9th March 2016

TMT

Worldpay

Price 277.80p

The US branch is a thorn in the group's side; no clear operating leverage before H2 17

Fair Value 278p vs. 290p (0%) **NEUTRAL**

Bloomberg	WPG LN
Reuters	WPG.L
12-month High / Low (p)	316.8 / 240.0
Market Cap (GBP)	5,556
Ev (BG Estimates) (GBP)	6,981
Avg. 6m daily volume (000)	9,885
3y EPS CAGR	32.6%

	1 M	3 M	6 M	31/12/15
Absolute perf.	0.8%	-6.3%	ns	-9.6%
Softw.& Comp.	6.3%	-5.8%	10.9%	-6.2%
DJ Stoxx 600	7.4%	-7.7%	-6.0%	-7.7%

YEnd Dec. (GBPm)	2014	2015e	2016e	2017e
Sales	3,627	3,963	4,240	4,580
% change		*9.3%*	*7.0%*	*8.0%*
EBITDA	286	302	392	496
EBIT	296.3	340.5	366.8	413.1
% change		*14.9%*	*7.7%*	*12.6%*
Net income	91.7	138.4	226.2	266.4
% change		*50.9%*	*63.4%*	*17.8%*

	2014	2015e	2016e	2017e
Operating margin	8.2	8.6	8.7	9.0
Net margin	-1.4	-0.8	3.4	4.7
ROE	26.0	-4.4	17.5	21.7
ROCE	14.0	12.1	14.5	15.5
Gearing	-1,173	212.4	158.2	112.1

(p)	2014	2015e	2016e	2017e
EPS	5.71	6.92	11.31	13.32
% change	-	*21.1%*	*63.4%*	*17.8%*
P/E	48.6x	40.1x	24.6x	20.9x
FCF yield (%)	0.0%	0.6%	1.7%	4.0%
Dividends (p)	0.00	0.00	1.78	2.69
Div yield (%)	NM	NM	0.6%	1.0%
EV/Sales	2.2x	1.8x	1.6x	1.5x
EV/EBITDA	27.3x	23.1x	17.4x	13.5x
EV/EBIT	26.4x	20.5x	18.7x	16.1x

Worldpay is struggling in the US (49% of group's sales), so the poor lfl top-line growth associated cannot create any leverage on its proprietary platform. We see no way out as the management does not intend to sell this division, whereas the market is consolidating. The real leverage on profitability won't be visible until H2 17e (once investment in its technology platforms is complete, i.e. Worldpay fully independent from RBS). WP's fundamentals are not impressive for the Payments sector (lfl sales growth, EBITDA and EBIT margin, FCF, financial position). We have revised downward our restated FY16/17e EPS sequence by 3.0% on average. Neutral rating reiterated and FV cut from 290p to 278p.

ANALYSIS

- **Worldpay is suffering in the US.** With an EBITDA margin of only 3.2% (-130bps), Worldpay US is putting the whole group's profitability under pressure (EBITDA margin of 7.6% vs. >=20% for European peers). The lack of size in the US, which is 49% of its FY15 sales, prevents the group from generating a significant leverage on its proprietary platform (very fragmented market). We are not optimistic for Worldpay's future in this region as its direct local competitors are much stronger (consolidation in favour of the largest players, e.g. Heartland recently bought by Global Payments) and its heavy net debt position makes any major acquisition impossible in the short/medium term (gearing of 212% in FY15 and 158% in FY16e). The management does not intend to get rid of the US; on the contrary, it is investing in integrated payment solutions in this geographical area.
- **No real operating leverage before H2 17.** Regarding Worldpay's investment plan in its technology platforms, the group remains dependent on RBS for the clearing & settlement components (vs. merchant servicing & data applications and clearing & settlement before). The company expects a completion during H1 2017 (vs. our -GBP1.3m and cons. of early 2017 into ou model), as a result its investment program should still weigh in FY17, but to a lesser extent (its total investment plan from 2012 to 2017e should stand at around GBP500m).
- **Lack of FCF generation.** Worldpay generated a positive FCF (GBP32.4m vs. our -GBP1.3m and consensus at -GBP2.1m), however the transformation rate for underlying EBIT into FCF was only 9.5% in FY15 and we expect 25.2% in FY16e, i.e. far from other PSPs (>=50% for European peers).
- **Limited positive impact from its 5.9% stake in Visa Europe (bought by Visa Inc.).** Worldpay's estimated share of these proceeds could be up to GBP930m (EUR1.2bn vs. our est. of EUR1.249bn), breaking down into 45% in cash, 31% in Series B preferred stock in Visa Inc. and 24% in post-transaction earnout. However, as we outlined in our initiation report, only 10% will be retained by Worldpay i.e. up to GBP93m (EUR120m vs. our est. of EUR124.9m) and Bain and Advent will receive 90% (these private equity funds own 42% of Worldpay's share capital). This positive impact is only 1.7% of Worldpay's current market capitalisation (0.8% for the cash part).
- **Does Worldpay really deserve a premium to its peers?** The group is benefiting from a rather resilient organic sales growth (+5.6% in FY15), a strong position in the UK (28% of its FY15 sales; #1 acquirer, with a normative EBITDA margin >15% despite a difficult market). That said, Worldpay still has much to prove since it released a 4th-year of net loss. Worldpay is not a growth story, but rather a story of medium-term margin improvement (via the end to its GBP500m plan to invest in its platforms which should be completed in H1 17e, and the rising share of e-commerce in its mix). When we initiated the coverage (1st February 2016), we already highlighted that, at that time's current price, the share had no margin for error, especially since we expected no EPS upward revisions either to our own figures or those of the consensus for 2016/17e.

VALUATION

- We maintain our **Neutral rating and cut our FV from 290p to 278p** (DCF at 312p, peer comparison at 270p, SOTP at 251p). Despite our far-from-pessimistic estimates, the share is not cheap, even taking into account only EV/EBITDA (it trades at 17.4x in FY16e whereas in our SOTP it deserves 16.1x taking into account a 12.5% premium on the UK part). As a reminder, **Worldpay is above all a physical merchant processor and acquirer in the US and UK** (77% of its FY15 revenue).
- **We advise investors to focus on EV/sales and EV/EBITDA multiples out to 2017e** given that investments in platforms bloat capex and D&A expenses, and therefore bloat EV/EBIT and P/E multiples (same vision for Worldline). We believe it will only be reliable **to reason in PEG once investment in the platforms is complete, namely as of 2018e**. The share is currently trading on an **average premium of 15% to its peers for 2016/17e but it clearly does not deserve any**.

NEXT CATALYSTS

- **AGM:** 10th May, 2016.

It seems essential to us to calculate Worldpay's profitability on: 1/ gross sales and not net sales, which artificially boost its margin rate and make comparison with other European players in the sector inappropriate; **2/ EBITDA reported by the group rather than underlying EBITDA**. Indeed, the numerous negative items that this latter excludes (cost of platform separation, reorganisation, costs linked to acquisitions) should be adjusted for solely at the EBIT level (underlying EBIT). **This is what the group's rivals do and what we have been used to for companies in the sector.**

Revenue and underlying EBITDA breakdown by businesss unit in FY14 and FY15

GBPm	Worldpay US		Worldpay UK		Global eCom		Total	
	2014	2015	2014	2015	2014	2015	2014	2015
Revenue	**1,666.4**	**1,933.7**	**1,229.0**	**1,130.7**	**731.2**	**898.6**	**3,626.6**	**3,963.0**
In % of total revenue	45.9%	48.8%	33.9%	28.5%	20.2%	22.7%	100.0%	100.0%
Y/Y change	*3.2%*	*16.0%*	*8.9%*	*-8.0%*	*15.2%*	*22.9%*	*7.3%*	*9.3%*
Y/Y change (lfl)	*7.1%*	*0.7%*	*8.9%*	*-8.0%*	*15.2%*	*22.9%*	*9.2%*	*5.6%*
Underlying EBITDA[1]	**75.4**	**62.3**	**156.1**	**179.2**	**161.5**	**184.2**	**374.7**	**406.1**
Margin	*4.5%*	*3.2%*	*12.7%*	*15.8%*	*22.1%*	*18.0%*	*10.3%*	*10.2%*

[1] The group does not provide the reported EBITDA margin breakdown.

Sources: Company; Bryan, Garnier & Co.

Main financial items from 2014 to 2017e

GBPm	2014 (reported)	2015 (reported)	vs. BG 2015e	vs. Cons. 2015	BG 2016e (old)	BG 2016e (new)	BG 2017e (old)	BG 2017e (new)
Revenue	**3,626.6**	**3,963.0**	**4,000.0**	**4,005.9**	**4,280.0**	**4,240.4**	**4,622.4**	**4,579.6**
Y/Y change	*7.3%*	*9.3%*	*10.3%*	*10.5%*	*7.0%*	*7.0%*	*8.0%*	*8.0%*
Y/Y change (lfl)	*9.2%*	*5.6%*	*7.0%*	*N/A*	*7.0%*	*7.0%*	*8.0%*	*8.0%*
Net revenue	**863.4**	**981.7**	**974.3**	**972.7**	**1,072.1**	**1,079.6**	**1,179.7**	**1,187.5**
Y/Y change	*7.9%*	*13.7%*	*12.8%*	*12.7%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
EBITDA	**286.1**	**302.4**	**304.0**	**308.7**	**402.3**	**392.2**	**505.7**	**495.5**
Margin	*7.9%*	*7.6%*	*7.6%*	*7.7%*	*9.4%*	*9.3%*	*10.9%*	*10.8%*
Underlying EBITDA	**374.7**	**406.1**	**404.0**	**406.9**	**462.3**	**452.2**	**510.7**	**500.5**
Margin	*10.3%*	*10.2%*	*10.1%*	*10.2%*	*10.8%*	*10.7%*	*11.0%*	*10.9%*
EBIT	**125.0**	**166.9**	**159.0**	**163.7**	**261.1**	**252.3**	**353.2**	**344.4**
Margin	*3.4%*	*4.2%*	*4.0%*	*4.1%*	*6.1%*	*6.0%*	*7.6%*	*7.5%*
Underlying EBIT	**296.3**	**340.5**	**335.0**	**334.7**	**376.6**	**366.8**	**422.5**	**413.1**
Margin	*8.2%*	*8.6%*	*8.4%*	*8.4%*	*8.8%*	*8.7%*	*9.1%*	*9.0%*
Net profit	**-50.0**	**-29.8**	**-14.9**	**-4.9**	**149.5**	**142.6**	**222.6**	**215.6**
Margin	*-1.4%*	*-0.8%*	*-0.4%*	*-0.1%*	*3.5%*	*3.4%*	*4.8%*	*4.7%*
Rest. net profit	**91.7**	**138.4**	**126.1**	**139.2**	**233.8**	**226.2**	**273.9**	**266.4**
Margin	*2.5%*	*3.5%*	*3.2%*	*3.5%*	*5.5%*	*5.3%*	*5.9%*	*5.8%*
EPS (p)	**-3.1**	**-1.8**	**-0.9**	**-0.2**	**7.5**	**7.1**	**11.1**	**10.8**
Fully dil. rest. EPS (p)	**5.7**	**8.2**	**6.3**	**7.0**	**11.7**	**11.3**	**13.7**	**13.3**
FCF	**0.7**	**32.4**	**-1.3**	**-2.1**	**116.5**	**92.3**	**228.6**	**221.4**
FCF/underlying EBIT	*0.2%*	*9.5%*	*-0.3%*	*-0.6%*	*30.9%*	*25.2%*	*54.1%*	*53.6%*
Net debt	**2,254.1**	**1,425.3**	**1,384.3**	**1,389.5**	**1,232.1**	**1,287.2**	**1,044.7**	**1,113.8**
Gearing	*-1,173.4%*	*212.4%*	*200.5%*	*N/A*	*146.7%*	*158.2%*	*101.9%*	*112.1%*

Sources: Company's consensus from 12 analysts (17/02/16); Bryan, Garnier & Co ests.

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