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Research Update:

Greek Gaming Company Intralot S.A. Outlook Revised To Stable On Improved Operating Performance; 'B' Rating Affirmed

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Research Update:

Greek Gaming Company Intralot S.A. Outlook Revised To Stable On Improved Operating Performance; 'B' Rating Affirmed

Overview

- In the 12 months to Dec. 31, 2015, Greece-based gaming company Intralot S.A. reported a 13.6% improvement in like-for-like EBITDA (up 1% including foreign exchange). Its EBITDA margin of 9.3% was slightly lower, but in line with our expectations.
- We see the outlook for 2016 as being supported by the merger of Intralot's Italian operations with Gamenet SpA, Intralot's growth in the important U.S. market, and its shift toward a more asset-light strategy focused on the higher margin technology business.
- We are revising the outlook on Intralot to stable from negative and affirming the 'B' rating on the group.
- The stable outlook reflects our view that Intralot's strategic initiatives in Italy and the U.S. will support meaningful improvement in the EBITDA margin over the next two years, enabling the group to maintain adjusted debt to EBITDA of below 3.5x, and adjusted EBITDA interest coverage of about 3x-4x, on a fully consolidated basis (or less than 5x and about 2x-3x, respectively, on a proportionally consolidated basis).

Rating Action

On April 28, 2016, Standard & Poor's Ratings Services revised to stable from negative its outlook on Greece-based gaming company Intralot S.A. and affirmed its 'B' corporate credit rating on the company.

We also affirmed our 'B' issue ratings on Intralot's senior unsecured notes issued by Intralot Capital Luxembourg S.A. and Intralot Finance Luxembourg S.A.

Rationale

The outlook revision reflects our assessment that the group's operating underperformance in 2014 and the first half of 2015 stabilized in the second half of 2015. Additionally, we believe that Intralot is on course for meaningful improvement during 2016 due to better conditions in key markets and strategic initiatives aimed at shifting toward the higher margin technology business.

In the 12 months to Dec. 31, 2015, Intralot reported a 1% increase in EBITDA

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that masked an underlying 13.6% improvement on a like-for-like basis, which was mostly offset by currency effects. The underlying improvement was most pronounced in the fourth quarter, when underlying EBITDA increased by 8% and reported free operating cash flow (FOCF) turned positive. The performance was supported by a number of contract wins, including in important and mature markets such as the U.S. and the Netherlands. The group's EBITDA margin on a gross revenue basis, which fell markedly in 2014 and the first half of 2015, stabilized in the second half of 2015 and finished the year in line with our expectations, at 9.3%.

Looking ahead, we anticipate a significant improvement in group margins in 2016, boosted firstly by Intralot's alliance with Gamenet SpA in Italy, Europe's largest gaming market, which will take effect in June 2016. The alliance will increase Intralot's margins by giving it a 20% stake in a more profitable combined business, relative to its stand-alone activity, which lacked economies of scale.

Intralot has announced a shift in strategy toward increasing its established, relatively asset-light technology business, which offers platforms for sports betting and lottery systems, and software for gaming machines globally. This business segment offers higher margins than customized technology contracts, with higher barriers to entry and better cash flow generation. In addition, Intralot plans to expand its local partnership network to accelerate growth and enhance the sharing of risk and capital expenditure (capex). If implementation of this strategy is successful, we anticipate that Intralot's credit metrics could sustainably improve over time.

Intralot's business risk profile continues to be supported by its position as a major supplier of integrated gaming systems and services, and its role as a game manager on behalf of third parties, including state-owned operators. The contract-based nature of Intralot's business offers some medium-term visibility on its revenues. The company has largely maintained and gained gaming contracts, which fosters rapid growth, particularly in deregulating markets. We believe Intralot's business risk profile is constrained, however, by its pronounced exposure to emerging markets, as well as to different regulatory and tax systems. Another constraint is the company's lack of scale in large and relatively predictable gaming and lottery markets such as the U.S. and some Western European markets.

Our assessment of Intralot's financial risk profile as aggressive reflects credit metrics that are largely in the significant category. We adjust our assessment downward by one category due to our opinion that not all of the cash flows are available to service debt. This is because some of the cash ultimately belongs to significant minority interests in some of Intralot's subsidiaries.

Our assessment of Intralot's financial risk profile is also based on the company's exposure to foreign exchange risk and its weak discretionary cash flow generation (DCF). We consider these to be a true measure of free cash flow for Intralot, as DCF is measured after deducting significant dividends

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paid to minority interests at the subsidiary level.

In our base case, we assume:

- A recovery in the adjusted EBITDA margin to about 11% in 2016 and about 14% in 2017 as a result of the alliance in Gamenet in Italy, cost reduction initiatives, and increased sales in the technology business.
- A reduction in interest costs from 2016 as a result of the upcoming debt refinancing.
- Capex of about €60 million in 2016 and about €75 million in 2017.
- Dividends to minority interest of about €50 million in 2016 and about €60 million in 2017.

Based on these assumptions, we arrive at the following credit measures:

- Adjusted debt-to-EBITDA of about 3.0x in 2016 and 2017 on a fully consolidated basis (or about 4.7x on a proportionally consolidated basis).
- Adjusted EBITDA interest cover of about 3.0x in 2016 and about 4.0x in 2017 on a fully consolidated basis (or about 2.0x and 2.5x, respectively, on a proportionally consolidated basis).
- Adjusted DCF to debt of below 2% in 2016 and 2017 on a fully consolidated basis.

Liquidity

We assess Intralot's liquidity as less than adequate. Although we estimate that the ratio of sources to uses of funds will remain comfortably above 1.2x in the next 12 months, we view that Intralot's interest coverage covenant headroom will fall to less than 10% due to additional interest payments as part of refinancing expected in 2016.

We estimate Intralot's key sources of liquidity for the next 12 months, starting from March 31 2016, to be:

- Cash on balance sheet of €277 million.
- Cash funds from operations of about €90 million-€100 million;
- Working capital inflow of €25 million-€30 million; and
- No availability under the group's fully drawn €200 million syndicated revolving credit facility, which will expire in May 2017 and is extendable for one additional year.

We estimate Intralot's main liquidity uses over the same period to be:

- €30 million-€35 million of seasonal intra-year working capital requirements;
- Maintenance and long lead time capex of approximately €25 million-€30 million; and
- About €50 million-€60 million of dividends related to minority interests.

Outlook

The stable outlook reflects our view that Intralot's strategic initiatives in Italy and the U.S. will support meaningful improvement in the EBITDA margin over the next two years, enabling the group to maintain adjusted debt to EBITDA of below 3.5x, and adjusted EBITDA interest coverage of about 3x-4x, on

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a fully consolidated basis (or less than 5x and about 2x-3x, respectively, on a proportionally consolidated basis).

Upside scenario

We would consider raising the ratings if Intralot's business risk profile was to materially strengthen, for example if the company was to meaningfully reduce its exposure to emerging markets.

We could also upgrade Intralot if the company generates sustainably positive DCF (meaning FOCF after paying dividends to minority interest partners), resulting in adjusted DCF to debt improving to more 2% on a sustainable basis. Any upgrade would be contingent on Intralot maintaining an adequate liquidity position, including adequate covenant headroom.

Downside scenario

We would consider lowering the ratings if Intralot's operating performance falls materially short of our current expectations, resulting in adjusted debt to EBITDA rising toward 3.5x or EBITDA interest coverage falling below 3x on a fully consolidated basis (or above 5x or below 2x, respectively, on a proportionally consolidated basis).

Ratings Score Snapshot

Corporate Credit Rating: B/Stable/--

Business risk: Weak
- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Weak

Financial risk: Aggressive
- Cash flow/Leverage: Aggressive

Anchor: b+

Modifiers
- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Less-than-Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: b

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Related Criteria

- Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Key Credit Factors For The Leisure And Sports Industry, March 5, 2014
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Intralot S.A.		
Corporate Credit Rating	B/Stable/--	B/Negative/--
Intralot Capital Luxemburg S.A.		
Intralot Finance Luxembourg S.A.		
Senior Unsecured*	B	B

*Guaranteed by Intralot S.A.

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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