

Gaming: GLPI's Offer for PNK Is Good for Each Company. What's Next? Probably a Higher Offer to Get It Done.

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Abstract:

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Gaming GLPI's Offer for PNK Is Good for Each Company. What's Next? Probably a Higher Offer to Get It Done.

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Overall, we view today's announcement as a positive for both the shares of PNK and GLPI, each rated OW.

* We like today's announcement in that PNK gets value up front without going through a lengthy and potentially uncertain process and the risks associated with its PropCo/OpCo separation plan. For GLPI, it would receive acquisition-related growth (a heretofore investor concern) and reduce its largely single tenant risk exposure (ditto) through creating and spinning out another OpCo.

Ultimately, we see scale and geographic diversification benefits that should/could result in a higher valuation multiple for GLPI. Lastly, we don't think GLPI's first offer is its only, best, or last offer-only because in most cases, it's not-despite management's history of being a value disciplined buyer of assets and companies. GLPI's offer of \$35.77 in consideration (GLPI shares and OpCo spin shares) implies ~10x 2016E EBITDA, above where PNK's trading multiple of 8.0x 2016E EV/EBITDA was as of last Friday's close. * Earlier today, OW-rated GLPI announced that it has sent a letter to the Board of Directors of OW-rated PNK detailing its offer to acquire the real estate assets of Pinnacle for GLPI shares in a transaction with an enterprise value of \$4.1b (equating to 11.2x GLPI's estimated \$365m

of real estate EBITDA). In addition, PNK's OpCo would become a separately traded public company and would be operated by its current management and Board of Directors. This last point we find interesting in that this aspect allows PNK's current management and board to keep their jobs, which PNK has to find at least somewhat appealing and potentially reduces a PNK social impediment to getting a potential transaction with GLPI done. GLPI apparently doesn't expect PENN to be involved and likely wants the tenant diversification. * Per GLPI, the offer follows failed attempts by GLPI to meet with and engage in a discussion on a combination with PNK's management. Recall, on November 6, 2014, PNK announced its plans to separate its current operations into two entities—a PropCo and an OpCo—similar to the transaction that old PENN completed in late 2013, which resulted in GLPI and the current PENN. * Do we see another entity bidding for PNK? We think it's highly unlikely, given GLPI's premium valuation (which is increasing today) relative to other potential bidders (so we see low risk in BYD or MGM or others in the gaming industry emerging).

* The only downside risk we see with GLPI's math of \$35.77 per share for PNK is that it is predicated on valuation assumptions where GLPI and PNK OpCo would trade. Specifically, GLPI assumes a (1) 2016E EV/EBITDA multiple of 14.7x for pro forma PropCo, which we think is fair, and (2)

7.5 times 2016E EV/EBITDA for OpCo, which, in our view, is a half-turn aggressive. If we are right on the latter and in agreement on the former, the math would suggest ~\$34 in value for PNK. That said, how can PNK argue that these multiples have risk and be aggressively derived when PNK itself is trying to get these same multiples by separating its PropCo/OpCo EBITDA solely to create incremental equity value per share? It can't.

* Options for PNK? (1) It could do nothing, stay the course, and work on its PropCo/OpCo separation, which could be met with resistance from its current holders, (2) engage with GLPI but dismiss the current offer as inadequate and signal that its board would be amenable to a higher offer, or (3) accept GLPI's first offer (low likelihood; who would do this? No one with a sense of fiduciary duty in our view). We think (2) is the most likely option. That said, we would not be surprised if PNK uses its current share price (higher today by ~14%) to issue equity to effect a stronger capital structure for the REIT (short interest is high at 18% of the float, and shorts would likely buy as a means to cover); this would also be a way for PNK to extract leverage to use against GLPI to extract a higher value. * Other details from today's disclosures from GLPI: (1) The real estate company resulting from the transaction GLPI is proposing would be the third-largest triple-net REIT by enterprise value. (2) Under the GLPI offer, following the spin-off of OpCo, Pinnacle's real estate assets

("PropCo") would be merged into GLPI and OpCo would enter into a mutually agreeable master lease agreement with GLPI. (3) In the transaction, Pinnacle shareholders would receive one share of OpCo common stock and

0.5517 shares of GLPI common stock for each share of Pinnacle they own.

(4) Pro forma for the transaction, Pinnacle shareholders would own 100% of OpCo and approximately 36m shares in GLPI, representing an approximate 20% equity interest in the larger, post-transaction GLPI. * Other details continued. (5) The transaction is expected to close prior to the end of 2015. (6) This value represents a 30% premium to Pinnacle's closing stock price on March 6,

2015, a 47% premium to Pinnacle's volume weighted average price over the last 30 days, and a 59% premium to Pinnacle's price on the date (January 16, 2015) when GLPI made its initial offer to Pinnacle. (7) GLPI's proposal is structured as a taxable transaction, and is not reliant, as is Pinnacle's, on a favorable IRS tax ruling. (8) GLPI's proposal will be fully underwritten to maintain its an capital structure. (9) GLPI indicated that its proposal is immediately accretive to GLPI's AFFO per share and results in a conservative leverage profile for both pro forma GLPI and Pinnacle OpCo.

Companies Discussed in This Report (all prices in this report as of market close on 06 March 2015)
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Date

Rating

Share Price

(\$)

Price Target

(\$)

14-Nov-13

N

44.90

47.00

14-Jan-14

N

37.23

37.00

29-Jul-14

N

34.45

34.00

28-Oct-14

N

31.46

31.00

09-Jan-15

OW

29.51

34.00

03-Feb-15

OW

33.74

36.00

Date

Rating

Share Price

(\$)

Price Target

(\$)

02-Jun-08

OW

13.51

23.00

05-Aug-08

OW

12.08

16.00

13-Oct-08

OW

5.00

9.00

19-Dec-08

OW

6.91

10.00

13-Apr-09

OW

9.70

11.00

24-Apr-09

OW

11.40

14.00

05-Jan-10

OW

9.37

13.00

05-Feb-10

OW

7.39

11.00

21-Apr-10

OW

11.86

14.00

27-Apr-10

OW

13.26

17.00

20-Jul-10

OW

10.13

15.00

28-Oct-10

OW

12.06

16.00

24-Jan-11

OW

14.86

19.00

14-Jul-11

OW

15.24

20.00

03-Aug-11

OW

13.90

21.00

27-Oct-11

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24-Jan-12

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10.54

17.00

28-Mar-12

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10.95

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9.14

14.00

25-Jul-12

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9.02

13.00

24-Oct-12

OW

12.74

16.00

21-Dec-12

OW

16.20

24.00

28-Jan-13

OW

15.45

23.00

13-Feb-13

OW

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20.00

23-Apr-13

OW

19.33

21.00

01-May-13

OW

19.52

23.00

04-Sep-13

OW

24.45

31.00

28-Oct-13

OW

24.23

29.00

06-Nov-13

OW

24.33

30.00

12-Feb-14

OW

23.51

29.00

30-Apr-14

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22.45

28.00

21-Jul-14

OW

24.32

27.00

06-Nov-14

OW

23.22

33.00

12-Feb-15

OW

25.99

36.00

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Gaming

Gaming

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