William Hill PLC
2011 Q1 IMS transcript
20 April 2012

Ralph Topping *- Chief Executive*

Good morning, everybody. Thank you for joining us for this update on our first quarter results. Across the piece, it's a strong performance. Margins have been very good, but there's much more to this story than just that.

Underlying over-the-counter betting continues to be resilient, and machines growth is continuing ahead of new product coming in; something that is, in actual fact, happening right now.

Sportsbook still leads the overall growth story in Online, and we've got more coming in that part of our business.

But I have, of course, said that mobile is a priority for us right now and over the course of the next few years. The good news is that we've been in the App Store since February, and the benefit of that is getting clearer and clearer.

The app has been downloaded 190,000 times, including more than 26,000 downloads on Grand National day alone, and has been consistently among the top performing sports apps. It has brought us many thousands of new customers who have never bet with William Hill before, which shows the benefits of being credible across every channel in our multi-channel offer.

Week 11 this year included three of the four days of Cheltenham. In that week, we saw mobile turnover hit GBP11 million, and sportsbook turnover jumped over the GBP50 million hurdle for the first time ever.

To keep the racing theme going, Online is striding ahead, with sportsbook posting the equivalent of over 80% of over-the-counter stakes in the period. Yes, the margin has been strong, which has benefited net revenue, but we're still getting above 30% growth in stakes, including 370% growth in mobile stakes.

Mobile was almost one-fifth of sportsbook revenues in the period; last year it was 5%.

I know there's always a big focus in Online, but we definitely don't forget how important Retail is to the William Hill business. It's been a resilient OTC performance in quarter 1. Stakes were up if you strip out the effect of bad weather and the comparatives. And it's important to note that that's in spite of a reduced recycling effect of the high margin.

With turnover stability and an improved margin, OTC delivered as much net revenue growth in percentage terms as gaming machines.

I'm pleased to say that turnover on the busiest days, i.e., the weekends and the festivals, tells us our top price trading strategy for the best horses is paying dividends and, in my view, increasing our share of the overall market. And I'm more than confident in the underlying strength of our OTC margin.

You will remember from prelims that I laid out our strategy around products, channels, and international. Well, we've got Storm Plus trialing in 100 shops now, and we'll have it in another 500 shops by the end of the second quarter. In these early stages, we've seen growth rates significantly ahead of the rest of the Inspired estate.

SSBT trials are also out there. We're going to update you on those later in the year.

And, of course, I've already talked about mobile.

On international, the Nevada licensing process is actually progressing well. I know there's been some press coverage on this, which, uncharacteristically, is never as accurate as you would hope, so it's worth remembering it's only 10 months since we submitted our applications. And we are still working to what we were guided to, which was a 12 to 18-month review timeline.

Playtech is required to product a submission to the regulator as a key supplier and partner, which I anticipate will happen imminently.

More widely, we've had a very enjoyable four or five months with Playtech recently. Our discussions continue to be sensible, and there's good recognition on their part that for William Hill the goal has to be having full control of the strategic direction of William Hill Online.

Now, I'm going to hand over to Neil, to cover the numbers off, and then I'll come back for Q&A.

Neil Cooper ***- Group Finance Director***

Thanks, Ralph. I'm sure you've all had a chance to look through the statement so I'll stick to key points, as usual, with a bit of color where I can.

Wagering levels have been positive across the Group in the first quarter; up 31% against a comparative period last year in sportsbook, and up 2% in Retail against the same.

Within Retail, OTC was down 2%, but this shows the effect a couple of weeks bad weather can have on a short period, with 8% fewer racing fixtures in the quarter. Excluding these worst effected weeks from the comparison, OTC stakes were up 0.7%, mostly from increased slippage, with the pence per slip broadly flat. It's a resilient performance.

The favorable year-over-year swing in the gross win margin has been a big feature of the period in both OTC and sportsbook. The biggest swing was driven by football margins, unsurprising to anyone tracking the Premier League and lower league results. We also benefited from a very favorable swing on the Cheltenham Festival, with, in particular, a very strong Gold Cup day.

OTC gross win margin was well above our normalized range at 19.4%; up 1.3 percentage points on the prior year comparative. Notwithstanding this strong quarter, I reiterate that our OTC margin expectations for the year remains in the 17% to 18% range. As you would expect me to point out, we've got plenty of time for the strong first quarter number to even out, despite an excellent Grand National result for the bookmakers.

Looking at Retail as a whole, the OTC staking position, combined with the stronger margin, gave 5% growth in OTC net revenue. Together with 5% growth in gaming machines, we saw 5% net revenue growth overall in Retail. Benefiting from operating leverage, this translated to 8% growth in Retail operating profit.

Gross win per machine per week was GBP918, and for the Inspired portion of the estate was GBP943; up 5%.

Retail operating costs are in line with our full year projections, up 4% year over year, and we're reiterating our guidance for the full year.

The number of shops open at the end of the period was 2,370, and the average for the period was 2,369. So far this year, we've opened four shops and closed five.

In Online, the turnover growth and a very strong 8.8% gross win margin combined to give us a 58% year-over-year increase in sportsbook net revenue. In-play was 43% of turnover, and up year over year 20% in the period, with pre-match up 41%.

In Online, the -- sorry, gaming net revenue was up 19% on the comparative period last year, with the strongest growth in Casino.

Whilst the net revenue decline in Poker looks a little disappointing, overall operating profit from the product is up following changes in the way we manage this product, so we're happy with the overall position.

In total, Online net revenue was up 33%.

Costs in Online were in line with expectation with a 29% expense increase, reflecting both growth in marketing spend and in other expense items.

Our marketing-to-net revenue ratio fell slightly to 26% in the quarter, moderated by our very strong gross win margin. We do, however, reiterate our full-year guidance on this key ratio.

Operating profit was up 29% at GBP38.3 million.

Turning to Telephone, stakes are down, in part, showing the impact of ceasing to take certain high-staking client activity last year. But the margin has improved to 7.3%, and we would typically expect Telephones gross win margin to be around 7%.

Finally, on the balance sheet, our net debt for covenant purposes is reduced by GBP61 million since the year end. I should note that this is likely to be at a lowest point in the reporting cycle this year as we have cash outflows on dividends and our impending US acquisitions ahead of us, as well as our internal forecast adverse working capital movements towards the year end.

Moving onto taxation matters, you'll have seen the announcement relating to Machine Games Duty. At 20%, we would have paid an additional GBP13 million in tax in 2011 to give you some sense of the scale of the impact of this change.

You will also have noted that the Government intend moving forwards with a point of consumption tax, but not until late 2014.

Finally, the corporation tax announcement will reduce our effective tax rate in 2012 by around 3 percentage points, from 20% previously guided to 17%. This is largely as a result of further deferred tax credits. The cash tax rate is less impacted; from 22% to 21%. And we've given the 2013 picture, as well, in the statement.

That's all I wanted to cover, so I'd like now to hand back to Ralph.

Ralph Topping ***- Chief Executive***

Thanks, Neil. So, in summary, it's a strong start to the year; continued good resilience in Retail, over-the-counter, plus growth from machines, good trend still in Online, and a strong mobile growth.

As ever, we don't do current trading in our IMS, but it's fair to say the Grand National result went our way last Saturday.

One final fact for the day, and I'm throwing this in just to give you something to dwell on, on Saturday we were the fourth most downloaded free app across all categories in the App Store.

You'll be familiar with a company called Instagram, which is number three, and they've just been purchased by Facebook for $1 billion.

Thanks for your attention. Now I'd like to hand over to the moderator for questions, and this will be a short question session. Thank you.

QUESTION AND ANSWER

Operator

(Operator Instructions). Vaughan Lewis, Morgan Stanley.

Vaughan Lewis ***- Analyst***

On the Playtech minority, can you just clarify what you said on the discussions there? Are they active discussions on buying that out? And given how well it's doing, William Hill Online, is that becoming more urgent?

Ralph Topping ***- Chief Executive***

What we're doing, we're into the discussion mode with Playtech at the moment, looking at all aspects; ruling nothing out, and ruling nothing in at the moment. Talks are going extremely well. We're extremely cordial. There's lots of ideas coming out of those which, over the fullness of time we'll assess.

Now, the talks we have with Playtech I envisage continuing over the summer. And at some point, in late summer, we'll be back and be confirming what's happening, for sure, at that time. But at the moment, some very good and interesting discussions with Playtech; very cordial.

Vaughan Lewis ***- Analyst***

Thanks for that. And one on OTC, if I can. I think Neil said that pence per slip was flat, so underlying volumes are flat as well. Is that the dynamic you're seeing? And are you seeing growth in football still and slight declines in the other products?

Ralph Topping ***- Chief Executive***

I think you've got to remember that for horseracing this year we had an 8% decline of fixtures year on year.

I think on football business, the football business is across the week, but particularly on Saturdays, and we've had some exceptionally good business on Saturdays. Football punters tend to be week-to-week punters; a big chunk of them are. So we're happy with the margin that we're getting at the moment.

We're seeing good performance in horseracing, and across other products, but on football we've had a margin which is above the normal guidance range.

Vaughan Lewis ***- Analyst***

And just a final one. On your pricing strategy then, do you think the margin is becoming a bit more volatile? Or is Q1 just a bit of a freak period?

Ralph Topping ***- Chief Executive***

Yes, I think, unfortunately, in some respects, because we report on a calendar year, and people get excited with what happens in any particular quarter, or over the full year. I think both in this business we've been feeling confident our guidance, is 17%/18%, is accurate and stands the test of time.

So you'll see it over the course of time as being maintained at 17%/18%, and I don't see any need -- reason to change that at all. Some years it'll be greater than that. Last year it was 16.8%, and this quarter we're up at over 19%. So I think the margin settles down. Hopefully, it'll be up towards the upper end, the 17%/18%, this year, though.

Neil Cooper ***- Group Finance Director***

Vaughan, just to remind you that quarter by quarter we do tend to see a seasonality on the margin, with Q1 and Q4 tending to be higher, because you've got more football and you've got jump racing; whereas Q2/Q3 has, obviously, relatively less football, which is our highest margin OTC product, and flat racing, which is often more predictable than jump racing.

So, if I remind you, you look at 2011 numbers, we did 16.8% for the full year; we did 18.1% in the first quarter. So it's not unusual to see a good, strong margin in Q1. I wouldn't get too carried away thinking that there is a structural change in the shape of the margin.

Vaughan Lewis *- Analyst*

But the more aggressive prices, the best price on best horses sort of thing, that hasn't made it more volatile? You think you're not taking more risk, it's just how it panned out this quarter, you think?

Neil Cooper ***- Group Finance Director***

Well, I think if you -- we're getting into a level of detail that we're probably better off talking about at a half year but, in broad, our mainstream bread and butter, horseracing, the margin shifted by a small degree.

I would remind you we had a very strong Cheltenham in the horseracing sense, versus a relatively weak Cheltenham last year. So you will have seen in horseracing a structural benefit just from that one festival because it's a big festival; it's our second biggest individual event, obviously after the Grand National, on horseracing.

Ralph Topping - ***Chief Executive***

Just on pricing, we've got a very good football compiling team, still reliant on them in this day and age to take a view and have an opinion on football, and we've got a very strong racing team. And at weekends, festivals, big match times, you'll see us sticking our neck out. And it goes for you a lot of the time, and it goes against you some of the time as well.

So, on the whole, it still comes back to the 17%/18% margin; it has no major distorting effect on margin. What it does attract is business, and that's both in Online and in Retail. So we're happy with our trading policy at the moment.

Vaughan Lewis ***- Analyst***

Very clear, thank you.

Operator

Gavin Kelleher, Goodbody Stockbrokers.

Gavin Kelleher - ***Analyst***

Just a couple of questions from me. Just on machines, can you elaborate any further on the significant outperformance of the new Storm Plus machines, in terms of any sort of figures on those, if you can?

And on Online, in Casino, the Playtech product seems to have accelerated in the quarter, the rate of growth versus what we saw last year, is there any particular reasons behind that?

And then you just mentioned --

Ralph Topping ***- Chief Executive***

I know you've got a considerable advantage over me; you've probably had the opportunity to write these questions down. I'm going to just respond to you on machines. We're not going to give you any more information on machines; we'll keep it at the half year. But when we say a significant outperformance we mean a significant out-performance.

On Casino, I think there was going to be some -- on Storm, yes, Storm Plus. I think on Casino there was always going to be some concern about how our performance would be in the first quarter, I think, given the events of last October.

I take great comfort out of the fact that our Casino numbers are growing. We've got a very good team in Israel now, and we're extremely pleased with that performance. But it is seasonal as well, and the first quarter's usually the best quarter in Casino.

Gavin Kelleher ***- Goodbody Stockbrokers - Analyst***

And just maybe one final question. Neil, you mentioned that you'd improved Poker profitability despite the decline in revenue, can you just mention, maybe, what was behind that?

Neil Cooper ***- Group Finance Director***

Yes, simplistically, we've had a number of affiliate-led customers, which obviously require a certain amount of marketing spend to capture, that we're no longer taking. So what you're seeing is you're seeing the loss of net revenue, but equally we don't publish operating profit by product but you would have seen a resulting reduction in marketing spend in Poker as well. So operating profit, net net, is ahead as a result of that.

Gavin Kelleher ***- Goodbody Stockbrokers - Analyst***

Okay, that's great, thanks a million.

Operator

Simon Davies, Canaccord.

Simon Davies ***- Canaccord Genuity - Analyst***

Just on Online, can you give a rough proportion of sportsbook now coming from football, and give a sense of your expectations for the Euros, and how you're going to price the book? Are you going to use them as a marketing tool to bring in additional customers, or are you just going to run it for your usual standard margin?

Ralph Topping ***- Chief Executive***

During the football season, about 40% comes from football on Online. But for the Euro, we're going to [autonomize]. For the Euro, we're not going to tell anybody what we're going to be doing with the Euros at all in case there's a few people listening in to this call. But we're looking forward to the Euros.

The other thing you should remember about this year is there's an Olympic football tournament, and it might be something that if they -- personally, if they don't play David Beckham, I think England's got a good chance of winning that tournament. They've no Scots playing in the British team.

Neil Cooper - ***Group Finance Director***

Yes, we haven't worked out why that is yet, whether it's a policy decision or a talent-based one.

Ralph Topping ***- Chief Executive***

I sit on the FA Board and it's a policy decision, I tell you that.

Simon Davies ***- Canaccord Genuity - Analyst***

Thanks.

Operator

Simon Whittington, UBS.

Simon Whittington ***- UBS - Analyst***

Just two questions, please. Just, firstly, wondering if you could remind us what the typical weighting of Q1 profits is. I seem to remember you saying it's slightly more than a quarter, previously.

Secondly, just wondering if there is anything at all you can say as far as the SSBT roll out is going. Thanks.

Neil Cooper - ***Group Finance Director***

Simon, just to say your recollection is right; it is slightly more than a quarter.

Ralph Topping ***- Chief Executive***

SSBTs are -- we've got a few trials. We've been running a few trials. We're probably down to two now serious contenders for our business. We're pleased with what we're seeing and we'll give you a further update on that in August, I think it is.

Simon Whittington ***- UBS - Analyst***

Okay, thanks a lot.

Operator

James Ainley, Citi.

James Ainley ***- Citigroup - Analyst***

I have a question on in-play. It looks like growth there has slowed quite markedly from 70%-odd last year down to 20%, whereas pre-match betting's held up in terms of growth rates. Could you talk a bit about what's behind that? Thank you.

Ralph Topping ***- Chief Executive***

Yes, in the first quarter last year we had a number of larger staking punters playing in-play who we took on and they haven't been around this year, mainly because of the way we've chosen and managed them. So it's -- I wouldn't read too much into the growth figures; underlying in-play is doing very, very well.

James Ainley ***- Citigroup - Analyst***

Okay, thank you.

Operator

Ed Birkin, Barclays.

Ed Birkin ***- Barclays Capital - Analyst***

Again, two for me. Everyone else seems to have asked two. On the quarterly machines, it's GBP918 you've got for average machine revenues, is that slightly down on Q4? If so, is there any reason for that? Has there been an increase in number of machines you've put across the estate which would have brought that down? Or are we starting to see the gross win --?

Ralph Topping ***- Chief Executive***

It's seasonality. If you look back it's always -- history tells us to expect the same thing, so it is seasonality.

Ed Birkin ***- Barclays Capital - Analyst***

Okay, great. Secondly, on the SSBT, can you tell us what pricing you're using for that? Are you using the normal retail pricing, or are you just using your online pricing?

Ralph Topping *- Chief Executive*

It's retail. What you're seeing, just to give you a wee bit more flavor on it, without giving you too much more detail, since you've been nice enough to only ask two questions, much more in the way of accumulator bets, higher margin bets.

And we're seeing quite a few -- a proportion of our business being on other sports, as well. So that when there's tennis, for instance, which you don't normally see in over-the-counter betting, you're seeing tennis accumulators, football accumulators, and whatever else. So I think it's the old push-button-click propensity that you get with [world] betting as well.

So it's interesting to see. And, as I say, we're down to probably two suppliers now, and we'll have information on that after the end of the half.

Ed Birkin *- Barclays Capital - Analyst*

Thank you very much.

Ralph Topping ***- Chief Executive***

All right, good talking to you.

Operator

Matthew Gerard, Credit Suisse.

Matthew Gerard - Credit Suisse - Analyst

Two, again, from me. Firstly, are we going to see a ramp up in machine density from the current 3.8 through to the end of this year ahead of variable MGD coming in next year?

Ralph Topping - Chief Executive

No, you're not going to see that at all, not in our current thinking, anyway. If you look back over time, our machine density has been the same. We've got the maximum number of machines we think we should have in the estate at this point in time. We reached that conclusion a few years ago.

It [tickles] up, perhaps, with seasonal shops in seaside towns. So if you're going to Cleethorpes, Matt, you might see, where if you've been there in the winter for a weekend and gone back in the summer some of the shops might have three in the winter but four in the summer. So we adjust like that. But it's remarkably static in terms of the percentage, and has been for a few years now, so no surprises from us on density.

Neil Cooper - Group Finance Director

It is fair to say, Matt, that if you replace the fixed cost tax model of AMLD with a variable tax model, at the margins there may be some opportunity. But we're already at 3.8-something, or 3.83, so the upside is fairly minimal; certainly not enough to get excited about, I don't think.

Matthew Gerard - Credit Suisse - Analyst

Okay, thanks. I've not actually been to Cleethorpes, Ralph, so I'll have to check that out.

Ralph Topping - Chief Executive

[It's a size of a box]; there's only room for you and one other guy in it, all right.

Matthew Gerard - Credit Suisse - Analyst

Second question, I had one more.

Neil Cooper - Group Finance Director

I notice you haven't asked him where Cleethorpes is.

Ralph Topping - Chief Executive

Matt's smarter than the average bear, he'll know where that is.

Matthew Gerard - Credit Suisse - Analyst

The second question's also on machines, actually. We've seen now six successive quarters, I think, of the machine gross win growth decelerating down to now 5%, does that in any way concern you? Do you think we're finding a plateau in machines now that we've trended towards for some time?

Ralph Topping - Chief Executive

No, I think we've got upside still to come in the Storm Pluses. And, as I said, think of the full year. We've got some interesting stuff happening with Inspired in terms of further new machine styling, and whatever else.

I'd suspend judgment on that. I'm pretty confident that we're going to see -- we'll see good numbers coming out of machines this week -- this year overall, so I'd suspend judgment at the minute. I'm in the optimistic camp, rather than in the sanguine camp that you seem to be in, Matt.

Matthew Gerard - Credit Suisse - Analyst

Do you think the exceptional OTC gross win margin's taken a bit of steam out of machines in this quarter?

Ralph Topping - Chief Executive

I think if you look at where we are in terms of the operating profit, we've certainly got the cash out of the punters' pockets really effectively. I always look at what the punter's prepared to leave behind from all sources, and we've had a good quarter in machines and OTC.

I still think there's more money in punters' pockets than we ever get at, so I'm remarkably confident on Retail and enjoying the ride on Online at the minute. I don't see any reason to change my optimism, which, as you recall, has been there for about three or four years now.

Matthew Gerard - Credit Suisse - Analyst

I suppose just one follow up on that, your key competitor's obviously started to take more money out of customers' pockets. You're still doing pretty well, together you're over half the industry.

Ralph Topping - Chief Executive

Who is our key competitor, Matt, would you remind me?

Matthew Gerard - Credit Suisse - Analyst

The colors in red from North West London.

Ralph Topping - Chief Executive

Sorry, yes, okay, yes. You can say the name, we won't shy away from it.

Matthew Gerard - Credit Suisse - Analyst

How do you think the independents are doing in UK retail? Do you think the industry's still struggling and the branded operators are moving sharply away from them? Or do you think the industry's recovered?

Ralph Topping - Chief Executive

Listen, I don't spend all my time on the phone to the independent bookmaker in Cleethorpes and ask him if he's struggling or not. He'd probably tell me to go and stick it somewhere that the sun doesn't shine. But my -- I'm only concentrating on the William Hill business. It's actually good to see the industry -- the industry appears to be doing well but I don't go down to the level of consulting with independents as to how they're doing, or whatever.

Neil Cooper - Group Finance Director

Matt, when you look at the Gambling Commission data, we, along with Ladbrokes and Corals and one or two of the other majors and minors, are opening outlets at circa 1% to 2% a year, and yet the number of licenses continues broadly steady. So you can read from that, that the longer term trends are for the bigger branded guys to organically grow and take share off the smaller guys who fall away. That's what the license date would suggest.

Ralph Topping - Chief Executive

I suppose the biggest independent, he still calls himself a independent, is Fred, but you've got to query why he still calls himself an independent with the scary operation he's got. Some very good independent operations out there who are doing well, but there's lots of one and two outlet shops still in the UK. But look at the bigger guys and how they're performing; see how the health of the sector is. I think we're all optimistic on the future and looking for some more deregulation in the sector.

Matthew Gerard - Credit Suisse - Analyst

Okay, thanks guys.

Operator

David Jennings, Davy.

David Jennings - Davy - Analyst

Unfortunately, I only have one question. It relates to the strength of underlying trading in OTC. Because you've reported OTC amount staked down 2%, but clearly the gross win margin is very, very high, and, as such, you've get far less customer recycling on the OTC side. I'm just wondering if you'd hazard a guess as to what amount staked would have been if your gross win margin had been flat year on year.

Ralph Topping - Chief Executive

I think you could do a theoretical calculation on that, which you could do it yourself actually, apply the 17%/18% raise, and in theory over-the-counter turnover would have risen quite substantially. But it is theory.

And as I say, you've just got to take a balanced and measured view of the first quarter. It's been very, very good for us. Underlying gives you confidence, even with an over 19% margin; you're still seeing growth, with 8% less horse racing.

I think I've been saying for a long period of time now that the working man is still going into the bookies, still going into pubs, still determined to enjoy his life, and long may that continue. I'm confident it will continue.

Neil Cooper - Group Finance Director

I think the other way to look at this also is, regardless of your mix between wagering and margin, the final answer is the net revenue that the consumer leaves with you.

Ralph Topping - Chief Executive

Yes, the cash the guy's going to leave behind is the real measure.

Neil Cooper - Group Finance Director

Obviously, we were 5% up on OTC net revenue.

Ralph Topping - Chief Executive

You kind of think turnover, at the end of the day. But if you've got a normal margin, the turnover would increase. I think it all points to the business being in remarkably good health.

David Jennings - Davy - Analyst

Indeed. Thank you very much.

Operator

Jeffrey Harwood, Oriel.

Jeffrey Harwood - Oriel Securities - Analyst

Just a question on the Online business. Can you touch upon the performance outside of the UK? Is there anything worth highlighting there, please?

Neil Cooper - Group Finance Director

Obviously, we've continued to consolidate our position in Italy; we launched a bingo product, and we're getting close to getting our sportsbook product out there.

In terms of other markets, Spain is a market where we've actually been ready to go in on a regulated basis for some while, and that pace is being dictated by the Spanish regulatory authorities as opposed to us. We're kind of champing at the bit a bit to get cracking there.

The bulk of the growth has typically and historically been in the UK, and has continued to be in the UK. So we continue to focus a lot of our efforts on driving our brand in the UK because, when you look at the share of customers we have versus what we think our market share is, we still think that there is mileage to go at the UK. Cost wise, we should be able to access that from a marketing perspective in a more cost effective way.

Jeffrey Harwood - Oriel Securities - Analyst

Sure, okay, thank you.

Ralph Topping - Chief Executive

Thanks, Jeffrey. Last question?

Operator

We've no further question at this time, gentlemen.

Ralph Topping - Chief Executive

Thank you very much. Thanks, everyone, for joining us. As ever, Neil, Lyndsay, and indeed Lili, are available today if you've further questions for us. Have a very good day. Thank you very much.

Operator

Thank you, ladies and gentlemen. This concludes today's conference call. Thank you for participating. You may now disconnect.