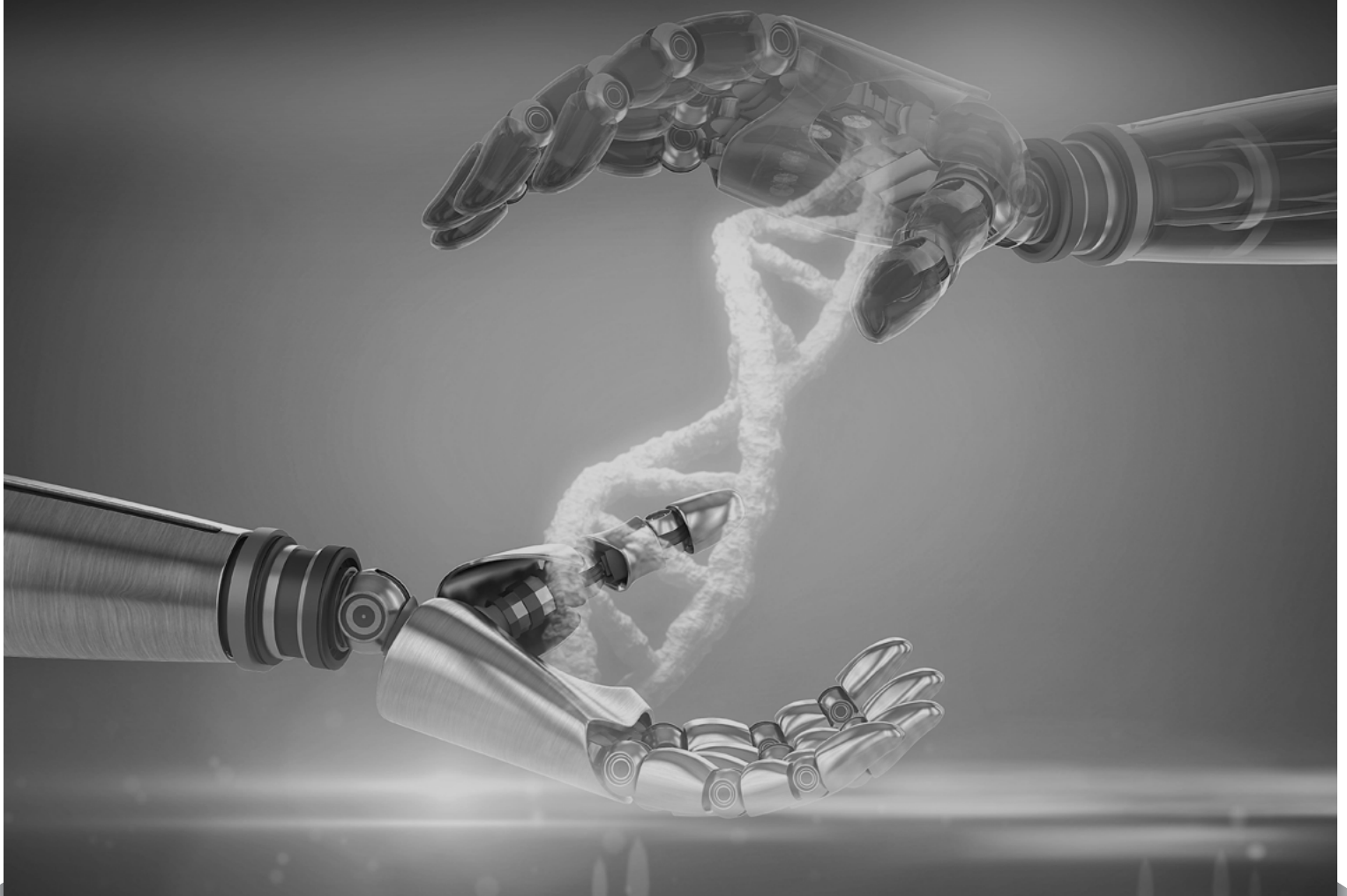




Emerging Stocks Down Under

📖 *First mover advantage doesn't go to the company that starts up; it goes to the company that scales up.* 📖

- Reid Hoffman (b. 1967), LinkedIn co-founder, tech venture capitalist



POINTS BET

A once in a lifetime growth opportunity

POINTSBET

A once in a lifetime growth opportunity

Stocks Down Under rating: ★★★★★

ASX: PBH

Market cap: A\$784.2M

52-week range: A\$1.92 / A\$12.42

Share price: A\$2.48

Despite being 'the land of the free', the USA has been slower than Australia to legalise sports betting. PointsBet (ASX: PBH) is one of a handful of companies seeking to capitalise on this and it has an established business in Australia. After listing at \$2 a share in mid-2019, shares went up to nearly \$18, but have since retreated to \$2.58 today. We accept that the company is not yet profitable. However, we still think the market is a once in a lifetime opportunity that is still being unlocked and PointsBet is well placed to capitalise on it.

Share price chart



Source: Tradingview

A significant opportunity awaits PointsBet ...

PointsBet is an online corporate bookmaker that was founded in Australia during 2015. It has an established business in Australia with over 230,000 cash active clients and a turnover of \$579.4m. It is hoping to achieve positive EBITDA in the Australian business for FY22. But it is the USA where the real opportunity lies.

Sports betting is gradually being legalised on a state-by-state basis. As of mid-2022 over 30 states have legalised sports betting. Since the legalisation of sports betting, over US\$125bn has been spent by American consumers, more than the net income for all the nation's farmers. Remember, this is with just over half the states having legalised gambling and some of the more populous states excluding themselves - California and Texas are two examples.

PointsBet listed in mid-2019 with promise that it would gradually penetrate the American market. It listed with a market capitalisation of ~\$220m and group revenue of \$25.6m. Fast forward to mid-2022 and it had \$139.1m revenue in 1HY22 alone, a market capitalisation of ~\$881m and group turnover of nearly \$1.4bn. It has now gone live with sports betting in 10 US states and the Canadian province of Ontario, along with iGaming in a further 4 US states, whereby users can access general gambling products. It also has a partnership with media outlet NBC to help it grow its band. Another important thing to remember is that PointsBet in America offers in-play betting. We can't blame investors for not acknowledging this because in-play betting isn't legal in Australia. But in more mature European markets, this is 75-80% of sports betting activity and the company is banking on the hope that it will be similar in the US.

... but not one without hurdles

Still, after surging roughly 8 times from its IPO price, PointsBet has significantly declined to under \$3 a share. We think there are two reasons for its decline. First and most, obviously, is that PointsBet isn't profitable yet and isn't expected to be for some time. For FY23, consensus estimates suggest -\$269.8m in EBITDA. And in 3Q22, it burnt \$85.3m in cash. In an environment of rising inflation and interest rates, investors want nothing to do with unprofitable companies.

Second, its rollout hasn't been as fast as investors anticipated. In its defence, we would note three points in relation to the broader market. First, sports betting markets are ultracompetitive with dozens of operators. In the state of Arizona alone, there were 18 operators that went live on Week 1 of the 2021 NFL season. Second, some states that have legalised sports betting only allow in-person betting – nine to be exact, including Mississippi, North Carolina and New Mexico. This will make it harder for online operators, such as PointsBet, to access these customers. Third, businesses have to pay significant licensing fees to the states. Iowa, for instance, charges US\$45,000 up front and US\$10,000 every year after that, and Iowa is considered among the cheapest.

And in relation to the company specifically, we observe that it has been spending significant money on marketing (including those ads with Shaq O'Neill) and has been building up its capabilities in order to stand out in the market. All of these set it up for the longer term but impact its cash burn. The company has also completed multiple capital raises that have diluted its share base significantly – its market cap is ~4x higher than what it listed at, but its share price is up by less than 50%.

Still Australia's best chance to make it in the American market

However, we have decided to give PointsBet four stars, considering the opportunity awaiting the company, its position relative to its ASX peers.

Remember, BlueBet (ASX: BBT) - which listed in mid-2021 - has only just secured market access for its fourth state and only expects to take first bets in its first US state in the coming weeks. BetMakers (ASX: BET), meanwhile, appears to only be focused on horse racing – although it is profitable. PointsBet, on the other hand, will be live in 14 states by this year's end and is the top sports betting operator by EGR North America for two years running. This is inevitably because of the differentiating features in the app including in-play options, the speed of bet settlements and cash-out options available to users. Bear in mind, PBH also has a strong Australian business too.

Although consensus estimates forecast an EBITDA loss of \$269.8m in FY23, a 60% growth in revenue is forecast – from \$300.5m to \$479.4m. Losses are expected to decline in the years ahead and profitability is forecast for FY26, by which time \$1.3bn in revenue is forecast. It is trading at just 0.6x its FY23 revenues, well below the 8x trailing revenue multiple it first listed at back in 2019.

Looking technically, we think it broke out of a long-term downtrend after last month's announcement of a \$94.2m investment from Sports Investment Group. The deal was completed at a 15% premium to its preceding 5-day VWAP and which gave it a 12.8% stake in the company. We also observe that PointsBet's directors, particularly Brett Paton, have been avid on-market buyers of the stock ever since it listed. Beyond the sentiment, it will help PointsBet accelerate its technology roadmap. Nevertheless, yesterday's close below \$2.50 does beg the question as to if it is about to return to a downtrend.

ESG investors will despise this company, with gambling typically a 'no-go' zone for them. Investors wanting safe, profitable companies likely won't either. But we think investors (as distinct from day traders) looking for a longer-term growth story that is literally a once in a lifetime opportunity (considering the size of the US sports betting market and how a huge proportion of the market is still to be unlocked), should give this company a close look.



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