Hydra Industries Acquisition Corp.
Acquisition of Inspired Gaming Group
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Company Representatives
Daniel Silvers; Inspired Gaming Group; Chief Strategy Officer
Lorne Weil; Hydra Industries Acquisition Corp.; Chairman and CEO
Luke Alvarez; Inspired Gaming Group; Founder and CEO

Presentation

Operator: Good morning. And welcome to the Hydra Acquisition of Inspired Gaming Group conference call. (Operator Instructions). Please note this event is being recorded.

Now, I'd like to turn the conference over to Mr. Daniel Silvers, Chief Strategy Officer of Inspired Gaming. Please go ahead.

Daniel Silvers: Thank you. As a reminder, this call is being accompanied by a slide presentation, which is available, along with Hydra's press release, in the Investor Information section of our website at www.hydraspac.com. A replay of the call and the accompanying slide presentation will be archived in the Investor Information section of the Hydra website.

Please also refer to the Safe Harbor language on page 2 of the presentation and in today's press release. Certain statements made during this call and in the slide presentation will be considered forward-looking statements under securities laws and the rules of the Securities and Exchange Commission. These statements are based on Hydra's and Inspired's management's current expectations or reasonable beliefs and are subject to risks, uncertainties and changes in circumstances, among other things. Investors should keep in mind that certain of the financial results of Inspired are unaudited and do not conform to SEC regulation S-X.

In addition, a non-GAAP financial measure, EBITDA, has been presented. Accordingly, certain financial information will be presented differently in Hydra's SEC filings relating to the proposed transaction.

I will now turn the call over to Lorne Weil, Chairman and CEO of Hydra.

Lorne Weil: Thanks, Dan. Good morning, everyone. Thank you very much for calling in this morning. This is obviously an exciting moment for us here. A lot of you who are on the call are old friends and investors of ours.

When I retired from Scientific Games, what I think is now clearly for the second and last time, two-and-a-half years or so ago, I had done somewhere between 80 and 100 investor earnings conference calls, and I really did not think that I was ever going to do another one again. But thanks to the wonderful partnership that we and Hydra have had with Macquarie over the course of the last couple of years, I have been dragged kicking and screaming back into the conference call business. And we're looking forward to doing this obviously every quarter, hopefully for as far into the future as we can see right now.

Some of you on the call were on the roadshow that we did a year and a half or so ago, when we did the IPO for Hydra, will remember what we talked about in terms of the ideal merger candidate that we were looking for. So some of those things -- you might recall we were very focused on something with a recurring revenue model. I have always been from the school that in order to grow 15% or 20% a year, it's a lot easier to start next year with everything you had last year, and then you only have to sell 15% more. Businesses where in order to grow 15% you have to sell everything you sold last year all over again this year, and then grow some more, is a very, very, very difficult business model to pursue in the long run. And those of you who follow closely the gaming industry will, of course, understand that.

We were focused on businesses that had predominantly a participation business model. Because in our experience, those tend to be businesses with very high degrees of operating leverage. And so the more you grow your customers' revenue, the more you grow your revenue. And when your revenue grows, your earnings tend to grow more. And as we get deeper into the Inspired story, you'll see the appropriateness of that.

Obviously, we wanted something that had a very strong technology component, because it's something that we understand, that we've been involved with most of our collective careers here. We ideally would like to have taken advantage of the many, many years of experience we've had dealing in government-sponsored gaming. And I think again, as we go through the Inspired story, there is in front of us a tremendous opportunity to utilize that experience and that expertise. We were hoping for something that had a good geographic footprint, ideally in markets like, for example, China, UK, Italy, where we have a lot of experience ourselves and therefore can have something to contribute, and so forth.

So I think -- and we talked about ideally something in gaming. We've looked at dozens and dozens and dozens of opportunities over the course of the last 18 months, many of them not in gaming, a number in gaming. But I think the way the situation has come together with Inspired, we could not -- and I think this is a unanimous view amongst all of us here and with Macquarie -- that we could not possibly have found a more perfect business to align ourselves with and to be in a platform that we go to [a board] with.

If you look at page 3 in the presentation that Dan just told you about -- I'll touch briefly on some of the specific things. As I said, the business has a very stable contract of recurring revenue, as Luke Alvarez will talk about in a minute. Something in excess of 90% of the EBITDA of this business is coming from multiyear recurring revenue contracts, which is a tremendous asset in terms of building a platform going forward.

The core business of Inspired is server-based gaming, a business and activity that many of you are quite familiar with. It's something I myself have had a lot of involvement with over the years, as I think you know. And again, it's a tremendous technology platform to grow from. And there's opportunities, as you see on the slide, in many, many markets.

A few years ago, as Luke will explain in somewhat more detail, Luke and his team were really only able to combine a tremendous capability in virtual videographics with the underlying Inspired software to create a business involving betting on virtual sports. That is growing like crazy, has tremendous margins and is really one of the best businesses, certainly in the gaming realm, I've ever seen.

As we get into the data, you'll see that really all of the growth is coming in the general digital world. And Inspired at this point is a 100% digital multichannel platform. Again, Luke will get into a discussion of that in more detail.

Of very, very great interest to us is the fact that Inspired has a tremendous geographic footprint, certainly in the UK, in continental Europe; a business developing beautifully in China, a very interesting business developing in Latin America, where we've had a lot of experience.

But the one major market, the big enchilada, if you will, is North America, where at least to date there's been relatively little penetration. In a moment, when I talk about some of the financial performance, it's sort of astonishing that the performance has been as outstanding as it is, considering that there's been relatively little participation in what's arguably the biggest individual market in the world. And one of the things that we're not just hoping but intending to do is to make as much use as we can of the experience we've had over the last 20 or 30 years building gaming businesses in North America to rectify the situation.

We love the management team. I've known Luke Alvarez myself for at least 10 years. I've always had enormous admiration and respect for him. I think we will make a tremendous team working together and have him support a really, really, very, very good management team, both in terms of the operating people that are currently in Inspired and a handful of very, very seasoned gaming executives that work in our office here in Hydra and who we expect will be heavily involved in assisting in the development of the business.

We're delighted and enthusiastic about the sponsorship that we have from Vitruvian, who is the current owner of Inspired and has shown a huge vote of confidence in what our plan is in their enthusiasm for continuing to be a major shareholder in the business. And similarly Macquarie, who probably knows more about gaming and has a greater degree of involvement and understanding of gaming than certainly any bank I am familiar with, voting to commit an additional $20 million of their capital to this business. So I think this again is a tremendous vote of confidence.

And all of this put together leads to what we saw, which was really a very impressive track record. And after a great deal of work together, the development of a business plan that is even more exciting and more enthusiastic and more powerful going forward -- much about that Luke will discuss in a minute.

So if we flip now to page 4, this is what I call the money shot. You can see, between fiscal 2013 and fiscal 2016, the EBITDA of the business has been growing at a compound rate of about 16% a year, very, very much faster than, let's say, would be considered the average growth rate of companies in the general gaming technology space; and, in fiscal 2016, based upon the estimates that we have circulated to you, an EBITDA margin of approximately 35%, which again, I think, is very near the top of the heap in terms of profitability.

So we're beginning with a business with great growth momentum, a tremendous level of profitability and a backlog of new opportunities that underlie the accelerating financial performance that is talked about here on page 4.

And with that, I'll now hand it over to Luke, who will explain to you what's underlying this [set projection]. Thank you.

Luke Alvarez: So good morning, everybody. This is Luke Alvarez. I'm Founder and Chief Exec of Inspired. I'm sitting here in New York with Lorne and other members of the Hydra team. And we have certain key members of the Inspired team dialed in from London. And it's very much the synergy of UK technologies and products that we've deployed in the last few years across Europe, combined with Lorne and the Hydra team's expertise, to accelerate our business into North America and other global gaming and lottery markets, which is the sweet spot, and why I personally and my team are excited about this deal.

Staying on slide 4 for the moment -- I'll give you in a moment a kind of breakdown of what's involved in the business. But our historical growth 2013 through to this year, 2016 -- we have our September fiscal year end -- has been driven for us by server-based gaming share gain in the UK, by the rollout of our virtual sports products into certain European markets, particularly Italy; and by the expansion of mobile virtual sports in a number of UK and European markets.

Going forward, in terms of anticipated growth through to 2018, we see continuing mobile expansion. We see server-based gaming deployments into various European markets. And we see the expansion of our virtual sports business into North America. We've not included in this upsides that we have around server-based gaming in North America, China and other mobile markets that we'll come onto.

So turning to slide 5 -- firstly, a brief explanation of fundamentally what it is that this company does. We have a common technology platform, represented by the kind of black rectangle at the center of the circle, which underpins two broad lines of products that we deploy into multiple geographies. Everything that we do in digital, everything that we do is networked and connected.

On the left-hand side are our server-based gaming products. This is where we deploy gaming and lottery terminals into retail venues, usually not resort casinos; usually lottery shops and betting shops and mini-arcades. These are kind of high street, main street endpoints, where the machines look and feel often somewhat like conventional slot machines but are fully networked, intelligent, 21st century devices.

We operate about 25,000 of those devices across the UK, Italy, certain markets in Latin America. We have contracts to deploy a number more into Europe and Latin America and Asia. And our customers there are many of the biggest betting and lottery operators in Europe and the world.

We're the leader in the UK. Our main competitor there and equal market participant is Scientific Games. We're one of the top three in Italy, where we compete with IGT and Megamatic. And we have significant upside opportunities, as we'll talk about.

On the right-hand side is our virtual sports business. This is a category we invented just over 10 years ago. It involves the broadcast of computer-generated sports. We operate now over 15 or so sports -- English football, tennis, bike racing, et cetera, horseracing; and now coming out, US sports such as basketball and so on. And these sports are broadcast into retail betting and lottery venues, and also these days onto people's mobile devices. And in those venues and on those devices, people bet on those sports as if they were betting on a live sport for a real lottery event.

We're live in over 30,000 venues around the world in about 35 countries, 200 regulated gaming and betting websites. And we're the number-one provider worldwide, with over 95% share of all regulated installs.

And mobile is a big growth driver, and you can see some of the big names we operate with there, in the UK, in Europe, in mainland China, and recently in the US, that I'll talk about.

So moving on to slide 6 -- as Lorne explained, our core business model is long-term contracted generally, recurring revenues, on a participation basis. So over 95% of our income is recurring. And the customers we deal with in the UK are very long-term relationships, typically on three- to five-year contracts -- the William Hills, the Betfreds, the Ladbrokeses and so on, left-hand side; and right-hand side, server-based gaming and virtual sports.

More recently, we made a big push into the Italian market, which is the largest gaming market in Europe alongside the UK; and more recently into other markets, particularly mainland China, with the China Sports Lottery and AGTech, which is about to complete as a subsidiary of Alibaba. Also, we work in the Philippines, in Latin America, in the Scandinavian region, in Greece, and in other key markets. And we'll talk more about those. Everywhere we operate, we operate in regulated markets and with the approval and, where required, the licensing of relevant regulatory authorities and global test houses.

So moving on to slide 7 -- the history of Inspired is we founded the business as a technology startup in Central London back in 2002 -- a handful of people, where we developed a mobile entertainment technology platform for distributing games and other entertainment to first-generation GSM SMS devices. Over the subsequent five years, we moved into server-based gaming terminals in venues and, in 2006, acquired the graphics company that forms the kernel together with our own technologies of our virtual sports business.

Between 2006 and 2010, we built up those two businesses such that by 2010 we were the UK leader in server-based gaming terminals and also the UK leader in virtual sports. At that point, around 2010, we signed our very first contracts in mainland China with a state lottery entity and in Italy with the national horseracing entity. And from 2010 to 2015, we substantially internationalized the business. So moved from a UK-only player to a very international player with a strong footprint across a number of European markets in virtual sports, and becoming one of the top two or three leaders in Europe, and indeed now the world, in server-based gaming.

We are now at the key point in the evolution of the business where we are positioned to go from an international player with a substantial UK core to a truly global player. And we think of the business as five years into a 10-year globalization. We have contracts signed in mainland China, our first contracts recently signed in North America, and many others in other markets which we're at the point of beginning to deploy.

So moving on to slide 8 -- I guess the core thesis of the business is that there's a kind of macro super-cycle that we are perfectly positioned to exploit and benefit from. Broadly, on the left-hand side, you can see that over the last 10 years, gaming and lottery -- these are total figures for net sales or net win -- have grown pretty steadily, at a few percent a year. The global market is now approaching $0.5 trillion of net win. But going forward, we think that overall rate will continue.

But our thesis is that the right-hand side, which is the growth of online gaming and lottery, and other forms of digital gaming and lottery, which has grown at a much higher rate -- that that will continue, such that -- our thesis is, in 10 years' time, we'll be in a larger total market that is very substantially digital. And our core positioning is to exploit that growth in digital, that much higher growth rate, as we are an entirely digital business with an entirely digital technology platform.

So moving on to slide 9 -- why do we think digital is happening and will continue and accelerate in our industry? At a high level, of course, it's because fundamentally our industry is a content industry. It's about putting entertainment, adrenalized entertainment, into the hands of players. And every other content industry in the world has been transformed, and is being transformed and disrupted, to the benefit of the digital disruptors by the advent of digital and networks.

We think specifically within our industry, there are four key drivers. Lorne earlier mentioned government adoption, something that he and the Hydra team have a great deal of experience in. We see governments accelerating their regulation and adoption of new digital gaming and lottery. Roughly half the planet in Europe, and at state level in much of the US, governments are struggling with big deficits and needing gaming and lottery taxes to help plug those gaps; and in many emerging markets, such as the Philippines and China and big swathes of Latin America, new middle classes emerging whom governments want to tax and see gaming and lottery as a great way of doing that.

So we've seen new regulation for digital gaming emerge in the five markets listed over the last few years. And we're seeing similar regulation evolve in multiple new countries. And every month, there's news of a new market coming on-stream.

The move to distribute it is important. The first wave of gaming growth worldwide over the last 10 years has mostly been about the growth of big multibillion-dollar resort casinos across North America, into places like Macau and Singapore more recently.

We think the next wave that is happening today is the propagation of a large number of much smaller venues. In many countries, like in mainland China or mainland Brazil, in Colombia and Philippines and so on, there is limited appetite for large numbers of mega resort casinos. The governments are quite happy to have large numbers of small venues with slightly lower state devices.

So distributed gaming, whether it's betting shops, lottery shops, lottery venues, sports bars as we have here in the US, we see as a big expansion. And if your venues are distributed, your technologies and product have to be digital. Because the only way you can support getting games to the endpoint is over a network.

We also see omni-channel or multichannel in the UK, where we have lots of endpoint venues and lots of endpoint devices. We also have enormous growth complementary to that growth in retail endpoints on mobile, and mobile specifically, to the last points, over desktop. In the UK, we've seen levels of adoption of, for example, virtual sports be kind of five to 10 times the level on mobile as we'd seen on desktop. And obviously, worldwide mobile is a huge market, China alone with 600 million smartphones now. So those are the four major drivers of digital adoption that we ride as a company.

Moving on to slide 10 -- the focus of the business today is these two categories, in which we have major sources of competitive advantage and high barriers to entry. On the left-hand side, we talked about our strength in virtual sports, very high market share, 95%; number one globally, obviously, [live] in this vast number of venues. That allows us to invest in the product at much higher levels and innovate new sports versus competitors.

This product is extremely attractive to big lottery operators in the US and in other markets, and also to big gaming operators. Because it's very attractive to millennials in particular and worked both in venues and on smartphones in a way that traditional slot machines are not so attractive to millennials.

Italy's a fantastic case study we launched at the beginning of 2014. And pretty much from a standing start in the first year, we did well over a billion in customer bets, $1 billion. And that's continued consistently since then. And we see multiple Italy-like markets around the world, including many US states.

On the right-hand side, we've talked about our leadership in the UK in server-based gaming, top-three leadership in multiple European markets, and our currently deployed estate. One of the uniques for us as a company is that we have a single server-based gaming technology platform that underlies all our endpoints. We've proven that that is one of the most technically stable and capable in the world's most technically demanding server-based gaming market, which is Italy and the Italian government test regime. And in that market, many of the biggest operators and suppliers in the space -- multibillion-dollar companies that you know well -- failed to make the technologies work, and we succeeded.

We've also had that same technology platform tested and approved by the Chinese Academy of Science for the China lottery market, with GLI-approved and G2S-ready, for the North America market. And that's a big growth opportunity for us.

Moving on to slide 11 -- slide 11 really summarizes the high-level positioning of the business today and vision for the business going forward. Fundamentally, we operate today on an international basis and plan to operate, over the next few years on a global basis, a regulated, compliant global gaming and lottery cloud. We want every device to which we supply content to be networked and connected to our datacenters or to cloud-based datacenters.

We will produce great games and great virtual sports across multiple regulated categories, push those out over the network to devices. Some of those devices will be machines taking cash in lottery and betting venues on high streets around the world. Some of them will be mobile phones and tablets in people's hands and on people's sofas. From our [techs'] point of view, there all [much of a muchness], the vision is a global cloud.

So moving on to slide 12 -- today, with the product footprint we have, which we will over time supplement and enhance with organic product development and with M&A -- today, we have four key products that we think of as a kind of quad play that we aim to deploy into each geographic market. That is retail virtual sports, mobile virtual sports, retail server-based gaming terminals, and mobile versions of the same games we deploy onto our SBG terminals.

In the UK, we deployed all four of those elements of the quad play. In Italy, we've deployed three of them, and we're moving into mobile video lottery this year. In many other markets, we deployed only one, and there's a big opportunity to cross-sell the other three.

So talking now to where the growth will come from, starting on the left-hand side -- in our virtual sports business, we have a large number of existing virtual customers in the UK and other key European jurisdictions. And there's straight organic growth by simply deploying more product and new games into those markets, and helping our customers optimize and increase their deployment of virtual sports.

We sign up every year tens of new customers in new jurisdictions. We will continue to do this. This year for instance, over the course of the last year, we signed up most customers in most of the main Scandinavian regions and a number of Eastern European markets. Going forward, we've just signed our first US customers, and we went live about three weeks ago in Nevada in our first two casino sports books with William Hill. We'll roll out in over 100 venues in Nevada over the course of the next six months and be going live in New Jersey with our first four contracts in the second half of this year. And we think there are big opportunities to sign up customers at US state lottery level, and we have a strong pipeline there. The Hydra transaction clearly helps accelerate us enormously into the US lottery market.

In Asia, we're live today in two provinces with our virtual sports in mainland China with the provincial state sports lotteries. We're also live in the Philippines with one of the regulated concessions. And we think there's big growth in the Philippines, in mainland China obviously, and in new Asian markets as they come on-stream. And mobile is a rapidly accelerating, fast-growing element of our virtual sports business that we see accelerating across Europe over the course of the next year, with big upside in Asia in North America in subsequent years.

On the right-hand side, our core business historically was our UK server-based gaming business. That business continues to grow. We've got over a decade of steady income growth through new content distribution. We will continue to grow that business as well as add terminals in adjacent verticals.

The Italy BLT business continues to grow. We are growing share and have considerable opportunities to do that. We've signed two major contract wins in the last few months and will be adding terminals over the course of the next year.

Greece is a big, new BLT and SBG jurisdiction, which will be coming on-stream, we believe, later this year. We have a contract with the state lottery OPAP to deploy 4,000 terminals alongside IGT and Scientific Games. We expect those to go live towards the end of this year.

We have contracts in multiple other jurisdictions in the European Union, in Latin America and in China; most of which are upside to our plan. And in North America, now we have the G2S, which is the American Gaming Association technical standard for next-generation server-based gaming devices. We believe we have a big upside through Hydra's strengths and relationships to bring on-stream new customers, particularly in the lottery segment. So we're excited about the opportunity to work with Hydra and grow the business on all of these dimensions moving into the next phase of our growth.

Lorne Weil: Great, thanks. This is Lorne again. Thanks, Luke. That was really terrific. I think the essence of the business and what's driving it should be pretty clear after having heard Luke's remarks.

If you could turn to page 13 -- very quickly, as I said when I started my comments, our goal from the beginning of launching the Hydra venture was to align ourselves with a business that had a potential to be a platform from which we could build a really big, really profitable, really exciting business. And I honestly don't think we could've designed a better platform than Inspired's in terms of creating opportunities for us to develop the platform, both organically in ways that Luke talked about as well as by acquisition.

This process of carefully and systematically building on an initial platform through those two avenues of growth is again something myself and our team here have had years of experience doing. During those years of experience, we no doubt made some mistakes. But being individuals who learn from our mistakes, I think we can move forward with this platform focused on the dimensions that the slide talks about and avoid any of the, let's say, missteps we might have had in the past, but fully exploiting all of the understanding we have of what makes a strategy like this work.

We come to it, on the left-hand side, with a strong geographic footprint. Probably the least served, as indicated by the [one check], is the USA and Canada. And needless to say, this is the aspect of the business that we here will be devoting the majority of our time to developing.

Across the bottom, there is a tremendous number of product and/or service areas that we can be combining in various permutations and combinations, generally in the recurring revenue participation business model in each of those geographies. And as Luke discussed in some detail, the real opportunity we see as we go forward is the multichannel or omni-channel opportunity to do this in retail and online and in mobile.

I think it's fair to say that if you look throughout the world at the companies, not just in gaming but in industry in general, who had had the greatest financial success, it seems to be those that are able to intelligently combine both online and offline business activities. Generally, they're more profitable, grow faster, more stable than those businesses that either are just in the online business or just in the offline business.

It's interesting to see even companies like Amazon, which we think of as purely an online company, beginning to develop its own physical retail distribution. Because the synergies between online and offline and the ability to move customers from one channel to the other is so obvious, particularly in a world now where, particularly in gaming, customer acquisition in the online world is so huge. But with a platform of offline business driving the online business, the cost of customer acquisition declines dramatically, and the whole process makes much more sense.

So essentially, this is what we're going to be doing for the next quite some time. We have, I think, a very clear roadmap of where we want to go with the business, both in terms of acquisition ideas that we've already begun to think about as well as a number of significant organic growth opportunities, which Luke discussed in detail.

Turning quickly to page 14 -- we have a team of people who know how to do this. We mention in particular, in addition to myself, Luke, who has done this for very many years; ironically, whose early business experience was with the same consulting firm that my first job out of business school was. And I don't know if that's good or bad, but it's an interesting coincidence nevertheless.

And we're thrilled to have Dan Silvers, who spoke briefly at the beginning of the conference call but will speak again in a moment, who has huge experience in strategy and business development and finance in the gaming industry. Dan and I got to know each other very well when he was at Bear Stearns and was our lead investment banker at Scientific Games. And we did some very, very good things together at that time.

Across the bottom, we've identified the key operating executives in Inspired, again all of whom are as good as it gets at what they do. But what I haven't mentioned here that I think is of equal importance is a similar handful of individuals in our Hydra office here in New York who have had collectively dozens of not hundreds of years of experience in the gaming business and who will be very much involved in the development of the business.

We turn to page 15. As I mentioned early on, the alignment of our objectives with the objectives of our two major shareholders, Vitruvian and Macquarie, I think was very important. And in Vitruvian's case, their decision to choose among a number of options available to them to partner with us is, I think, a tremendous vote of confidence. And the wisdom and experience that they bring to us will be of huge value.

And likewise, Macquarie, as I mentioned before, there's probably no bank in the world that has had the depth of experience and has the depth of understanding of gaming that Macquarie has.

I had been fortunate to have been doing business in one form or another with Macquarie for years. I would not have gone ahead and entered into a partnership with them, had I not had a million percent confidence in their ability and in their commitment. And they've been unbelievably helpful in this process. And obviously, the equity commitment that they're making going forward speaks volumes about their view of the opportunity that we're about to embark upon, because, again, there isn't anybody who understands these things better than they do.

And with that, I'll turn it to Dan now, who will talk about some financial stuff.

Daniel Silvers: Thank you, Lorne. If you flip to slide 16, this slide should give you a good sense for why Hydra is so enthusiastic about this transaction.

As you can see, using the Company's core server-based business as a base for the expected high-growth virtuals business, provides what Hydra believes to be a very attractive growth profile.

Additionally, you'll see that EBITDA margins are indicated to increase by over 1,200 basis points between 2014 and 2018, from 22.3% to 34.4%.

One item that does merit some clarification, if you look at the top left chart, which is labeled revenues, SBG, you'll note what looks to be some downward variability between 2014 and 2016.

Actually, this variability is primarily related to a number of hardware sales which carried zero EBITDA margin at the time. But these sales were undertaken to allow for improved economics to Inspired through the life of the relevant contracts, which is something we expect to be the major beneficiaries of.

If you flip to page 17, you will see an outline of the general terms of the transaction. A few items of note. The Company will be known as Inspired Entertainment and will trade on NASDAQ under the ticker INSE, once it closes.

The implied enterprise value of the transaction -- of the Company pro forma for the transaction is approximately $310 million, plus an earn-out of up to 2.5 million shares at an assumed price of $10 a share.

In no event will the consideration related to the earn-out represent greater than a multiple of 1.3 times the associated EBITDA in the earn-out calculation.

The selling group will retain a really significant equity position here of at least 35% of the Company. And that's something that both we and the sellers are quite excited about. And so we think it's a huge indication of their support.

There will be a seven-member board, of which Lorne and Luke will be two of the members. We expect to put in place a very shareholder-friendly equity incentive plan that has double-trigger vesting tied to stock price performance hurdles.

And finally, the transaction is fully financed with Inspired's existing facilities which mature in 2019.

That said, we do believe there's a meaningful upside available to shareholders through a refinancing of these facilities at rates lower than the current 14% blended rate.

If you turn to slide 18, obviously, there's quite a lot of information on this page, but I'll note a few highlights.

As we've mentioned, Macquarie al be investing $20 million of fresh equity in the deal, and the selling group will be maintaining a very meaningful equity position post-closing.

Pro forma for the deal, and assuming a $10 share price, the implied enterprise value of the Company, again, is approximately $310 million, which represents 6.5 times 2017 projected EBITDA and 5 times 2018 projected EBITDA.

Shortly we'll discuss with you and you'll see that both of these reflect meaningful discounts to what we believe are the relevant comp sets.

Additionally, pro forma leverage will be below 3 times at 2.7 times net to 2016 estimated EBITDA.

As I said earlier, we do believe there's a great opportunity to refinance the existing debt at more attractive levels.

If you flip to slide 19, as I just mentioned, we believe we're creating this company at a meaningful discount to the comps. And that's whether you look at digital games or gaming equipment peers.

However, unlike traditional gaming equipment peers, more than 96% of our revenues are contractually recurring in nature, and we think that that's a very, very important factor as we looked at it from the Hydra perspective.

We expect to evolve to close to a 50/50 mix of virtuals and server-based gaming going forward. And so we've included both sets, such that you can make your own judgments about an appropriate blended multiple for the Company.

If you turn to slide 20, it gives you some key timing info going forward. We expect to file a preliminary proxy statement in the next few weeks. Following finalization of the proxy statement, we will set a date for the shareholder vote, and expect to close very shortly thereafter.

Lorne, I'll turn it back to you to conclude.

Lorne Weil: Thanks, Dan. That was great. I'll conclude on page 21, just to reprise the main ideas that we've discussed so far. And I'll go through this pretty quickly.

What we're excited about is the stable recurring revenues that we've indicated are in excess of 90% of EBITDA. There is terrific core business in server-based gaming, which, thus far, has led to the diversification to virtual sports, which has been wildly successful and I think has the ability to be diversified into a number of other adjacent product and service areas as well.

We're completely sold, based on the experience we've had in the last few years on the notion of the importance of multi-channel or omni-channel platform. We obviously really like the fact that there's an enormous, relatively untapped market opportunity in North America.

I think we have the makings of a tremendous partnership. Again, as I said before, Luke and I have known each other for many years. We have been working together extremely well and synergistically in building the plan that we presented to you this morning. And I have every expectation that that will continue into the future.

Obviously, we're very glad to have the support that we do from Vitruvian and Macquarie. And we're starting off with tremendous revenue and EBITDA margin momentum.

One of the things we had said when we sat out on this path, again, with Macquarie is, we don't mind repair jobs, we like repair jobs, but repair job was not going to be our first shot out of the box. That whatever we started with was going to be already performing beautifully and in a way that if there, indeed, was an opportunity to then take on something that required some fixing and some turning around, we're very happy to do that, knowing that we have the strength of the core business behind us.

So that wraps up our prepared comments. And I know we've been on the phone for a long time, and I apologize for the length. But I think there was a lot of very important things to talk about, at least once, and we've had an opportunity to do that.

But now if there are any questions, we're happy to answer them. So, Operator, if you can put us in Q&A mode, please.

Questions and Answers

Operator: Okay. Thank you. We'll now begin the question-and-answer session. (Operator Instructions) At this time, we will pause to assemble our roster. Todd Eilers.

Todd Eilers: Congratulations on the deal. Wanted to ask a question, on slide 16, you guys have some projections broken down on the terminal side and the virtual sports side. Was kind of curious to get maybe a little bit more color on kind of growth projections.

On the terminal side, it looks like you guys have a nice step-up there in revenue in 2017 and 2018. And was wondering if you can maybe elaborate a little bit more on kind of what markets and products you kind of see driving that.

Luke Alvarez: So, Todd, this is Luke. I mean, some of that is simply ongoing organic growth. In the UK, kind of income per units, obviously, we're on our participation and we see steady low single-digit growth continuing in the UK. Actually, this year we're quite a long way ahead of that.

Obviously, a major component is our existing European market. So we've recently won a couple of important contracts in Italy, which we actually haven't announced, but which we'll be deploying a few thousand extra end points, largely CapEx free over the next 18 months. And, of course, we've also [assumed] in there at some points that the Greece project on the G2SSBG platform begins to deploy. And we have announced the contract win there a year or so ago. We've got about 4,000 terminals to deploy, with upside.

So those are the principal components on the SBG side.

Todd Eilers: Okay. Perfect. And then also had a question, Lorne and Luke, you guys mentioned the North America, or I guess Lorne mentioned the North America kind of untapped opportunity.

Was wondering if you could talk a little bit more about where specifically kind of you see the opportunity in North America. Is it more on the virtual side? Is it more on the server-based gaming side? How should we kind of think about that going forward in terms of opportunity?

Lorne Weil: Sure. I think actually the opportunities are in both server-based gaming and virtual sports in both United States and Canada, actually as well in Mexico, where we think there's a terrific opportunity. And in both in the, if we're oversimplifying in the gaming world and in, let's say the lottery or the government-sponsored world, I think you and I have talked in the past that my view has been that the next great frontier in the, let's call it the gaming business in North America, was in the government-sponsored lottery, if you will, space, moving from a model, as Luke talked about, where a state has a few very large casinos into models where there will be very widely distributed gaming and in a way that utilizes Inspired's technology, almost ideally.

You may have seen recently, for example, Pennsylvania is at least circulating legislation that would bring into effect precisely that model. And I think that over the next few years, we'll see in both US and Canada, both in terms of new opportunities and replacement of existing wide area distributed system, simply because the server-based gaming approach to doing that is so much more cost effective and typically generates so much higher revenue per any denominator you choose to look at.

So we see great opportunity in the Americas for server-based gaming. And I should mention that there's really nothing for that opportunity reflected in the projections that Luke gave you.

I think you know from our experience together, we typically never include in guidance or projections revenue from contracts that we don't have. And so we see this as a big upside.

As far as virtual sports, there again, we see that opportunity both on the gaming side and on the lottery side.

On the gaming side, as Luke mentioned, we have recently, very recently, signed agreements in Nevada and in Atlantic City to put virtual sports in casinos, ideally as probably in the race book environment, or race and sports book environment. And we see the opportunity to do that in many more gaming venues as a big opportunity.

And likewise, in lottery. And again, this is something you and I have discussed over the years a number of times. The lottery world has been waiting for something new that's more interesting and more exciting than ping-pong balls popping out of a hopper. And at least as been proven in the UK and China and in multiple locations around the world, people are very, very enthusiastic and very, very excited about watching a virtual soccer game or a virtual basketball game or a virtual Formula 1 car race.

And in case you're a -- it's too bad this isn't a webcast, Todd, because then we could actually show some live videos.

But like I have a kid who basically spends half his life playing soccer and the other half playing FIFA on TV. And when I watch him play FIFA, I really think I'm watching a real soccer game. I can't believe that a guy that looks like Ronaldo is actually not Ronaldo.

And I can tell you that the Inspired graphics are even better than the FIFA graphics. So when these players are watching these virtual sports games and betting on it, it's fascinating and exciting, and I think has the potential to be a phenomenal lottery game in the states and one which is easily accommodated by all of the lottery rules and regulations that are currently in place in the US and Canada.

Todd Eilers: All right. Great. Thanks a lot. Really appreciate the thoughts. And again, congrats on the deal announcement, guys.

Lorne Weil: And thank you for calling, Todd. We really appreciate that.

Operator: Mark Heiman.

Mark Heiman: Congrats on the deal. I think it looks very interesting. Just a few questions. I'm guessing some of this will be in what you file later.

The first is, where is the Company going to be domiciled?

Lorne Weil: It will be a Delaware corporation, as Hydra is. Luke, obviously, is based in London, but really based everywhere because he spends most of his time on the road at Gibraltar --

Mark Heiman: So for tax purposes, it's a US corporation?

Lorne Weil: Hydra will become Inspired Entertainment, and, yes, it will remain a Delaware corporation.

Mark Heiman: Okay. Got you. And then just some other questions. As far as the voting and control goes, what type of, I guess kind of protections would there be in terms of minority shareholder rights going forward? Obviously, there's two seats from Hydra, but, obviously, the original owner still controls the majority of those.

Daniel Silvers: I'm sorry. I didn't fully hear what you said at the end.

Mark Heiman: So are there any voting agreements in place or standstill agreements in place? I mean, for instance, if Vitruvian wanted to take over the rest of the Company, et cetera, they're already at 35%.

Daniel Silvers: There are certain shareholder agreements in place. We will be filing an 8K later today that has the SPA and the associated material documents.

And so it probably makes sense to get those filed. And then, obviously, we're happy to talk offline if you have specific questions as you go through them.

Lorne Weil: But just to add to that, though, and I think I'm correct in saying this, and Luke is the most familiar and, obviously, has and has had for years the closest relationship with Vitruvian.

But on the issue of Vitruvian taking the business over, the investment in Inspired, I believe, would have been Vitruvian's first fund, Luke?

Luke Alvarez: That's right.

Lorne Weil: And Vitruvian is now on their third fund. And I think the mechanics and the governance within Vitruvian is what has led to the deals that they've done with us in terms of reducing their investment in their first fund. And I think the notion that one of the later funds would be used to take over a company that had been owned in an earlier fund, I think is something that they probably can't do, can't mechanically or from a governance point of view.

Mark Heiman: Right. Right. Well, that was exactly my last question, which was going to be, was their decision to sell two-thirds of it based on the fact that a fund was maturing and a need for liquidity?

Lorne Weil: Yes.

Mark Heiman: Sounds like the answer to that --

Lorne Weil: Right.

Mark Heiman: -- question is yes. Okay. Great. That's really helpful. And then going back to the actual business. What type of capital, CapEx requirements are needed here [in year]? I assume that with installations I think you'd made reference to, there's some capital --

Luke Alvarez: So, I mean, in general, as a matter of principle, our server-based gaming contracts in the UK are mostly, though not always, CapEx'd by us. So periodically, typically every five years we need to refresh the machine state.

We will have some of that in relatively small quantums back end of 2017, early 2018, but no major replacement activity really, until 2020.

In other markets, I mean, we did CapEx for the first phase of growth in Italy, although, the recent contract wins I've mentioned will be CapEx largely by the customers. There will be some maintenance CapEx of some of the existing clients in Italy in late 2017 and 2018, again.

But the big new opportunities, I mean, obviously Greece, Greece is CapEx'd, although extremely efficiently, and the big Chinese opportunities and so on are entirely CapEx'd by the operating customer.

On the virtual sport side of the business, mobile side of the business, which is the higher growth part of the business in the plan you've seen, the [guidance] you've seen, that's entirely CapEx free, very high margin, very cash generative, even as it grows at a fantastic rate.

So we are investing in the business and have been over the last two or three years in product and software development. So that gives us significant upsides as those products go live in markets like China or SBG, new mobile products, and new virtual sports games for North America.

Daniel Silvers: So just to put a couple numbers to it, our 2016 CapEx budget is $29.4 million. But of that, only $7.4 million of that relates to core business, essentially machine CapEx. The rest is funds for investment in new opportunities and growth.

And I would say where we believe the business is going, as Luke alluded to on the virtual side, most of the growth is likely to come through less capital-intensive business. And so as we go forward, we expect our capital requirements as [apportioned] to the size of the business to decrease over time.

Mark Heiman: No, that absolutely makes sense. Guys, thanks so much again for taking all my varied questions. And congratulations again.

Daniel Silvers: Thank you.

Operator: Eyal Ofir.

Eyal Ofir: Eyal here with Dundee Capital. Just a quick question to follow up on the CapEx back and forth you just had. How should we think about this from a revenue recognition standpoint? Does the stuff in China, is that going to be kind of recognized up front or is that going to be a recurring component?

And then, in terms of when you talk about CapEx especially out of Greece and some other markets, but what's your return on investment in terms of from CapEx to getting back the capital? Like how long does it take you?

Daniel Silvers: You want me to handle the rev rec, and then you can -- so obviously, historically the Company has reported on UK GAAP, as we will be reporting on US GAAP. And obviously, each deal is different. And so the rev rec will depend on each deal.

But I think what is likely to happen over time is that you will see more -- the rev rec will better match the actual sort of over time performance to reflect the recurring revenue nature of the business.

And so we believe US GAAP, which we will be reporting in, accurately reflects the underlying economics of the transactions.

Luke Alvarez: And to be clear, I mean, for the figures quoted on slide 16, for this historic period and FY16, the US GAAP revenue is in excess of 95% recurring. In terms of business model, as I said, the fundamental business model is contracted participation, recurring revenues.

So as we move into markets like China and North America virtuals and so on, we expect that business model to continue.

Eyal Ofir: Okay.

Lorne Weil: But just another point, completely clear, I think Dan and Luke both addressed it, but I want to be sure you understand this, because it's extremely important. That under UK GAAP, if a server-based gaming contract is entered into, let's say it's a five-year contract and there was, just to make the math simple, a $5 million software license sold to the customer up front, and then a recurring revenue stream over the next five years, in UK GAAP, as long as that software license was paid for, that $5 million software license sale can be included, is included, in revenue and EBITDA in the income in the year in which it was done.

According to US GAAP, we can't do that. So if there is a sale of or there's a server-based gaming contract or, for that matter, a virtual sports contract, where there's a significant upfront payment for a software license, that upfront payment must be amortized over the life of the contract.

If we had showed you the numbers that are on page 16 in UK GAAP, they would be significantly higher than the numbers that we're showing here, which we have restated into US GAAP.

Of course, the converse of that is we will now have in future years the benefit in EBITDA of the amortization of the upfront software fees that we otherwise have excluded from income.

Eyal Ofir: Okay.

Lorne Weil: So what's being presented here and the way we will be presenting financial statements going forward will be as conservative as we can.

Obviously, if the software license is paid for, even if we haven't accounted for it as revenue in the P&L, we will have the cash on the balance sheet, and that cash can be used to finance the CapEx that might otherwise be needed in the contract.

And generally, I think that's how we see most of what we're going to be doing going forward.

Eyal Ofir: Okay. So there'll be a [tail] no matter what, so you'll have a significant --

Lorne Weil: Absolutely.

Eyal Ofir: -- and recurring revenue? Perfect.

Lorne Weil: Well, there'll be two tails. There'll be the tail of the amortization of any upfront license sales over the life of the contract, and, hopefully even more importantly, the recurring participation that we will have in the revenue generated for the customer by the system itself.

Eyal Ofir: Okay. And in terms of the return on investment from the Inspired side of the equation, like how long did it take you guys to recoup the capital you deploy on these machines? Is it six months? twelve months?

Luke Alvarez: It depends on the contract and so on. I mean, typically, [if we sign] on a machine, we'll sign a five-year contract, and we aim to get our money back in about 18 months. But there is movement either side of that. And, clearly, that also correlates to contract length.

As we said, on the virtual sports side, there's very little CapEx. And what CapEx there is is mostly production software development.

Eyal Ofir: Okay.

Luke Alvarez: (Inaudible) capitalization and so on.

Eyal Ofir: Okay. Great. And then before I pass the line, just one last question for you guys. Obviously M&A seems to be a theme going forward for both, from Lorne's background and also the Inspired side.

Is there any specific areas you guys want to focus on in the future in terms of adding capability, we should think about?

Luke Alvarez: I mean, look, I think we can refer you back to that three-dimensional grid that Lorne talked to around M&A. There are gaps on that grid. We would certainly aim to fill out some of those product gaps. There's also [like really] a geographic gap around North America, which Hydra helps with enormously, but we may choose to add footprint there.

So there are obvious opportunities around filling out the grid. And I think broadly that will guide our strategy.

Eyal Ofir: Okay, great. Thanks. I'll pass the line. Congratulations again.

Lorne Weil: Thank you.

Operator: (Operator Instructions) [Artham Fulkham].

Artham Fulkham: Congratulations on the transaction. I was curious about the financing. So you'll be having a loan which has a rate of 14%, which includes 4% PIK. And based on everything what you describe to us about the business and the (inaudible), this seems to be an extremely high rate.

So I was wondering who provides that loan? Why do you need such a high rate? And whether the provider of the loan is [Maguire].

Lorne Weil: Sure. So that loan is, there's a revolver provided by Lloyds and there's a term loan provided by [Aries]. Those were existing debt facilities within the Inspired structure, which we got extended out to 2019, as part of this transaction.

That said, they are prepayable. We agree, we would hope that we could, in short order, refinance those at rates inside of the 14% blended cost of capital. And we believe that there's tremendous upside to shareholders when we do that. And I think it's fair to say that we are focused on that.

Luke Alvarez: I mean think about it as the very first generation of those loans were put in place in 2010 on the Vitruvian acquisition. They're kind of historic relationships. Clearly, we had a lot of other stuff to be focused on in making the transaction happen and we have significant opportunities to grow the business through M&A going forward.

So [there'll be] opportunities to refinance in short order.

Daniel Silvers: And just order of magnitude, right, it's roughly a little over $100 million, $110 million on a converted basis, because they are pound denominated. Every one point reduction in interest expense -- in rate is like a million bucks of incremental [free] cash. So we are focused on that.

We think it's a great opportunity from the Company and shareholders to benefit from a refinancing of that debt, and we're focused on it.

Artham Fulkham: Got it. Awesome. Thank you for the color. A quick question about how do you treat any software development expenses and things like that? Do you expense everything in the current period or do you capitalize?

Luke Alvarez: So we distinguish between software development that's kind of in support of current customer activities to sustain current levels of income, which we expense, and software development that's about developing new products and technologies for new markets that will expand incomes.

That latter is capitalized as treated as own labor capitalization. A large percentage of that quantum of known machine CapEx that Dan quoted earlier is only by capitalization.

Artham Fulkham: Okay. And when you quote your EBITDA numbers, if you were to treat those expenses which you capitalize as far as the software development goes, in that case, how much your EBITDA will go down?

Daniel Silvers: You know what? We obviously haven't put that out in the public. Let us -- and certainly not a breakout of that incremental $22 million that's non-core capital. And so I think at this time it's probably not the right time to go into that level of granularity on this call.

Artham Fulkham: Well, guys, it's obviously up to you. Just from the investors' perspective, [when you] know our numbers would show a very high EBITDA and very low acquisition multiple. And then when you find out, there's actually significant chunk of that would have been expensed or would be expensed in their models by analysts. That obviously raises questions from people who (inaudible) on the transaction and decide between redemption or sticking around.

So it's important. I understand that now may be not appropriate time for you to disclose it. But I hope you will take this into account and preferably (inaudible) at some point.

Luke Alvarez: But also, I think it's important that you understand the kind of core thesis here. I mean, we talked about the business being 5 years into a 10-year globalization. We've gone through a process of going from UK only to substantially international, present in two or three other markets quite materially, with a number of contracts signed in additional markets, like North America or China, which are generating minimal to no income as of today, but will start to generate income over the next couple of years.

As part of that, we have increased our development in software and product innovation to service those new markets. Fundamentally, we want investors who are flying into the thesis that Inspired and Hydra in combination can take this business and over next five years turn it from an international into a truly global player, both organically and through M&A. And our investment is part of that process.

Lorne Weil: It's Lorne Weil speaking. This issue that you're talking about is obviously a very important one. But by the time the proxy is mailed to the shareholders with plenty of notice to make your decisions either about voting in favor of the deal or whether or not they choose to redeem, this question that you're asking will be addressed in great detail.

One of the things we're obviously doing is very, very, very carefully reviewing the UK GAAP financial figures that Inspired has had historically, and be absolutely certain that in every respect they are stated to be consistent and compatible with and obedient to US GAAP.

We mentioned on the revenue recognition issues having to do with, for example, the upfront sale of a software license, that US GAAP requires be amortized going forward.

I don't know you. But you sound like someone familiar enough with investment in the US to know that you can't just capitalize any software [that] you feel like. There are very, very strict, very careful rules, many of which existed before Sarbanes-Oxley, many of which became much more comprehensive after Sarbanes-Oxley.

And whatever is presented in the proxy will be at least as conservative as the very strict and very circumspect accounting rules in the United States require.

Artham Fulkham: Excellent. Thank you, Lorne. I really appreciate the color. And last question, on the CapEx, which already couple of investors asked you. So it's a small clarification just to make sure that I did not miss something about your business.

When one of you gave an example about a five-year license sale with $5 million exchanging hands, and you talked about the tail. Do I get it right that under the UK, IFRS, I assume, or GAAP, you would have reported that as a sale of revenue recognized within year one, but the cash would be actually paid pro rata over the next five years? So --

Daniel Silvers: No

Artham Fulkham: -- when we (inaudible) to the -- no. So the cash flow will be paid in --

Daniel Silvers: No.

Artham Fulkham: -- year one as well?

Daniel Silvers: You're half right. The software license in the UK, the license would be sold upfront. The license, let's say it's $5 million. The license would be paid for and the $5 million of revenue would be recognized in the P&L.

In the US GAAP, the $5 million, cash would be received. It would go initially on the balance sheet, but would then be used effectively to finance the CapEx needed to generate the five years of recurring revenue. And the $5 million software license would be amortized a million a year over the five years of the contract.

Artham Fulkham: When the actual cash will be paid? In year one or pro rate over five years?

Daniel Silvers: Well, there's cash up front and then there's also recurring revenue over time.

Lorne Weil: He means the cash. The cash from the sale, I mean, it could be any way it's structured with the customer. But the way it has been is the entire software license is paid for up front.

Luke Alvarez: Typically our virtual sport deals have had two components - an upfront software license, which under UK GAAP is recognized up front, but under US GAAP, it's spread over the life of the contract. The cash for that upfront software license is typically received over the first three to twelve months of a, for example, five-year contract.

And then the second component is a recurring revenue share, which is typically paid monthly based on actual revenues and participation thereof. And that, obviously, is received every month over the five-year life of the contract.

Under UK GAAP, the license would be recognized as revenue up front, and the recurring would be taken on a monthly basis throughout the life of the contract. Under US GAAP, both the license and the recurring are taken over the life of the contract.

Daniel Silvers: So, Luke, I think we're coming to the end of the time. We're obviously happy to --

Artham Fulkham: Thank you.

Daniel Silvers: -- talk offline with anybody that has further questions on this stuff.

Operator: This concludes our question-and-answer session. I'd like to turn the conference back over to Lorne Weil for any closing remarks.

Lorne Weil: Okay. Thank you very much, Operator. We really appreciate all of you joining the call this morning. Obviously, as we move forward over the course of the next several weeks, we will be looking forward to an opportunity to speak with many of you further. Obviously, ideally, we're happy to meet and discuss these issues with you further in person.

And, of course, we'll be keeping you posted through press releases and other communications how things are moving forward as we progressed. Dan gave you a pretty clear sense of what we think our timetable is. Any of you should, of course, feel free to be in touch any time you wish to discuss these things further. And we look forward to talking to you again, both in the course of completing this transaction and as we go forward in the future, quarter by quarter, as we become a public-operated company on NASDAQ.

So thank you again, and we look forward to talking to you again soon.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines.