend outflows to the minorities; (3) limited historic growth track record; (4) exposure to regulatory and fiscal risks inherent to the gaming industry, and (5) the increasingly muted outlooks for global growth in 2019, for example in Intralot's markets in Argentina (B2 stable) and Turkey (Ba3 negative) which together comprise around 30% of EBITDA (20% excluding the IDDAA contract).

More positively, Intralot's Caa1 CFR takes into account (1) its leading market position as a global supplier of integrated gaming systems and services; (2) a diversified contract portfolio with 87 contracts and licences; (3) its broad geographical presence in 50 jurisdictions with a foothold in the US which has significant growth potential following the invalidation of the US federal sports betting ban, although with dependency on certain countries in emerging markets such as Turkey and Argentina; (4) some revenue visibility as a result of a large number of long-term contracts, although this credit positive is dampened by frequent changes to the core business through disposals and the recent contract losses of IDDAA and partial loss in Morocco; and (5) growth potential from further liberalization of the gaming sectors in less mature markets.

LIQUIDITY

Moody's considers Intralot's liquidity profile to be weak. The company's significant near-term cash requirements to support working capital, capital expenditures and dividend payments to minorities are expected to drive negative free cash flow into 2020 and cash on hand is declining. Additionally, the company may have to repay a EUR15 million term loan if the covenants cannot be renegotiated before the end of March. The significant cash balance of EUR195 million on balance sheet as of 30 June 2018 reduced to approximately EUR160 million in December 2018 including the EUR19.5 million proceeds from the disposal of Azerinteltek. Consolidated cash is also not fully available since around EUR78 million resides (including Azerinteltek proceeds) in partnerships and belongs to minorities according their relevant stakes. Moody's also notes the requirement for around EUR25 million of cash for basic operational needs and expects the company to need access to external sources of cash to fund capex over the next 18 months (although capex can be reduced by around EUR15 million in 2019 without the IDDAA contract). Although the IDDAA contract loss is clearly negative, it is likely to be a cash positive event for Intralot in 2019 because of the capex reduction and repatriation of residual cash which the company estimates will be around EUR10 million. The company's existing RCFs amounting in aggregate to EUR80 million both maturing on 30 June 2021 contain leverage and interest coverage covenants that would be breached if tested. The facilities will not be renegotiated under the current terms. The company has stated that its 20% stake in Gamenet Group S.p.A. (B1, stable) which is valued at EUR45 million based on Gamenet's market capitalization as at 5 March 2019 will be sold at an appropriate time, and there is also a plan to dispose of Polish operations. However, the timing of either potential disposal remains uncertain.

RATIONALE FOR NEGATIVE OUTLOOK

The negative outlook reflects the absence of available access to external sources of cash and the increased difficulty the company may have in achieving this. It also reflects the uncertainty surrounding future earnings now that consolidated, annualized EBITDA will be reduced by around EUR44 million in 2019 (c. EUR15 million on a proportionate basis) without the IDDAA and Azerinteltek contracts.

WHAT COULD CHANGE THE RATING UP/DOWN

Given the negative outlook, Moody's anticipates no upward pressure on the ratings. A stabilization of the negative outlook could result if the company obtained access to external liquidity facilities, with covenants that, in Moody's view, allow comfortable headroom considering the potential for deteriorating financial metrics, and if the company could demonstrate a sustainable reversal of the decline in EBITDA through contract wins.

Downward pressure on the ratings could result from any further deterioration of underlying cash or other source of a weakening in the company's liquidity, or a materially adverse regulatory change or further loss of key contract.

STRUCTURAL CONSIDERATIONS

The EUR500 million 5.250% Senior notes due 2024 and EUR250 million Senior Notes due 2021 rank pari passu. The notes and bank facilities share the same guarantee package, set for a minimum of 70% of the consolidated EBITDA and total assets in the facilities agreements. Moody's notes that the presence of minorities in certain guarantor subsidiaries significantly reduces the potential support available from such entities.

The principal methodology used in these ratings was Gaming Industry published in December 2017. Please see the Rating Methodologies page on www.moody's.com for a copy of this methodology.

PROFILE

Headquartered in Athens, Intralot, is a global supplier of integrated gaming systems and services. Intralot designs, develops, operates and supports customized software and hardware for the gaming industry and provide technology and services to state and state licensed lottery and gaming organizations worldwide. Intralot operates a portfolio of 87 contracts and licences across 50 jurisdictions employing approximately 5,100 people. Intralot is listed on the Athens stock exchange and has a market capitalization of c. EUR70 million as of 5 March 2019.

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Related Research

Credit Opinion: Intralot S.A.: Update of key credit factors following downgrade to B3

Credit Opinion: Intralot S.A.: Update of key credit factors following downgrade to B2

LGD Assessment: Intralot S.A.

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