

Growth On The Cards For Emerchants

BY JAMES DUNN - 24/06/2015



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The payments arena is one of the most interesting of the financial services sector at the moment, with disruption par for the course. And Australian payments solutions provider Emerchants Limited (EML) is right in the thick of it.

Emerchants provides pre-paid financial card products and services, using its proprietary processing system to offer solutions for reloadable and non-reloadable pre-paid card programs. Initially focusing on the store gift card and loyalty card market, EML has branched out into government payments, non-bank consumer lending and gaming/wagering cards with betting providers, which offer immediate access to funds.

The company was the first card issuer in Australia to be Payment Card Industry Data Security Standard (PCI DSS) accredited, and is the only non-bank processor of BPay payments.

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In November 2013, EML signed a five-year agreement with Queensland's Department of Treasury and Trade to become its preferred supplier of pre-paid card solutions. The deal

includes the option of two consecutive two-year contracts, which could take it to nine years in total. Using pre-paid cards allows the Queensland Treasury and the state government's various departments and agencies to benefit from cost savings, fraud control, and risk control advantages over traditional methods of funds disbursement such as credit cards, cash and cheques. The first pre-paid program rolled out was a Disaster Recovery Card for the Department of Communities, Child Safety and Disabilities Services, allowing it to quickly and efficiently distribute assistance grants during a declared disaster.

In March 2014, EML moved into the betting business, launching the Ladbrokes EFTPOS card. It followed this with card programs for BetStar and Bookmaker.com, and launched the Ladbrokes Visa card program in September 2014. During November 2014, the Group further expanded its market presence with the launch of a prepaid card program with Sportsbet, the largest corporate bookmaker in Australia, and struck multi-year agreements with bet365 and CrownBet. The bet365 and CrownBet programs will be launched in the second half of this year.

Also in September 2014, EML bought British pre-loaded card business Store Financial Services – which was 25%-owned by EML chief executive Tom Cregan, who was not involved in the acquisition decision. Operating in nine European markets, Store is one of Europe's largest shopping mall gift card processors and program managers, with more than 100 programs in place, and is affiliated with Store Financial Systems, the world's largest provider of shopping mall prepaid programs.

The Store acquisition gives Emerchants a platform to launch its reloadable card business into Europe, leveraging Store's established and profitable non-reloadable business. More importantly for EML shareholders, Store's business has been profitable since 2012, and is expected to provide an immediate boost to Emerchants' earnings. In calendar 2015 – that is, the first full 12 months of ownership – Emerchants expects Store to generate revenue of \$8.6 million and contribute \$2.7 million in EBITDA (earnings before interest, tax, depreciation and amortisation) to the group's results.

Store was a significant acquisition, costing Emerchants \$24.9 million – about 40% of its pre-transaction market capitalisation of \$62 million – made up of half cash, and half shares to the vendors, at 50 cents a share. The cash consideration was funded through a \$14 million institutional placement. Market capitalisation has moved to \$111 million.

EML has also signed a three-year agreement with MoneyMe Financial Group and CreditCorp Group, under which Emerchants will provide MoneyMe and CreditCorp with fully reloadable Visa

prepaid debit cards for their small loans customers. The MoneyMe program will also be launched in the second half of 2015.

In October 2014, EML launched a program in October 2014 with CCIG, a franchise operator of 24 Cash Converters stores, under which CCIG uses the company's prepaid cards as the vehicle for paying out loan proceeds. This deal built on a 2012 deal with online consumer lender Nimble, a four-year arrangement under which Nimble uses EML's Visa cards to disburse loan proceeds: Nimble's customers can use the Visa cards to pay bills through BPay, and directly load funds on to their cards through their bank accounts.

Then, in the December quarter, EML struck a relationship with Australian taxi app and mobile payment provider Ingogo. The Group expects that growth to increase in the coming years based on their expansion outside of the Melbourne and Sydney taxi markets.

In the same quarter, Store signed a multi-year agreement with German property developer and shopping mall manager MFI to roll out a gift card program across its 25 shopping malls, replacing an existing paper-based gift voucher system. The MFI program got under way in January 2015, and EML expects it to contribute to earnings in FY16.

EML has also implemented similar programs with Hammerson PLC, which operates 21 malls in the United Kingdom and France – nine of Hammerson's UK malls are using the program – and Value-Retail, which operates eight malls in five European Union markets.

Emerchants is now organised into four "verticals" – Consumer Lending, Gaming and Wagering, Commercial and Non-Reloadable (store and loyalty cards.) The company says the customers signed and launched in the second half of 2014 – Sportsbet, Ladbrokes, Bet 365, CCIG, MoneyMe and Ingogo – will contribute significantly to future earnings, along with strong growth in the Non-Reloadable business, Where EML had previously advised that the Non-Reloadable business would show little growth in FY15, it now expects dollar loads to be \$10 million–\$15 million higher than in FY14, driven by larger programs with companies including Fujitsu, National Australia Bank, Harvey Norman, The Good Guys, Suncorp, Good Food Card and Best Restaurants of Australia card.

Even with most of these business additions in their infancy, the first-half FY15 result showed some impressive improvements. Transactions rose by 88%, driven by a 239% increase in the Australian reloadable business, stored value balances more than tripled, while total dollars loaded rose by 143% (reloadable card stored balances surged by 215%). The number of active accounts rose by 175%.

Total revenue rose by 111%, to \$5.1 million. This allowed EML to show an inaugural positive EBITDA figure for a reporting period, of \$562,000, compared to a \$1.3 million EBITDA loss at December 2013. Gross profit rose by 86% to \$3.75 million, and the net loss improved from a loss of \$2.2 million at December 2013 to a loss of \$430,000 at December 2014.

This half, EML has focused on the launch of its new programs in the Gaming & Wagering and Consumer Lending businesses, which it says will provide further revenue growth in FY16 and beyond. Also, the company says it is getting closer to signing a major deal in the salary packaging business.

Revenue growth is the key to profitability for EML. Revenue is generated largely based on dollar “loads” onto cards. For every dollar loaded on one of its cards, EML generates between three and four cents of revenue. Moreover, EML earns a fee for each transaction on a card, and also earns interest on the stored value on its cards.

The balance sheet is strong: at the half-year, EML had no debt, and cash of \$5.3 million on hand, having raised \$14 million during the half, largely used to fund the Store acquisition.

EML is likely to show an improved FY15 result, but while strong revenue growth and the first 12-month positive EBITDA figure can be expected, bottom-line profit will most likely have to wait another year. The company will start to show the full benefit of revenue from contracts with Sportsbet and CCIG, but the wagering contracts won't be fully mature until the 2015 Spring Racing Carnival, which should provide further momentum. EML expects strong growth in FY16 from the Hammerson, Value-Retail and MFI contracts in Europe. Cash generation should really start to pick-up over FY15 and FY16.

The Emerchants share price has not set the world on fire over the past 12 months – it is up just under 7% – hamstrung by the market's perception of how Apple's planned launch of its own payments service later this year. But Emerchants says Apple will still need the payment schemes (such as Visa and Mastercard) and processors (such as Emerchants) – it sees Apple Pay as an opportunity, not a threat. And the analysts that follow the company seem to concur: on Thomson Reuters numbers, their consensus target price for EML, at \$1.13, is not far off twice the current share price of 62 cents.

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