

NO GAMBLING ON TATTS



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Tatts Group (TTS) operate lotteries throughout Australia including popular games such as OzLotto and Powerball. Regulation within the industry makes it a highly lucrative business to incumbent operators such as Tatts.

The government awards long-life licenses to generally one or two operators per state effectively creating a monopoly or duopoly market structure. Tatts holds the license to operate lotteries in NSW, QLD, SA, VIC, TAS and NT - with exclusivity in the former three states.

Tatts' dominance over the market provides for clear economic advantages. In an industry characterized by high barriers to entry, Tatts are largely unencumbered by competitive pressure. This allows for sustainable profits to be drawn over the longer term. The scale of Tatts' distribution network and sizable prize pool further guard profitability from new entrants. Unlike typical monopoly industries, government intervention is relatively low and we see limited regulatory risk.

Earnings from lotteries are strong and predictable and provide a dependable stream of cash flows to the business. Earnings are supported by strong demand, largely insensitive to changes in consumer sentiment, and favourable microeconomic structures (as discussed above).

We believe the business has potential to further grow earnings through implementation of a new distribution strategy. At present the bulk of lottery sales are conducted through newsagents that charge a fee to distribute the product. Tatts have begun to roll-out a direct online sales model which should provide for higher margin sales and access to new markets – particularly the 18-30 year old demographic.

Tatts also operate wagering services in many of the key states in Australia. The wagering industry is relatively mature with a number of domestic and international competitors. While we believe there is potential upside from consolidation within the industry, we expect Tatts to remain under competitive pressure in the interim. Accordingly, wagering accounts for less than 30% of group revenue.

In short, our high conviction on Tatts Group rests upon their resilient lottery related earnings and cash flows, exclusive assets and strong dividend yield of c. 5.0%.

Tatts Group is currently held in Perpetual's Industrial Share, Australian Share, Concentrated Equity, Share-Plus, Geared Australian Share and Pure Equity Alpha Funds.