EDISON

EML Payments

H123 results

Considering its options

Software and comp services

EML Payments' H123 results reflected the changing mix of revenue (lower establishment fees and breakage, higher interest income), the effect of the ongoing remediation of regulatory issues in the European and UK PFS businesses and the restructuring of the group. With the Irish regulator raising additional concerns post results and applying a more stringent growth cap to EML's Irish subsidiary, PFS Card Services Ireland Limited (PCSIL), the board has initiated a strategic review of the business.

Year end	Revenue (A$m)	PBT* (A$m)	NPATA** (A$m)	Diluted EPS* (c)	DPS (c)	P/E (x)	EV/EBITDA*** (x)
06/21	192.2	30.2	21.0	6.6	0	8.9	4.3
06/22	232.4	16.0	19.3	3.4	0	17.2	4.5
06/23e	240.3	(23.1)	(22.0)	(4.9)	0	N/A	8.7
06/24e	253.2	2.0	3.0	0.4	0	135.7	7.9

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **NPATA = net profit after tax, excluding acquisition-related costs. ***Based on underlying EBITDA.

H123 results reflect focus on compliance

For H123, EML reported gross debit volume (GDV) growth of 55% y-o-y (7% excluding Sentenial, which was acquired midway through H122), revenue growth of 2% (-0.6% organic) and an underlying EBITDA decline of 50%. Lower breakage and non-recurring revenues in Gifting and lower establishment fees in General Purpose Reloadable (GPR) due to the regulatory remediation programme were partially offset by higher interest income on float. Overheads increased on an underlying basis to support the increased focus on compliance and one-off costs of $21.6m included regulatory remediation, litigation, fraud losses and restructuring.

Regulatory challenges; strategic review launched

Post results, the Central Bank of Ireland (CBI) wrote to EML expressing dissatisfaction with the remediation programme and raising the prospect of a more stringent growth cap for PCSIL. This growth cap has since been applied, effective 31 March 2023 to 31 March 2024. A board sub-committee has been formed, chaired by new non-executive director, Peter Lang, to oversee the remediation programme. A strategic review of the business has also been launched. EML maintains guidance for underlying EBITDA of A$26–34m in FY23. We have revised our forecasts to reflect H123 results and the new growth cap, which combined reduce our FY24 revenue forecast by 6.7% and EBITDA by 26.5%.

Valuation: Reflects increased uncertainty

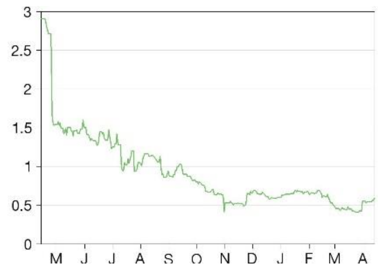
EML is trading at a substantial discount to global payment processor and prepaid card peers on an EV/sales and EV/underlying EBITDA basis. Evidence of positive progress with the Irish and UK regulators as well as the outcome of the strategic review could trigger upside from this point.

14 April 2023

Price	**A$0.585**
Market cap	**A$219m**

Net debt (A$m) at end H123	6.8
Shares in issue	374.0m
Free float	93%
Code	EML
Primary exchange	ASX
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	33.0	(9.3)	(80.1)
Rel (local)	29.2	(9.1)	(79.4)
52-week high/low		A$2.91	A$0.41

Business description

EML Payments is a payment solutions company managing thousands of programmes across 32 countries in Europe, North America and Australia. It provides payment solutions for banking, credit and disbursement services, earned wage access, gifts, incentives and rewards, and open banking and FX.

Next events

Q323 update	May

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EML Payments is a research client of Edison Investment Research Limited

Review of H123 results

We summarise EML's H123 performance in Exhibit 1. Group revenue grew 2% y-o-y, group underlying gross profit increased 5% y-o-y and underlying EBITDA declined from A$26.9m in H122 to A$13.4m in H123. In Exhibit 2, we summarise the key adjustments to reach EML's underlying EBITDA and NPATA measures.

Exhibit 1: Half-yearly performance

	H123	H122	y-o-y
GDV (A$bn)			
Gifting	1.1	0.9	16%
GPR	6.5	6.3	4%
Digital Payments	41.8	24.4	71%
Group GDV	49.4	31.6	55%
Yield (bp)			
Gifting	321	408	-87
GPR	110	111	-1
Digital Payments	3	3	0
Group yield	24	36	
Revenue (A$m)			
Gifting	34.0	37.1	-8%
GPR	72.1	69.6	4%
Digital Payments	10.5	7.7	37%
Group revenue	116.6	114.4	2%
Gross profit	70.4	75.4	-7%
Gross margin	*60.3%*	*65.9%*	
Underlying gross profit*	78.9	75.4	5%
Underlying gross margin	*67.6%*	*65.9%*	
EBITDA	(8.2)	14.2	N/A
Underlying EBITDA	13.4	26.9	-50%

Source: EML Payments. Note: *Adjusted for fraud losses of A$8.5m.

Exhibit 2: Reconciliations from reported to underlying profit measures

A$m	H123	H122		H123	H122
EBITDA	**(8.232)**	**14.203**	**NPATA**	**(15.992)**	**3.961**
Regulation remediation & class action costs	8.502	12.659		7.102	9.101
Fraud losses	8.476	0.000		6.357	0.000
Restructuring costs	4.627	0.000		3.239	0.000
Underlying EBITDA	**13.373**	**26.862**	**Underlying NPATA**	**0.706**	**13.062**

Source: EML Payments

The company impaired goodwill by a total of A$121.4m during H123, split as A$86.2m for PFS and A$35.1m for Sentenial. EML also reduced the estimated contingent consideration payable for Sentenial from A$28.9m at the end of FY22 to A$10.7m at the end of H123 resulting in a one-off credit of A$19.3m at the net finance cost level. An earn-out of up to €40m is payable based on revenue achieved by Sentenial's Nuapay business in CY23. The maximum pay-out requires CY23 revenue of least €30m and the earn-out is structured on a sliding scale to reward growth from the €3m base level at acquisition. As the Sentenial deal took longer to close than expected, delaying the investment by EML of sales and marketing resource, the likelihood of achieving the maximum pay-out is low.

EML closed H123 with cash of A$79.2m and net debt of A$6.8m (excluding leases). During H123, the company received A$10.9m in cash for the sale of its stake in Interchecks.

Divisional performance

Gifting: Incentives growth outpaced mall card growth

The Gifting division saw 16% growth in GDV year-on-year, with incentives growing at a faster rate than malls (31% versus 7%). An employee benefits programme in Ireland that leveraged the Small Benefits Scheme was a key contributor to growth. The division reported less breakage this year than last year as the effects of COVID-19 related mall closures have been worked through. The division reclassified A$2.2m of H122 revenue from breakage to non-recurring revenue to reflect the one-off nature of the work. Yield declined due to lower breakage and a higher proportion of incentives cards in the mix. Interest income increased from A$0.1m in H122 to A$1.1m in H123, reflecting rises in interest rates globally. Gross margin was materially in line with the prior year.

GPR: Interest income increased materially

GPR GDV increased 4% y-o-y, despite the effect of regulatory remediation in the PFS business, which reduced the ability to launch new programmes. Salary packaging volumes in Australia were up 8% y-o-y. Yield was essentially flat year-on-year, with establishment income down 27% y-o-y but interest income increasing significantly from A$2.2m in H122 to A$8.0m in H123. Gross margin was flat year-on-year at 56%; excluding A$2.4m in one-off fraud costs underlying gross margin was 59%.

Digital Payments (DP): Sentenial fraud weighed on gross margin

DP GDV increased 71% y-o-y reflecting a full six-month contribution from Sentenial versus three months in H122. Sentenial contributed GDV of A$36.5bn, of which c A$0.7bn (+19% y-o-y pro-forma) came from Nuapay's open banking service. The original DP business grew GDV 6% y-o-y. Sentenial contributed revenue of A$5.6m in the period versus A$2.7m a year ago. Yield was flat year-on-year at 3bp. The previously disclosed fraud in the Sentenial business cost A$6.1m at the gross profit level, bringing the gross margin down to 28.0% compared to 81.5% in H122. Excluding this loss, the underlying gross margin was 89%.

Board changes

In early February, the company confirmed that it was refreshing the board, with three directors (David Liddy, Melanie Wilson and Tony Adcock) resigning on or before the 2023 AGM. On 22 February, the company announced it had appointed three new independent non-executive directors who will stand for election at the 2023 AGM, with the three previous directors stepping down with immediate effect. The new directors are:

- Dr Luke Bortoli: previously he was CFO of Afterpay (2018–21), held senior roles at Aristocrat (2015–18), and prior to that was an investment banker at UBS. The board has appointed Dr Bortoli as chairman.
- Peter Lang: worked at McMillan Shakespeare in various executive roles.
- Connor Haley: nominee director from the company's 8.14% shareholder, Alta Fox Capital.

Regulatory update; strategic review launched

Post H123 results on 22 February, PCSIL, EML's Irish subsidiary, received a letter from the CBI. On 24 February the company disclosed that the CBI considers that PCSIL has made limited remediation progress to date with significant and ongoing deficiencies remaining in PCSIL's AML/CFT control framework. It is also not satisfied with PCSIL's remediation plan and timetable for completion.

EML had previously expected to complete the remediation programme and third-party assessment by the end of CY23, but now considers that this timeframe is at risk and is subject to further engagement by PCSIL with the CBI.

The CBI noted that it was considering applying a new growth cap to payment volumes for the period 31 March 2023 to 30 March 2024, allowing no growth from the level processed in the period January to December 2022. This compares to the existing 10% cap applied to the 12-month period to 8 December 2023. The CBI gave PCSIL the opportunity to provide it with submissions by 10 March for its consideration. On 31 March, EML announced that the CBI had imposed the 0% growth cap from that date and also confirmed that there was no change to the FY23 guidance given on 22 February.

The growth cap only applies to the European general purpose reloadable programmes covered by PCSIL's e-money institution licence, which made up c 30% of group revenue for H123. The company took an impairment charge for PFS in H123 but may need to increase this now that the more stringent growth cap has been applied.

A board sub-committee has been set up to oversee the issue, headed by Peter Lang. The company has also launched a strategic review of the business.

Outlook

At H123 results, the company revised its FY23 guidance slightly, reducing the revenue range from A$240–260m to A$235–245m but also reducing the overheads range from A$135–145m to A$133–140m resulting in unchanged underlying EBITDA guidance of A$26–34m. It also guided to underlying NPATA of a loss of A$4m to a profit of A$4m.

The company noted that interest income was A$2.5m in January and rates have risen again since then. Just using the January level for the rest of the year would result in interest income of A$24.1m for FY23, compared to A$5.1m for FY22.

We have revised our forecasts to reflect H123 results and to factor in slower growth for GPR in FY24 due to the more stringent growth cap.

Exhibit 3: Changes to forecasts

		FY23e Old	FY23e New	Change	y-o-y	FY24e Old	FY24e New	Change	y-o-y
Revenues	**A$m**	**240.9**	**240.3**	**-0.3%**	**3.4%**	**271.3**	**253.2**	**-6.7%**	**5.4%**
Gross profit	A$m	161.5	154.1	-4.6%	-2.3%	183.8	172.4	-6.2%	11.9%
Gross margin		*67.0%*	*64.1%*	*-2.9%*	*-3.8%*	*67.8%*	*68.1%*	*0.3%*	*4.0%*
Underlying gross profit	**A$m**	**161.5**	**162.4**	**0.5%**	**2.9%**	**183.8**	**172.4**	**-6.2%**	**6.2%**
Underlying gross margin		***67.0%***	***67.6%***	***0.5%***	***-0.3%***	***67.8%***	***68.1%***	***0.3%***	***0.5%***
EBITDA	A$m	10.5	(0.2)	-102.0%	-100.6%	39.2	28.8	-26.5%	-13850.6%
EBITDA margin		*4.4%*	*-0.1%*	*-4.4%*	*-14.8%*	*14.4%*	*11.4%*	*-3.1%*	*11.5%*
Add back one-off costs	A$m	16.0	26.6	66.3%	N/A	0.0	0.0	N/A	N/A
Underlying EBITDA	**A$m**	**26.5**	**26.4**	**-0.4%**	**-48.4%**	**39.2**	**28.8**	**-26.5%**	**9.0%**
Underlying EBITDA margin		***11.0%***	***11.0%***	***0.0%***	***-11.0%***	***14.4%***	***11.4%***	***-3.1%***	***0.4%***
Normalised operating profit	A$m	7.1	(19.4)	-374.1%	-205.3%	16.1	5.8	-64.1%	-129.9%
Normalised operating margin		*2.9%*	*-8.1%*	*-11.0%*	*-16.0%*	*5.9%*	*2.3%*	*-3.6%*	*10.3%*
Reported operating profit	A$m	(31.4)	(158.9)	405.4%	N/A	(6.4)	(13.7)	113.9%	-91.4%
Reported operating margin		*-13.0%*	*-66.1%*	*-53.1%*	*-66.2%*	*-2.4%*	*-5.4%*	*-3.1%*	*60.7%*
Normalised PBT	A$m	3.3	(23.1)	-794.3%	-244.4%	12.4	2.0	-83.4%	-108.9%
Reported PBT	A$m	(35.2)	(143.9)	309.1%	42224.5%	(10.1)	(17.5)	72.0%	-87.9%
Normalised net income	A$m	2.7	(18.5)	-794.3%	-244.4%	9.9	1.6	-83.4%	-108.9%
NPATA	A$m	(8.1)	(22.0)	170.6%	-213.8%	11.9	3.0	-74.4%	-113.8%
Add back one-off costs	A$m	12.8	20.7			0.0	0.0		
Underlying NPATA	**A$m**	**4.7**	**(1.3)**	**-128.4%**	**-104.1%**	**11.9**	**3.0**	**-74.4%**	**-329.3%**
Reported net income	A$m	(28.1)	(144.3)	412.9%	2906.3%	(8.1)	(14.0)	72.0%	-90.3%
Normalised basic EPS	A$	0.01	(0.05)	-793.8%	-243.2%	0.03	0.00	-83.5%	-108.9%
Normalised diluted EPS	A$	0.01	(0.05)	-804.5%	-245.5%	0.03	0.00	-83.5%	-108.7%
Reported basic EPS	A$	(0.08)	(0.39)	412.6%	2882.3%	(0.02)	(0.04)	71.8%	-90.3%
NPATA/share	A$	(0.02)	(0.06)	170.4%	-212.9%	0.03	0.01	-74.5%	-113.8%
Dividend per share	A$	0.00	0.00	N/A	N/A	0.00	0.00	N/A	N/A
Net debt/(cash)	A$m	(4.5)	(1.7)	-61.7%	-117.6%	16.8	18.8	12.3%	-1203.3%
GDV	A$bn	100.5	99.3	-1.2%	23.7%	107.2	102.0	-4.9%	2.7%
Yield	bp	24	24	0	-5	25	25	0	1
Divisional data									
GDV									
G&I	A$bn	1.4	1.5	3%	11%	1.6	1.6	3%	10%
GPR	A$bn	13.1	13.3	2%	8%	14.4	13.7	-5%	3%
Digital Payments	A$bn	85.9	84.5	-2%	27%	91.2	86.6	-5%	3%
Revenue									
G&I	A$m	74.7	68.2	-9%	0%	82.2	77.5	-6%	14%
GPR	A$m	142.7	150.8	6%	2%	158.5	151.2	-5%	0%
Digital Payments	A$m	23.3	21.0	-10%	27%	30.4	24.3	-20%	15%
Gross profit									
G&I	A$m	59.0	54.2	-8%		64.9	61.6	-5%	
GPR	A$m	82.8	87.5	6%		93.5	90.0	-4%	
Digital Payments	A$m	19.5	12.2	-37%		25.2	20.6	-18%	
Gross margin									
G&I		79.0%	79.5%			79.0%	79.5%		
GPR		58.0%	58.0%			59.0%	59.5%		
Digital Payments		83.7%	57.9%			82.8%	84.9%		

Source: Edison Investment Research

Exhibit 4: Financial summary

A$m	2017	2018	2019	2020	2021	2022	2023e	2024e
30-June	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT								
Revenue	58.0	71.0	97.2	121.0	192.2	232.4	240.3	253.2
Cost of Sales	(13.7)	(17.7)	(24.2)	(32.9)	(63.8)	(74.6)	(86.2)	(80.8)
Gross Profit	44.2	53.3	73.0	88.1	128.4	157.8	154.1	172.4
EBITDA	14.5	21.0	29.7	32.5	42.2	34.3	(0.2)	28.8
Normalised operating profit	11.9	18.1	25.6	22.4	31.6	18.4	(19.4)	5.8
Amortisation of acquired intangibles	(8.9)	(7.2)	(7.5)	(11.1)	(20.2)	(16.5)	(17.0)	(17.0)
Exceptionals	0.2	(0.3)	(3.0)	(13.6)	(11.2)	1.4	(120.0)	0.0
Share-based payments	(5.3)	(5.0)	(4.2)	(6.1)	(5.0)	(3.0)	(2.5)	(2.5)
Reported operating profit	(2.1)	5.6	10.9	(8.5)	(4.8)	0.3	(158.9)	(13.7)
Net Interest	0.0	(0.1)	(0.0)	(0.7)	(1.4)	(2.4)	(3.7)	(3.7)
Joint ventures & associates (post tax)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	(0.5)	(1.8)	1.3	(17.1)	1.8	18.7	0.0
Profit Before Tax (norm)	11.9	17.9	25.6	21.6	30.2	16.0	(23.1)	2.0
Profit Before Tax (reported)	(2.1)	5.0	9.0	(7.9)	(23.3)	(0.3)	(143.9)	(17.5)
Reported tax	2.1	(2.8)	(0.6)	0.7	(5.4)	(4.5)	(0.4)	3.5
Profit After Tax (norm)	8.9	14.4	20.5	17.2	24.1	12.8	(18.5)	1.6
Profit After Tax (reported)	0.0	2.2	8.5	(7.1)	(28.7)	(4.8)	(144.3)	(14.0)
Minority interests	0.0	0.0	(0.2)	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net income (normalised)	8.9	14.4	20.3	17.2	24.1	12.8	(18.5)	1.6
Net income (reported)	0.0	2.2	8.3	(7.1)	(28.7)	(4.8)	(144.3)	(14.0)
Basic ave. number of shares outstanding (m)	245	246	249	304	360	371	374	374
EPS - basic normalised (A$)	0.036	0.058	0.081	0.056	0.067	0.035	(0.049)	0.004
EPS - normalised fully diluted (c)	3.559	5.674	7.812	5.489	6.579	3.398	(4.942)	0.431
EPS - basic reported (A$)	0.000	0.009	0.033	(0.023)	(0.080)	(0.013)	(0.386)	(0.037)
Dividend (A$)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Revenue growth (%)	148.6	22.5	36.9	24.4	58.9	20.9	3.4	5.4
Gross Margin (%)	76.3	75.1	75.1	72.8	66.8	67.9	64.1	68.1
EBITDA Margin (%)	25.1	29.6	30.6	26.9	21.9	14.8	-0.1	11.4
Normalised Operating Margin	20.5	25.4	26.4	18.5	16.4	7.9	-8.1	2.3
BALANCE SHEET								
Fixed Assets	90.6	108.0	162.9	872.1	685.3	827.3	839.7	850.0
Intangible Assets	60.1	65.8	104.6	371.7	350.1	448.5	322.2	307.0
Tangible Assets	2.8	3.5	5.4	14.6	11.2	12.7	10.2	12.5
Investments & other	27.6	38.7	53.0	485.8	323.9	366.1	507.3	530.4
Current Assets	96.9	131.6	313.8	1,008.6	1,603.5	1,855.1	1,980.4	2,030.0
Stocks	10.3	12.6	18.2	22.3	16.4	21.5	13.2	14.1
Debtors	6.3	8.9	14.4	21.7	22.0	35.8	33.0	34.8
Cash & cash equivalents	39.9	39.0	33.1	118.4	141.2	73.7	85.1	44.6
Other	40.4	71.1	248.2	846.2	1,424.0	1,724.1	1,849.1	1,936.5
Current Liabilities	(62.8)	(90.5)	(299.0)	(1,357.8)	(1,792.8)	(2,100.1)	(2,391.3)	(2,490.3)
Creditors	(23.8)	(21.2)	(33.9)	(47.5)	(62.9)	(65.7)	(78.4)	(73.1)
Tax and social security	(0.0)	0.0	(0.8)	(2.6)	(6.0)	(2.8)	(2.8)	(2.8)
Short term borrowings	0.0	0.0	(15.0)	0.0	(1.4)	(1.8)	(1.8)	(1.8)
Other	(39.0)	(69.3)	(249.4)	(1,307.7)	(1,722.5)	(2,029.8)	(2,308.4)	(2,412.6)
Long Term Liabilities	(4.2)	(19.3)	(33.5)	(82.6)	(81.1)	(145.2)	(125.2)	(97.6)
Long term borrowings	0.0	0.0	0.0	(35.8)	(36.9)	(81.6)	(81.6)	(61.6)
Other long term liabilities	(4.2)	(19.3)	(33.5)	(46.8)	(44.2)	(63.6)	(43.5)	(35.9)
Net Assets	120.6	129.8	144.2	440.2	414.9	437.1	303.6	292.1
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Shareholders' equity	120.6	129.8	144.2	440.2	414.9	437.1	303.6	292.1
CASH FLOW								
Op Cash Flow before WC and tax	13.1	19.7	28.4	31.2	41.2	33.3	(1.2)	27.8
Working capital	4.9	(9.2)	2.0	3.6	31.7	(68.4)	26.0	(14.3)
Exceptional & other	(0.8)	(1.2)	(0.7)	(12.7)	(17.3)	0.4	1.0	0.0
Tax	2.1	(2.8)	(0.6)	0.7	(5.4)	(4.5)	(0.4)	3.5
Net operating cash flow	19.3	6.5	29.2	22.8	50.2	(39.2)	25.3	17.0
Capex	(2.9)	(5.3)	(5.8)	(11.0)	(12.6)	(14.1)	(18.9)	(21.2)
Acquisitions/disposals	0.0	(0.7)	(44.0)	(142.5)	(3.5)	(57.1)	10.6	(10.7)
Net interest	0.0	(0.1)	(0.0)	(0.7)	(1.4)	(2.4)	(3.7)	(3.7)
Equity financing	0.2	0.0	0.4	240.8	0.6	0.0	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	(3.6)	(0.6)	(0.4)	(7.0)	(11.0)	(1.9)	(1.9)	(1.9)
Net Cash Flow	13.0	(0.2)	(20.6)	102.3	22.2	(114.6)	11.4	(20.5)
Opening net debt/(cash)	(26.9)	(39.9)	(39.0)	(18.1)	(82.5)	(103.0)	9.7	(1.7)
FX	(0.0)	(0.6)	(0.3)	(2.0)	0.6	(1.1)	0.0	0.0
Other non-cash movements	0.0	0.0	0.0	(35.8)	(2.4)	3.0	(0.0)	0.0
Closing net debt/(cash)	(39.9)	(39.0)	(18.1)	(82.5)	(103.0)	9.7	(1.7)	18.8

Source: EML Payments, Edison Investment Research

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