Consolidation in the Online Gambling Industry

Martin Oelbermann, Managing Director of MECN, assess the aftermath of the bwin/PartyGaming merger announcement and its potential impact on the wider industry.

On Thursday, July 29, 2010, PartyGaming and bwin finally announced their long expected merger – the first relevant merger among online gambling heavyweights.

The facts

bwin shareholders hold majority

Of the combined entity, approximately 48.4 percent of shares will be owned by PartyGaming shareholders and 51.6 percent by bwin shareholders.

Teufelberger and Ryan will lead company

Norbert Teufelberger and Jim Ryan will be co-CEOs of the combined entity with bwin co-CEO Manfred Bodner joining the board of directors.

€55 million in synergies

The merger is expected to generate synergies totalling €55 million.

Financial figures

Pro-forma 2009 net gaming revenue of €682 million and EBITDA of €196 million were reported before synergies.

Headquarters to be established in Gibraltar

The company's headquarters will be established in Gibraltar. bwin's business locations in Vienna and Stockholm are not under discussion.

Other facts include:

- bwin and PartyGaming brands will be retained.
- Germany is the biggest market – the new company will achieve 25 percent of its combined revenues in Germany.
- The company assumes that about 15 percent of customers are shared by bwin and PartyGaming.
- Both companies have a combined market capitalisation of ca. €3 billion (source: Bloomberg).
- Completion is expected in Q1 2011.

The reasoning

Commenting on the proposed merger, Norbert Teufelberger, Co-Chief Executive of bwin said:

"The timing of this merger is optimal, as the industry is currently going through a phase of consolidation, and size does indeed matter. Europe and the USA are well on the way to regulation. One can achieve more as the market and technology leader, thus assuring our future.

"These two companies are a perfect match. Not only shall we have the first full-house for sportsbetting, poker, casino and games, together, we shall be Number One with respect to product portfolio, technology, development, marketing and customers."

Commenting on the proposed merger, Jim Ryan, Chief Executive of PartyGaming added:

"With market-leading positions in poker, sportsbetting, casino, and games (in particular bingo), the enlarged Group will have a winning formula to exploit the growing online gaming market, supported by a strong balance."

First reactions in the industry

The reactions of the industry were mostly positive. Shares of both bwin and PartyGaming rose around 20 percent in the first days after the merger announcement. Also, the shares of other operators increased (e.g., 888 shares increased by seven percent).

In regards to the most relevant benefits/reasons for the bwin/PartyGaming merger, the surveyed industry experts pointed out foremost that the merger will be helpful in competing in liberalised markets and the obvious reduction of costs (e.g., software/IT licenses, marketing...).

In contrast, the experts do not expect the increased liquidity will help the merged company to compete against poker market leaders such as PokerStars.

In addition, more than 80 percent of the surveyed experts believe that further mergers will significantly hurt the B2B service and technology providers.

Consolidations – a key driver for the future of the online gambling market

In MECN's report "Online Gambling Trends 2010/2011" (www.online-gambling-trends.mecn.net), MECN asked industry insiders to name the key drivers and factors most likely to shape the online gambling industry in the next two to three years. Directly after the increasing number of liberalisations (e.g., France, Denmark) the trend toward consolidation and mergers was ranked the second most relevant industry driver.

Most discussions about consolidation in the industry have been about the 'big guys' getting together – but in reality, there are many more options for consolidations and mergers.

1. Acquisitions to strengthen international portfolio

bwin's acquisition of Gioco Digitale exemplifies survey participants' assessment (see exhibit 2). Developments in the Italian market and probably also in the French market show that local players can capture significant market share in liberalised markets, but many global operators often come too late and then have only one option left – acquisition of local players.

2. Offline and online worlds get together

Strong offline brands that do not yet have a significant online business will have no other option for closing this gap than to acquire existing online operators.

3. State buys private operator – why not?

Only 11 percent of our survey participants believe that acquisitions of private operators by state operators will play a significant role. This might be true for the next two to three years, but if and when state operators turn into large (maybe partially privatised) companies, there is nothing to keep them from spreading their wings and acquiring private operators.

Factors driving consolidation in the online gambling industry

So far, the discussion has mostly focused on consolidation among private operators, but we want to extend it to all major groups in the market:

- private operators and their traditional suppliers
- state/public operators and their traditional suppliers.

In our view, various factors will drive consolidation in the short and medium-term – some of them apply to all groups, some only to selected groups – below are a selection of key drivers:

1. No more boom – instead, maturing markets

Online gambling markets are starting to mature, and only some local 'boom markets' are likely to show the growth figures we saw in the past.

2. The pressure to reduce costs prevails

After the UIGEA was passed, many operators left the US market and had to face a significant drop in revenues. Although operators significantly reduced their organisations, many key operators still have large organisations and platforms that are far from having reached full capacity – therefore, the pressure to reduce costs prevails.

3. Online business affected by scale effects

In online gambling, as in most other online businesses, many cost elements, such as R&D, platforms and marketing are affected by economies of scale. This is equally true on the revenue side, especially for P2P/network models (poker, betting exchanges) – size and liquidity matter.

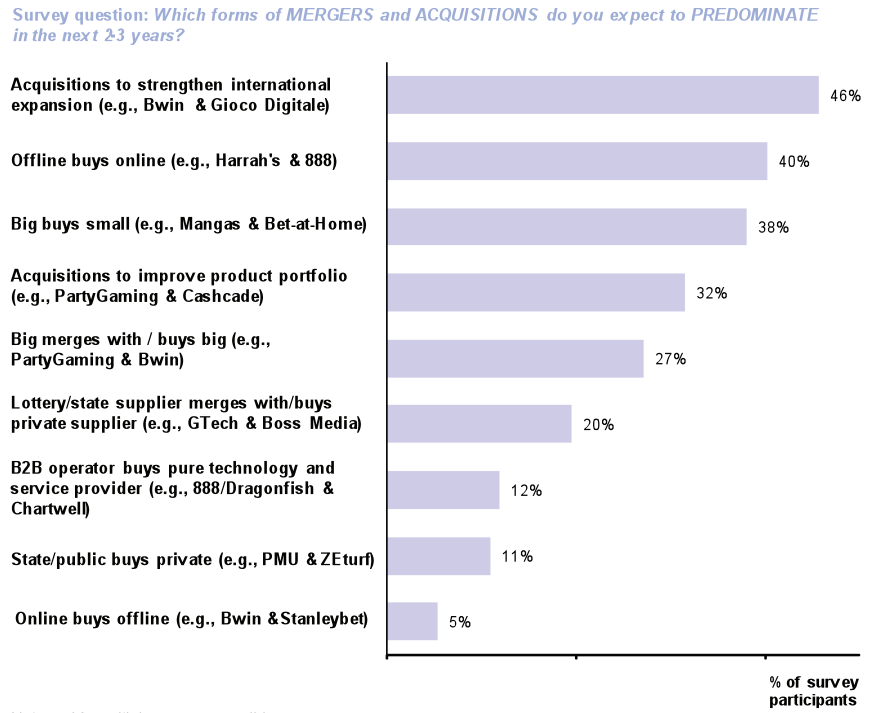
4. Cross-selling is key for most operators

Many online gambling operators extend their product portfolio continuously to offer customers all types of gambling (betting, casino, poker, casual/skill games and bingo) and to keep them on their sites. Although acquisition is not always the cheapest approach to achieve a comprehensive offering for a company's customers, operators must react quickly to market developments and demands rather than lose customers by taking too much time to grow organically.

Exhibit 1: Share development in the first days after the merger

Source: Yahoo

Exhibit 2: Mergers and acquisitions expected to predominate in the next 2-3 years



Note: n=92; multiple answers possible
Source: MECN survey May 2010, MECN report "Online Gambling Trends – 2010/2011"