Is Amaya Inc. About to Buy Intertain Group Ltd.?

Description

After a tough few months, shares of **Intertain Group Ltd.** (TSX:IT) have been surging on rumours that it will be taken over by Quebec-based **Amaya Inc.** (TSX:AYA)(NASDAQ:AYA), which already owns 2.7% of the company.

Amaya may have competition, however, as Intertain says its "received many expressions of interest in acquiring all or material parts of its business," adding that it would consider "a sale of the company, one or more business units or partial offers and recapitalizations."

While an Amaya and Intertain combination would make sense given both companies operate complementary online gambling businesses, there are some recent complications to any potential deal.

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Image Source: YCharts

Regulatory environment isn't too keen on industry consolidation

According to *Bloomberg*, both companies' primary industry "is beset in some jurisdictions by regulatory uncertainty as lawmakers decide how to tax and regulate online gambling."

Things may have gotten even more difficult this week after regulators charged Amaya chief executive David Baazov and others for insider trading that stemmed from Amaya's $4.9 billion buyout of PokerStars in 2014. Baazov faces five charges of "aiding with trades while in possession of privileged information, influencing or attempting to influence the market price of the securities of Amaya Inc., and communicating privileged information."

Further complicating things, Amaya had been in the process of taking itself private. That transition is now in doubt.

When the news broke, Amaya shares fell 21%, while Intertain was dragged down 9%. If investors were leery about a possible combination before, the recent charges are clearly putting a damper on any appetite for future industry transactions.

Premiums are getting wiped out fast

When Intertain management announced that suitors were interested in the company, shares popped from $9.30 to $11.80 in just days. Since those highs, shares are back to $9.60. As a standalone business, Intertain has released guidance; it is expecting to earn $140-160 million in profits this year off of $460-500 million in revenues. At $9.60, shares are trading at only five times expected earnings.

It's clear that there's a massive market discount for being in an industry where regulation could wipe out your entire business. Still, there's no denying that the stock is incredibly cheap if the status quo is maintained.

Amaya, meanwhile, faces some significant hurdles even though shares are similarly cheap, trading at just seven times trailing earnings. **Moody's** recently revised the company's rating outlook to negative from stable following the insider trading charges. A Kentucky court also fined the company $870 million for losses incurred by Kentucky residents using PokerStars between 2006 to 2011.

Roughly 10% of all shares are currently shorted, and with volume so low, it would take nearly 80 days to fully wind down the mounting short positions.

If you're tempted to catch a falling knife, Intertain looks to be trading at a lower valuation and comes with less baggage. Intertain's management team also noted that it was getting interest by "many" parties looking to make an acquisition. So even if Amaya can't come through with an offer, there's still plenty of buyout upside left.

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