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"Full Year 2015 Financial Results" Conference Call

Thursday 31st March, 17:00 (GR Time)

Conductor:

Antonios Kerastaris, Group CEO,
Giorgos Koliastasis, Group CFO
Nikolaos Pavlakis, Group Tax & Accounting Director &
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Conference Call Conducted by Chorus Call Hellas

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OPERATOR: Good afternoon ladies and gentlemen, this is the Chorus Call Conference operator.

Welcome and thank you for joining Intralot's Full Year 2015 Results Conference Call.

At this time, I would like to turn the conference over to Mr. Elias Athanasiou, Group IR Director.

Sir, please go ahead.

ATHANASIOU E.: Yes, thank you very much. Hello everyone. We would like to welcome you on this conference call to discuss INTRALOT's Fiscal Year 2015 Financial Results. Together with Mr. Kerastaris, our Group CEO, Mr. Koliastasis, our Group CFO and Mr. Pavlakis, our Group Tax & Accounting Director, will briefly review INTRALOT'S financial results and operating achievements for the twelve months ended December 31, 2015. Following the very short presentation, we will be at your disposal for any questions you may have.

I will now pass you over to our CFO.

KOLIASTASIS G.: Thank you very much Ilias. Good afternoon everybody. Welcome to our yearly results presentation.

Going to Slide 3 of our presentation, where we have a brief outcome of our performance of last year, let's go on the top left, the graph depicts the revenue evolution in the last quarters. Fourth quarter Group revenues topped €535 million or 2.2% better off than the same period a year ago, bringing the yearly revenues to €1.9 billion, an improvement of 3.3%. The positive performance of last year going to country by country lever were Italy, Bulgaria and South and Central America's entities, which we managed to fully absorb, the revenue dropped; in Australia driven by the sale of the Victoria license and the Azerbaijan revenue dropped due to the macro effects in the currency and the situation in the country, it's worth to mention that more than 50% of the growth is driven by organic performance.

Adjusting for one-offs, what has happened in the last year on a like-to-like basis, the revenue…the yearly revenue increased by 4.2%? Now if we go on the top right, the graph depicts the evolution of the EBITDA performance. The fourth quarter EBITDA reached €45 million, a 3.5% versus same period a year ago, giving a yearly figure of €177 million which is more or less 1% versus prior year. The three key drivers of the performance versus prior year are the following. One is a decrease in the gross profit margin, in terms of absolute as a natural figure and as a percentage driven by the increased payout ratio by 0.7%, and the loss of the profits from the discontinued businesses.

Secondly, an increase of the OPEX by 3.4% mainly driven by the expansion of U.S., businesses and increased margin on selling investment in the Turkey businesses.

And third, a positive effect of the better of the other revenue line where the key driver in this line is the better instant ticketing performance of the US businesses. On a comparable basis, and mainly excluding the discontinued or new businesses' performance, so making apples to apples, and net of the FX impact, the EBITDA increased on a yearly basis by 13.6%.

Now if we go on the bottom left, the evolution of net income after minority interest, we see there that the figure has a small improvement in Q4 of 2015 compared to the same period of 2014 of around €3 million, bringing however a total yearly figure to minus €65 million compared to close to €50 million in the financial year 2014. The three drivers apart from the EBITDA in this line are the increase of depreciation by close to €11 million, the negative foreign exchange effect of around €7.4 million which partially were counter-balanced by a net interest expense improvement of around €8 million.

The net debt, which is the last…the bottom right graph, shows an improvement in the last quarter of €6.4 million, however giving a full year figure of close to €478 million.

If we see the key elements of the cash flow, we see that operating cash flow excluding the working capital impact and the cash taxes impact was more or less in line compared to same period… to full fiscal year of 2014 close to €134 million. In terms of CAPEX, again the figure are in line with 2014, which is driven…has topped €68 million, driven by investments in new businesses specially in US, product development cost and research and development expenses, which brought a total figure of the net debt on a year-over-year basis to increase by close to €96 million. As at that base, the book value of bonds purchased by the Group were €48 million versus the €6.4 million that we had at December 31, 2014.

The net debt as we discussed earlier, marginally dropped in 4Q, mainly driven by significantly improved cash flow generation in Q4 versus prior quarters.

And I think with this, I am now passing to Ilias for the segmental performance.

ATHANASIOU E.: Thank you very much. Going on to Slide 10 of the presentation, where we present the breakdown per type of contract. License operations contributed 82.5% to our total sales; this was an increase of approximately 5% versus the same period of last year mainly driven by our operations in Jamaica, Italy and Argentina. Management contracts contributed 6.9% to the total turnover, a drop of approximately 5% again this time, driven by the drop off of the Romanian contract in 2014. Technology contributed 10.7% to total sales, a drop of 2.5% again driven by the second contract that we have in Romania.

Going on to the next slide, Slide 11, where we have our revenue per product analysis, sports betting sales increased by 0.6% in the year. It is important to note that Azerbaijan had the lighten performance as George mentioned before. If we exclude the impact of Azerbaijan here the betting sales increased by 6% and this is very important because 2014 was a tough year as a comparison due to the fact that we had…the World Cup took place which always has inflate sales sport betting.

Moving on to numerical games, that grew by almost 9%, the primary drivers here was our operations in the US, Jamaica and Argentina, despite the discontinuation of the Australian numerical games that was sold in early this yea,r early in 2015 namely in February. VLTs, AWPs grew by 10.6% mainly driven by our Italian operations, racing dropped by 11% mainly due to the impact of Azerbaijan. IT products and services dropped by 4.1% mainly due to Romanian and OPAP contracts. The total associated growth to 3.3%.

On the next slide, revenue per product contribution sports betting continues to lead the contribution to our top line with something less than half of our revenue sports 7.2% versus 48.5% of last year. Numerical games is the second largest contribution to our top line with something more than 31%, VLTs 11% and the racing products almost 3%.

Moving on to Slide 13, wagers handled by INTRALOT; Eastern Europe grew by 8%, this is mainly due to the strong performance of Turkey. Western Europe contracted by 5% this is mainly due to Greece. North America increased by 27%, impressive growth due to the new projects that we have incorporated there in the US. South America very strong performance of Peru, Argentina and Jamaica led this region to grow by 30%. Asia mainly driven by Taiwan and Korea grew by 18%, and Africa mainly driven by Morocco grew 15%.

Moving on to the last slide, Slide 14, we handled a total of just over 24 billion of wagers, which is an increase of 12% compared to last year. The biggest contributor being Asia with 7.5 billion followed second by North America 5.7, Europe almost 4 billion.

Eastern Europe almost 4 billion, Western Europe 6 billion, South America 1.15 billion. This is the end of our short term presentation. I will now pass you to our CEO for his comment and we will continue. Mr. Kerastaris, please.

KERASTARIS A.: Good afternoon to everybody from sunny Buenos Aires, please excuse the quality of the line I may have problem receiving your comments but we will manage. Going to the performance of 2015 the numbers that the team has delivered to you confirm our resilience and growth potential in challenging times marked by sustainable revenue and EBITDA growth as long as….. along with a positive free cash flow in the last quarter of the year. This has been a key target for us and being able to achieve it even for a quarter 2015 was for us a significant achievement.

New contracts in the new lands in the U.S., the Netherlands, Morocco, Nigeria and Kenya underscore our ability to sustain and grow our business through select markets across the globe. I'm very happy today to announce that we signed a further extension with a project enhancement in Holland, in the Netherlands until 2019 plus one more year as an option, so this is signed today and announced during this call, and also today we signed an extension of our agreement for Kenya for sports betting to include the markets of Uganda and Tanzania. So this goes to prove that we are putting together a bigger footprint as far as we can, and also extending product offering to our customers.

Going forward, we expect to accelerate revenue and EBITDA growth offered by a healthy pipeline of newcontracts coupled by an operating model that focuses on cash flow generation through a rationalization of our cost base and balancing structure. Overall we remain committed to transforming INTRALOT from a project based company to a product and services joining specialist, and we are amending the strategy we first sat on them and diversify our offering through a combination of gaming competence centers. We have developed during 2015 three new competent centers for technology and innovation in three countries apart from our traditional Greek competent centers.

So we have expanded in Argentina, Philippines and Malta to also cope with the increased throughput that is required for our new product and services, and targeting investments in companies such as Bit8 and it's a acclaimed CRM platform. Secondly we expand our global partnership networking in licensed operations and manage services. Our recent alliance with Gamenet in Italy is the first in a series of potential transactions that seek to balance our footprint, release growth capital and unleash INTRALOT's full potential as a unique player in the global gaming scene. You know my view on how to grow a company. We need to have a focus on the products. We need to have a leaner business model. We need to invest define technology and innovation. We need to be faster in the market and we need to adapt to the needs of our customers. So going forward you will see an INTRALOT with a wider footprint, with better stronger partnerships in the local markets and an appetite to grow. So with this I hand over again to you for your questions and comments.

Q&A

OPERATOR: The first question comes from the line of Needham Chris of Needham Brothers. Please go ahead.

NEEDHAM C.: Hi guys. Nice quarter. I wanted to ask you about free cash flow and the prospects for free cash flow going forward. Would you be able to offer an estimate of what you think maintenance CAPEX might be, other companies sometimes do this in your industry where they separate what has been spent on growth oriented initiatives versus what is being spent on really maintaining the current run rate of the business, is that possible or would you be willing to do that?

KERASTARIS A.: Yes, we have covered this topic also in the past years during the maintenance CAPEX, which means updates, equipment meaning terminals upgrades and replacements and the regular updates of our releases are in the range of €30 million per year. This is based on growth of……..

NEEDHAM C.: Did you say 30??

KERASTARIS A.: 30

NEEDHAM C.: Okay, great.

KERASTARIS A.: The guidance that I have given last year for 2015 and the focus for 2016 is that the total budget will be in the range of 60, which includes all of our growth initiatives and innovation projects, as well as the regular flow of new businesses.. nothing major in terms of a new business going forward. And our performance in 2016 is in that range, slightly higher affected by the new contracts in the United States. So we are within the limits of the guidance that we have given in terms of CAPEX.

NEEDHAM C.: Okay. And…..I'm also wondering about….you have a somewhat unusual structure in terms of the way that the joint ventures are set up as such a big part of the business. It’s unusual I think in this industry or at least from what I can tell and you know, the businesses to have so much of the distributable cash going to minority interests, and I know this is probably done in a way that helps you gain business in these jurisdictions to have local partners, I understand that there is strategic reasons for structuring the business in this way, but I'm wondering how we can kind of get a sense of how free cash flow may start to come back to us as the majority shareholders because I think it is somewhat strange that, you know, as majority owners of these, you know, joint ventures at the minority interest seem to be getting the majority of distributable cash recently.

There was a time where INTRALOT paid cash dividends to its common shareholders and in the last few years you know, most of the…all the dividends have been going to minorities. So I'm just wondering, is this something that you think is…can be changed in the future or is it just, you know, something where you know, we just have to accept that this is the way it's going to be. Because I have, you know, we've seen that there is some kind of uncertainty and unpredictability in the way that cash goes to minorities. You had, I think you explained last year, a strange situation where you know, a lot of the dividends that were due to the Turkish operators were paid in one kind of lump sum, and so it's kind of hard for us to get a sense of how the free cash flow would develop going forward when we don't really have visibility or transparency into those joint venture arrangements in what they are owed. So I'm just wondering is there a way that we can ease out of that going forward or is this just something that we are going to have to learn to deal with?

KERASTARIS A.:: As a business model, and you know, I fully agree with the spirit of your questions, the big picture is that we will continue to grow with partners. In the local markets tax is paid on the profits and dividends are distributed according to the shareholding structure. So if in a country we have a net profit, and net profit is distributed to the shareholders in the form of minorities.

I'm not happy at all with the fact that the parent company is not distributing a divident to the shareholders. Part of the rebalancing and part of the transformation exercise is that at the end of the day we will transform a company that has been good at growing to a company that is also producing tangible returns for its shareholders. And this is a key objective for my team and myself going forward. I fully agree with you the dividend aspect for the parent company should become a key focus area and, you know, my efforts and the efforts of the team are going behind that in changing and going back to the original structure where we had a strong dividend performance. It's not going to happen overnight, it is not going to happen in 2016, but clearly this is a key target for us.

NEEDHAM C.: Okay. And one last thing and then I will jump out. , The Italy transaction where your business in Italy has been basically transferred to Gamenet in exchange for shares and that entity. Would you be able to tell us how much of your overall business that represents, in terms of what percentage of your maybe sales and EBITDA, the Italian business represents?

KERASTARIS A.: Okay. So, in Italy we had the business for nine years where, we were at number 5, in the sports betting market. And we had the small AWP in VLT business. Overall, in terms of the revenue, this represented north of 20% of our overall group revenue. But if we look at the EBITDA performance, it was a very small contribution to the business. Why was that, because in any market, in any industry, the number five player doesn't have the right margins going forward? And the Italian market is a market we have discussed this number of times where consolidation needs to happen, has already started happening. And to be able to have a good chance to compete in a market of €90 billion, because that's the size of the Italian market, yYou need to be a sizeable player. In that context, we decided to merge our business into the Gamenet business and create the number two practically player overall in the Italian market with a pay money that will exceed €1 billion. And the other thing is that both businesses are complementary. So, we did not merger our business into sport betting with another sports betting operator. We made our business with VLT and AWP the number two VLT and AWP operator and Italy.

In that aspect, we are complementing the two businesses; we are complimenting the product offering. We are making full use of a retail network because we are putting the sports betting product into the gaming halls and vice versa, the VLT product into the sports betting outlets, we will continue to have the INTRALOT and Gamenet brand side by side in the market. So, this is a merger that actually creates more synergies both in the top line and the bottom line and creates a sizeable player in the Italian market and our feeling is that 20% of this company has more value for our shareholders than being the number five sports betting operator in Italy. And in that context we made this transaction.

For those of you that do not know Gamenet, Gamenet is a formidable company run by very experienced people and very strong shareholding base. So the Trilantic Capital Fund is a sizable knowledgeable very well established and connected partner. And we see things coming from this partnership as well in the future. So, we feel we have found and we have been selected by the right partners. And I think, strategically, this move will be a significant improvement for our presence in Italy.

NEEDHAM C.: That's good. Yeah, it looks like a smart field, from what I can tell, on the public possibly available numbers on Gamenet. It looks like the company has, you know, substantial EBITDA and owning 20% of that it does, probably, make more sense than keeping 100% of something that is only marginally profitable. So, I think you are probably right, that's a smart deal and…..anyway I congratulate you guys on another quarter. I will step off the line.

KERASTARIS A.: Thanks.

OPERATOR: The next question comes from the line of Bruennler, Jan of Makuri.
Please go ahead.

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Bruennler, J.: Good afternoon. Thanks a lot for the call. I was wondering if you could expand a bit more on your strategy. We have seen under your leadership the investment in product development, the investment in R&D and Bit8 technology and so on. So, it would be good to get to some more color on how we are going to see that being translated into growth and EBITDA, cash generation, which markets are you going to attack, how do you intend to monetize this over the next year or two…?

KERASTARIS A.: Listen, there are some things but I can reveal and obviously some things I cannot reveal. A good example of what we are discussing with the new technology and the new products is being able to expand to the African…Eastern African region with a product that did not exist six months ago. So, we started in Kenya in December 2015. And today, like I told you, we signed expansion of this contract to cover Uganda and Tanzania. Now, mind you, this a market of 160, 170 billion GDP and it's a market that is out of bounds.. out of limits for us, simply because we did not have the product to address this market. So, by creating the right product and creating the right solution for the specific market, we signed an agreement for the specific region that could be a significant, or the plan is that it will be a significant contributor to both our top line and EBITDA. And it's also a market because of the nature of the market where CAPEX is zero. So, it is the kind of agreement that our investors would like because its fast, its very good return, very good margin and you can expand very quickly because of the nature of the product. There we are doing SMS and mobile sports betting.

Again, in the market of 160 and 170 billion of GDP. , Rule of thumb for our business is that our business is in the range of 1.5% to 2% of GDP of any country. So, just to give some figures here on what we are doing that. In the question of rebalancing, because you will see that we are investing in the new products and in the new countries, but, we are also changing the approach, like we did in Italy, of whether we want to be an investor, an operator or a technology provider. The idea is that by reducing power exposure by making a lighter balance sheet,. and at the end of the day by reducing our net debt, because that's the next step for us, we will be able to have a leaner operation and a leaner balance sheet that will allow us to grow faster. And that is the key business driver and I think that, that two or three new things we will announce in the coming weeks, will also, apart from what we announced today, indicate that we are on the right track to achieve just that.

Bruennler, J. Thank you. Now, if we look at your….the existing relationships that you have across the globe in the Americas and in Europe in particular, do you expect to up-sell some of your clients with the new products that you are introducing in content management in mobile gaming for example?

Kerastaris A.:.: That's what we are doing across the globe. So, we are introducing new products in the United States. Recently, we displayed during **ICEe** a new self- service terminal for sports betting, which is unique in the world and this is going on pilot very quickly in one of the markets, which is an addition that not only creates a new game, but it also is a new distribution channel because it's self-service, it's unattended. These are good examples. The whole range of two products that were again launched during **ICE** this February is already finding its way into many of our customers including the Netherlands. So, for us, improving and expanding the product offering base is a key priority.

And investing in technology has helped us to do exactly that.

Bruennler, J All right, that's all from me. Thank you very much.

KERASTARIS A. Thank you again.

OPERATOR: The next question comes from the line of Mr. Draziotis Stamatios of Eurobank Equities. Please go ahead sir.

DRAZIOTIS S.: Yes, hi there. Thank you very much for taking my questions. Just a couple of clarifications if I may please. The first one has to do with what you….with what you mentioned about CAPEX and what you mentioned in the press release that the Gamenet agreement would be the first in a series of potential transactions. I mean does this mean that we should anticipate a pickup of CAPEX in 2016 relative to 2015 because I missed what you said before. And another question would be, with regard to the payout for your license operations, did you say this increased 70 bps in 2016…in 2015, sorry…

KERASTARIS A.: On the CAPEX I said previously, I will repeat the guidance for 2016 is that we will be in the range of €60 million like we were in 2015. On the license operations I am not sure I understand you…I understood your question, so could you please repeat?

DRAZIOTIS S.: I am just wondering basically what the payout was for the license operations, so payout as percent out of license revenues?

KERARSTARIS A.: Payout just to give an indication that payout that we report is the mix of the various payouts in our various operations. So for example in Turkey, the payout is by law determined at 50%. In Italy, that is a competitive market, the payout is north of 80%. So when creating, and I am taking the two extremes, and all of the other countries fall somewhere in between in the 60s and low 70s. So the reported average payout is influenced by the mix of the business. So, it's not that we have one market and we can say there is a payout trend. What we can say and what we see across the world is that our live betting grows and this is the part of sports betting that is growing faster than anything else. Live betting has like-for-like a higher payout compared to a pregame bet. So the more we will see the world growing to live betting this will drive payout higher. That is why the right measure, the right KPI for the performance that we are looking at is the GGR....

DRAZIOTIS S.: And what was the change in GGR in 2015 year-on-year?

KERASTARIS A.: So in 2015, we had….. George you have it.

KOLIASTASIS G.: Yes it is 4.4% increase.

DRAZIOTIS S.: 4.4% higher year-on-year in 2015. Okay, thank you.

OPERATOR: The next question comes from the line of Chang Lisa of Bank of America, Merrill Lynch. Please go ahead.

CHANG L.: Hi, thanks for taking my question. So I want to just follow up on some of the questions other people have asked. With regards to reducing net debt, can you clarify if you have any particular plans whether that's the loans, bonds or and is there a target leverage that you have in mind?

KERASTARIS A.: Giorgo, will you cover that.

KOLIASTASIS G.: Okay. We are currently at 2.7 net debt EBITDA and our plan is to improve it further. It will depend heavily by the forthcoming transactions or the bills that are in the pipeline and as well as the investment in new businesses in the U.S. or other businesses that may come. The intention is to go less than 2.7.

CHANG L.: So you are not going to it is not two times or two and half times or anything very specific.

KOLIASTASIS G.: And…no, no we don't have this target yet.

CHANG L.: Okay and can you clarify, do you have any plans with the balance sheet and/or for example like to keep the RCF as it is or to find a new facility?

KOLIASTASIS G.:.: Okay. Our debt structure currently consist of two high yield bonds in the RCF what we are planning to have…the high yield market was closed for a period of time and was reopened in the last one and half months or so. So, what we are trying to see is we are trying to see how to use the cash balances that we have on our balance sheet plus anticipated cash from potential transactions and profit generation and cash generation in the months to come in order to see which is the best way to go either to capital markets, which currently are relatively expensive versus what we are targeting us or increase our RCF facility. We are in discussions as we speak…..for this.

CHANG L.: Okay, great. And is there a chance that you use proceeds from disposals and just invest it in other businesses and not reduce that?

KERASTARIS A.: What do you meant invest in other businesses?

CHANG L.: You said that we are looking….

COMPANY REPRESENTATIVE: Other businesses that are INTRALOT-related you mean.

CHANG L.: Yes you said investing in new businesses in the U.S.

KERASTARIS A.: We will continue to invest in this business and we will continue to expand both geographically as well as in the product offerings. So this is clear. This said, we would like to have a lower ratio of debt to EBITDA and we would like to have a lighter balance sheet and these are the areas that we are working on you know for the last months and we will continue to work within 2016 and hopefully we will give very strong signals in that direction…that direction very soon.

CHANG L.: Okay, thank you. And then one last question from me. So, a gentleman previously asked how we should think about dividends to minorities is there a way that we can better think about the EBITDA we should attribute to minorities is like there is some adjustments in relation to proportionality.

KERASTARIS A: Giorgo you have that?

KOLIASTASIS G.: The proportionality? I don't have it currently, if I can come back later and give it you.

CHANG L.: Okay, great that's fine. Thank you.

OPERATOR: Gentlemen, Mr. Kerastaris there are no more questions register at this time. You may now proceed with your closing statements. Thank you.

KERASTARIS A.: I would like to thank you very much once again for joining us for the conference call. See you in a couple of months with Q1 results. Thank you again.

KOLIASTASIS G.: Thank you all.