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## US Sports Betting

## PASPA Overturned: US Sports Betting To Open Up

**The US Supreme Court has ruled that PASPA, the law which prohibits states from legalising sports betting, is unconstitutional.** The Court's judgement states that the legalization "of sports gambling is a controversial subject" that "requires an important policy choice, but the choice is not ours to make." As we wrote in [this note](#), this will allow US sports betting to be adopted on a state-by-state basis, with New Jersey likely to be first within a matter of weeks or months.

**The news is positive for European gambling operators**, opening up a market that could be material in time. However, we note that Gambling Compliance estimates indicate a market size of \$2bn by 2025 (from 21 states), only 3% of the current global sports betting market. In addition, we see potential for an uneven state-by-state regulatory environment to add complication (and cost), as well as taxes, fees to sports leagues, and high initial marketing costs to hold back earnings contributions. Furthermore, we continue to think that land-based interests (casinos, tribal entities, sports venues) will be protected, marginally benefiting US operators like MGM, PENN, BYD (covered by MS analyst Thomas Allen). We continue to see William Hill (rated Equal-weight) and Paddy Power Betfair (rated Underweight) as well positioned to access a growing market, given their existing US businesses (note [here](#)), but we also expect competition from other operators (GVC and 888 also have existing B2B businesses) and suppliers to secure favourable partnerships to be intense. Hence, we would not buy the shares of either on US optionality at current valuations, particularly as both face other issues (weak revenue growth for PPB, UK taxation risk for both). However, we do see the potential for US companies to buy into the European gambling sector (note [here](#)), providing sector-level M&A support.

**Up to 9% upside potential for William Hill, ~6% for Paddy Power Betfair.**

William Hill management has previously estimated that New Jersey could be twice the size of Nevada at maturity (~\$10bn of wagering), and that its Monmouth Park JV could be 10% of the market. This implies ~\$80m of revenue, or \$25m of EBIT (assuming the same high margins as in Nevada). Accounting for the JV this implies £8m income or 4% to PBT, worth ~15p per share on 15x P/E. Looked at another way, using the industry estimates above, if William Hill were to gain 10% market share (comparable with online leaders in the UK) of the \$2bn gross win market, this implies ~£20m of PBT (9%) or 35p per share. On the same basis, £20m would be 6% to Paddy Power Betfair PBT (~£4 per share).

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## Valuation methodologies & risks

### **PPB.L 6800p Underweight**

Our price target of 6800p for Paddy Power Betfair is based on an average of 5 methods. 1) WACC of 9.0% and a terminal growth rate of 3%, implying a 11.1x terminal EV/EBITDA multiple, which gives £72. 2) P/E at 16x, at a slight premium to peers, reflecting its scale benefits and high regulated mix, which gives £62. 3) EV/EBITDA at 12.0x, at a slight premium to peers, reflecting its scale benefits and high regulated mix, which gives £64. 4) FCF yield of 5.5%, in-line with peers, which gives £73. 5) SOTP, using 8x EBITDA for Retail (reflecting smaller, higher quality, higher revenue generating estate than peers) and 13x for Online (reflecting its market leading scale and growth profile) which gives £67. The average of these is £68. Downside risks: increase to UK point of consumption tax; duty rises or operational setbacks in key geographies; technology integration or stability issues; increased cost pressures; further management departures. Upside risks include: faster than expected market share gains in the UK or Australia; regulatory progress that opens up wider markets in the USA, in-play betting in Australia, or newly regulated markets; use of its strong B/S and cash generation for deals or buybacks.

### **WMH.L 325p Equal-weight**

Our Price Target 325p for William Hill is based on the average of three methods. 1. DCF (368p), based on a WACC of 8.7% and terminal growth of 1.2%. 2. P/E SOTP (302p), based on comparable market multiples (9x 2019e for Retail, 16x for Online and USA and 13x for Australia). 3. EV/EBITDA SOTP (297p), based on comparable market multiples, (6x for Retail, 12x for Online and USA, 10x for Australia). Downside risks include: 1/ further deterioration in online revenue growth, 2/ regulatory or duty changes for Machines in Retail, 3/unforeseen cost inflation, 4/ structural pressure in retail, exacerbated by the differential pricing model with more attractive odds online than in shops. Upside risks: 1/ faster than expected growth in Online, 2/ strong cash generation funding dividends and share buybacks, 3/ industry consolidation 4/ accretive acquisitions, 5/ turnaround in Australia.

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(as of April 30, 2018)

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STOCK RATING CATEGORY	COVERAGE UNIVERSE		INVESTMENT BANKING CLIENTS (IBC)			OTHER MATERIAL INVESTMENT SERVICES CLIENTS (MISC)	
	COUNT	% OF TOTAL	COUNT	% OF TOTAL IBC	% OF RATING CATEGORY	COUNT	% OF TOTAL OTHER MISC
<b>Overweight/Buy</b>	<b>1168</b>	<b>38%</b>	<b>305</b>	<b>40%</b>	<b>26%</b>	<b>550</b>	<b>39%</b>
<b>Equal-weight/Hold</b>	<b>1337</b>	<b>43%</b>	<b>371</b>	<b>49%</b>	<b>28%</b>	<b>641</b>	<b>46%</b>
<b>Not-Rated/Hold</b>	<b>53</b>	<b>2%</b>	<b>5</b>	<b>1%</b>	<b>9%</b>	<b>7</b>	<b>0%</b>
<b>Underweight/Sell</b>	<b>539</b>	<b>17%</b>	<b>83</b>	<b>11%</b>	<b>15%</b>	<b>207</b>	<b>15%</b>
<b>TOTAL</b>	<b>3,097</b>		<b>764</b>			<b>1405</b>	

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months. Due to rounding off of decimals, the percentages provided in the "% of total" column may not add up to exactly 100 percent.

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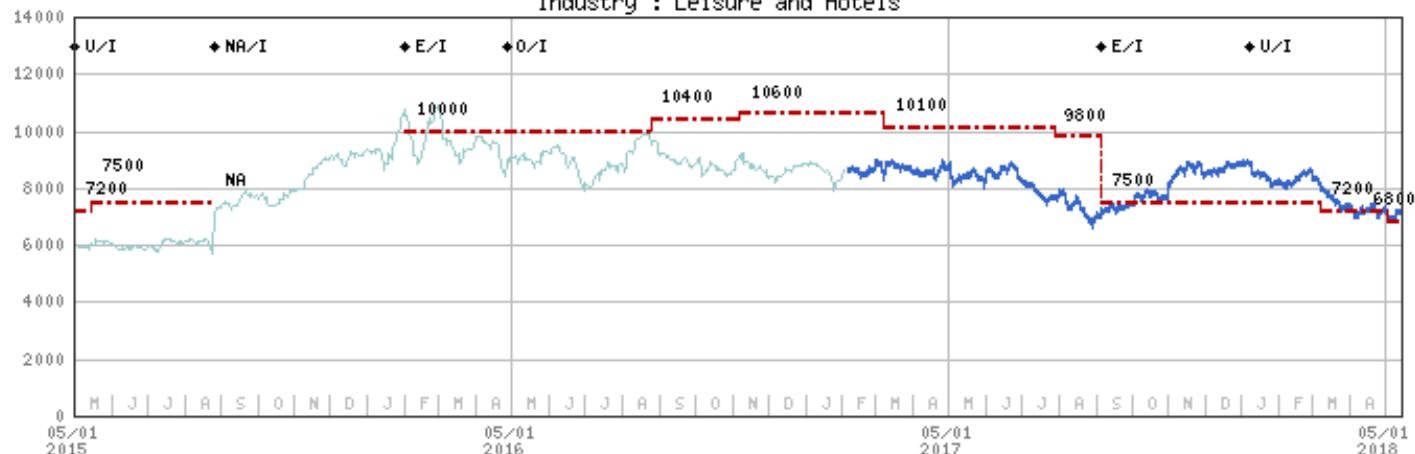
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### Stock Price, Price Target and Rating History (See Rating Definitions)

Paddy Power Betfair Plc (PPB.L) - As of 5/13/18 in GBP  
Industry : Leisure and Hotels



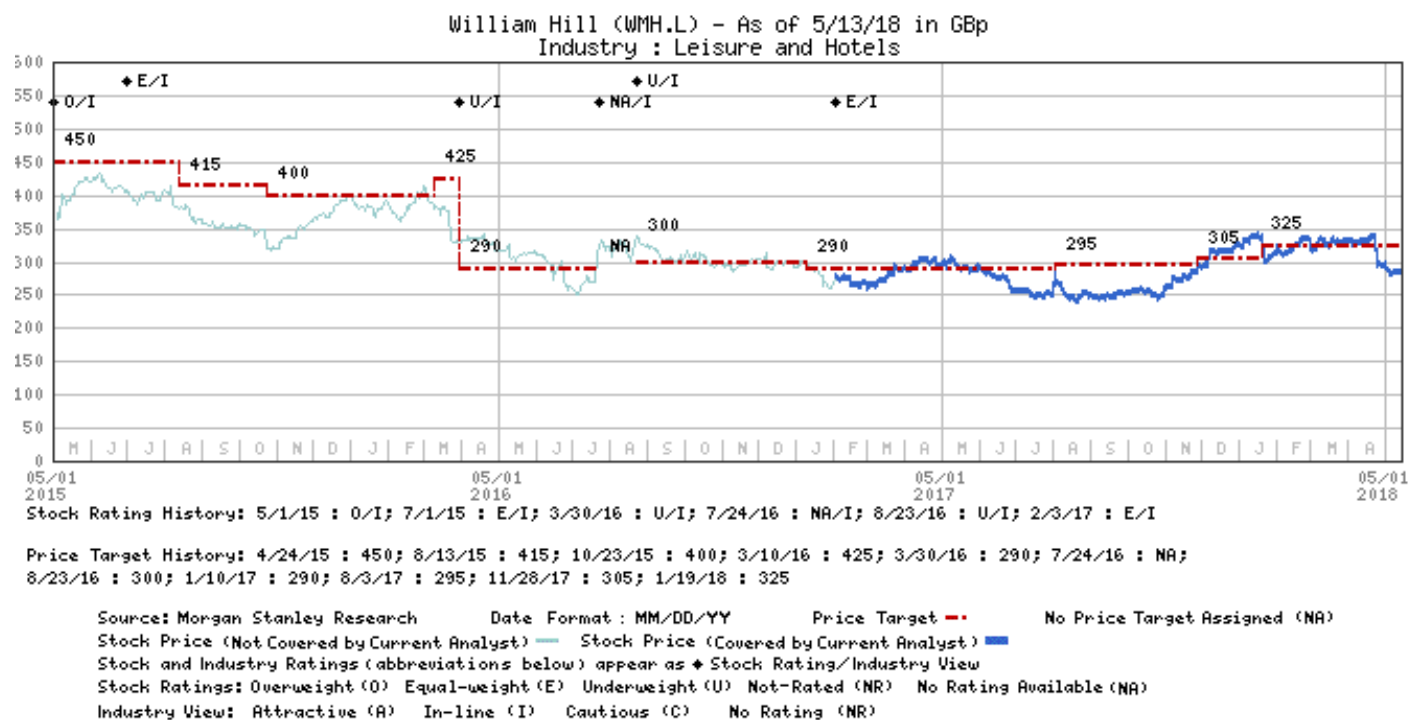
Stock Rating History: 5/1/15 : U/I; 8/26/15 : NA/I; 2/2/16 : E/I; 4/26/16 : O/I; 9/5/17 : E/I; 1/8/18 : U/I

Price Target History: 3/6/15 : 7200; 5/15/15 : 7500; 8/26/15 : NA; 2/2/16 : 10000; 8/25/16 : 10400; 11/7/16 : 10600; 3/8/17 : 10100; 7/28/17 : 9800; 9/5/17 : 7500; 3/8/18 : 7200; 5/3/18 : 6800

Source: Morgan Stanley Research      Date Format : MM/DD/YY      Price Target ---      No Price Target Assigned (NA)  
 Stock Price (Not Covered by Current Analyst) — Stock Price (Covered by Current Analyst) ■  
 Stock and Industry Ratings (abbreviations below) appear as ♦ Stock Rating/Industry View  
 Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)  
 Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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COMPANY (TICKER)	RATING (AS OF)	PRICE* (05/11/2018)
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JD Wetherspoon (JDW.L)	U (01/05/2015)	1,155p
Paddy Power Betfair Plc (PPB.L)	U (01/08/2018)	7,105p
Parques Reunidos (PQR.MC)	O (02/20/2017)	€13.62
Playtech Plc (PTEC.L)	O (07/09/2013)	797p
William Hill (WMH.L)	E (02/03/2017)	283p
<b>Jamie Rollo</b>		
AccorHotels (ACCP.PA)	O (04/04/2017)	€46.45
Basic-Fit NV (BFIT.AS)	O (07/20/2016)	€25.50
Carnival Corp. (CCL.N)	E (12/06/2017)	US\$64.02
Carnival Plc (CCL.L)	E (12/06/2017)	4,828p
Compass Group (CPG.L)	E (04/02/2012)	1,508p
Greene King PLC (GNK.L)	O (03/16/2018)	540p
InterContinental Hotels Group (IHG.L)	E (11/29/2017)	4,768p
Merlin Entertainments (MERL.L)	O (06/13/2014)	374p
Mitchells & Butlers (MAB.L)	E (12/05/2016)	272p
Royal Caribbean Cruises (RCL.N)	E (01/05/2016)	US\$107.06
Scandic Hotels Group AB (SHOTE.ST)	U (01/08/2018)	SKr 85.50
Sodexo SA (EXHO.PA)	U (02/02/2018)	€83.72
SSP Group PLC (SSPG.L)	U (09/05/2017)	650p
Thomas Cook Group (TCG.L)	O (01/08/2018)	136p
TUI (TUIT.L)	E (11/16/2016)	1,766p
TUI AG (TUIGn.DE)	E (11/16/2016)	€20.00
Whitbread (WTB.L)	E (10/25/2017)	4,228p

Stock Ratings are subject to change. Please see latest research for each company.

\* Historical prices are not split adjusted.