RESEARCH REPORT

January 8, 2018

Stock Rating	BUY
Price Target	$42.00

Bear Case	Price Target	Bull Case
$36.00	$42.00	$44.00

Ticker	TSX:GC
Market Cap ($MM)	2,061.0
P/E NTM	19.2x
EV/EBITDA NTM	9.7x

52 Week Performance

Great Canadian Gaming Corp.

We Like the Odds

Amidst a Canadian consumers sector with limited names that fit all the characteristics of QUIC's investment strategy, Great Canadian Gaming Corporation appears to be a diamond in the rough. With recent major bundle acquisitions and plans to modernize existing casinos, the company is poised for future growth and success. Our three-pronged investment thesis includes the following factors:

(1) New Opportunities in OLG Modernization

Great Canadian has recently begun expanding into the lucrative Ontario gaming industry. With bundle acquisitions and modernization plans, the company should experience immense growth moving forward.

(2) Checking off all the Boxes for QUIC's Investment Strategy

Great Canadian benefits from an industry-regulated environment to achieve a strong and sustainable competitive advantage. The company is led by an "Outsider" CEO and surrounding management team who are masters of capital allocation. Despite recent growth, we believe the company still possesses enormous upside potential.

(3) Superior Financial Fundamentals

Great Canadian's management team has been able create a compounding machine out of its business. On all analyses, the company has consistently compounded capital at high rates of return, while maintaining a best-in-class balance sheet.

When considering investing in Great Canadian, we analyzed management's ability to redeploy incremental capital along with comparing trading multiples to industry competitors. Doing so provided further confidence in this investment.

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Company Overview

The Great Canadian Gaming Corporation (TSX:GC) offers gambling, entertainment and hospitality services in British Columbia, Ontario, Nova Scotia, New Brunswick and Washington State. GC operates 21 gaming facilities, within which exist, 15 casinos, 4 racetracks, 3 show theatres and over 45 food and beverage outlets. GC's gaming facilities are operated under long term contracts with regional regulatory bodies, including the Ontario Lottery and Gaming Corporation (OLG) and the British Columbia Lottery Corporation (BCLC). The company is sizeable, with a current market capitalization of $2.1Bn and total revenues equalling $566.4MM in 2016. GC earns a portion of its total gaming revenue (some is collected by governmental bodies) and, with the exception of Nova Scotia, who collects revenue from non-gaming revenue as well, all revenue earned through non-gaming business operations (e.g. revenue attributed to hotels). Regionally, the vast majority of revenue is generated from GC's operations in British Columbia, where it operates recognizable and respected properties, such as the River Rock Casino and Hastings Racetrack. This regional concentration is despite the fact that gambling in British Columbia is only responsible for 16.5% of total Canadian gambling revenue, whereas provinces with greater populations, Ontario and Quebec for example, are responsible for 40.3% and 20.3% respectively. Nationally, the company holds approximately 2.7% market share. Recently, GC has begun refurbishing and rebranding many of its properties and expanding, by developing new properties. This can be partly attributed to OLG, as it recently awarded GC a few long term contracts which give GC the right to operate several more gaming facilities. The current CEO of GC is Rod Baker, who has held the position since 2011. Previous to his role as CEO of GC, Baker was President of a financial services and merchant banking company, Ridgeline Corporation.

EXHIBIT I

Gambling Industry Product and Service Segmentation

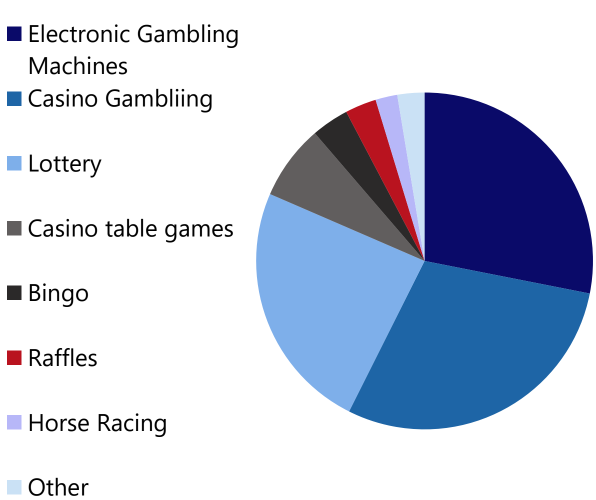
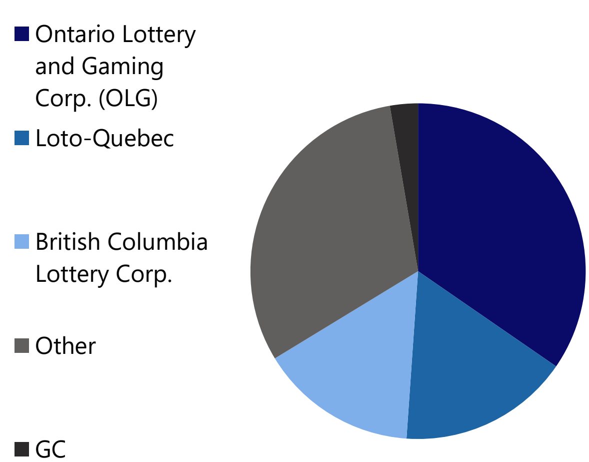


EXHIBIT II

Major Industry Players by Market Share



Industry Overview

Gambling in Canada is a $15.5Bn industry. Over the past five years, industry has declined by 0.8%, as consumers decreased overall discretionary spending and in a disproportionately high amount, spending on gambling. This decline can also be attributed to: slow per capita income growth, rising prices of some essential products and competition from US casinos. In addition, the overall volatility of the Canadian dollar has discouraged US citizens from traveling to Canada to gamble. Another factor, which has affected the growth of the traditional gambling industry, is the rising competition resulting from alternative forms of entertainment (e.g. smartphone games).

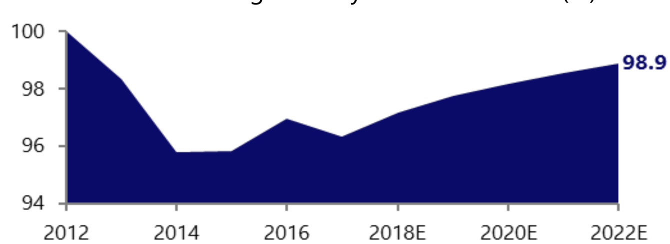
The industry is concentrated, with the largest four operators controlling an estimated 69% of industry revenue. This consolidation is primarily due to heavy regulation, which has also resulted in nearly half of all revenues being paid out to governments and charities. Crown Corporations hold a large share of the market and regulation of the gambling industry is within the jurisdiction of the provinces. While each province regulates the industry in a unique manner, federal law requires that gambling is "conducted and managed" directly by provinces. To comply with this law, provinces enter into long term contracts with private sector operators that give the responsibility of specific services or the entirety of day-to-day operations for gambling facilities to these companies. The responsibility to ensure that the facility adheres to regulations, among other, smaller, responsibilities, is left to the governmental regulatory body. In this way, provinces comply with the Criminal Code of Canada but avoid the responsibility of having to operate all gambling facilities directly. One of the main Canadian gambling regulatory bodies is the Ontario Lottery and Gaming Corporation (OLG). To drive private investment in gaming infrastructure, create jobs and increase provincial government revenue, OLG has begun a bidding process for the right to operate "bundles" of potential or existing gaming facilities. These bundles are grouped according to the geographic regions in which they are located. This process is a part of the OLG's Modernizing Lottery and Gaming in Ontario program.

It is expected that the gambling industry will grow slowly over the next five years (approximately 0.5%) despite further US competition, as new casinos continue to be built in states like New York and Massachusetts. The following trends, which promote industry growth, are anticipated for key industry economic drivers in 2017: consumer spending will increase, the Canadian dollar will weaken, relative to the US dollar and leisure time will increase. These trends are expected to offset the detracting force of increasing US competition and drive growth in the gambling industry. However, if the threat of consumer debt affects economic growth, it is probable that discretionary spending will be further reduced, leading to stagnation or decline in the gambling industry.

While insignificant to current revenues, the emerging online gaming segment could provide the Canadian gambling industry with much needed stimulus. Traditionally, Canadians have used unregulated offshore websites, called the "grey market", to game online. These offshore companies offer online gaming opportunities to citizens globally, but are based out of countries with little gambling regulation. Therefore, these companies circumvent North American regulations and taxes, yet still have access to the North American customer base. To capture this lost revenue stream, provinces have begun to offer online gaming through their various crown corporations (e.g. OLG). However, these websites have yet to significantly contribute to provincial gaming revenue due to grey market competition.

EXHIBIT III

Canadian Gaming Industry Revenue Growth (%)



Investment Thesis I: Opportunity in OLG Modernization

In 2012, OLG announced a modernization initiative which was intended to drive private investment in the gaming industry and increase governmental revenues from it. Now, in 2018, the modernization process is in a stage which involves OLG awarding bundles of long term contracts (called gaming bundles) for potential or existing gaming facilities to private operators. These gaming bundles consist of several gaming zones, grouped together on a geographical basis. In total, this initiative concern 27 gaming zones that span the province of Ontario. The size of facility developed in each zone is regulated by the OLG's prescribed maximum number of slots allowed and maximum number of live tables allowed for that zone. For each gaming zone, there is a separate bidding process which follows the same three general steps. Firstly, the private operators must pass a prequalification process, this creates a "short list" of potential operators. Next, the operators on the short list are allowed to apply for the contract. Finally, the contract is awarded to the winning bidder.

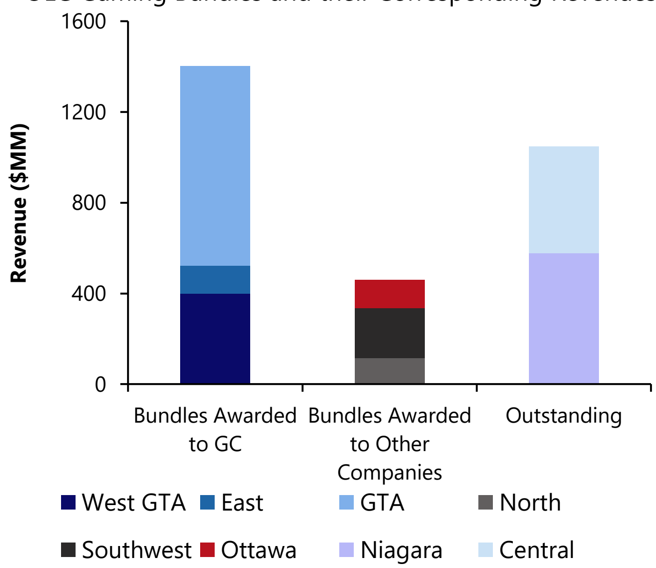
The OLG modernization process presents an opportunity for GC to expand. Already, GC has been awarded the Greater Toronto Area (GTA) Bundle, the West Greater Toronto Area (West GTA) Bundle and the East Bundle. In regard to the GTA Bundle, GC is a 49% equity partner, working in partnership with Brookfield, an alternative asset manager. Concerning the West GTA Bundle, GC in a 55% equity partner working in partnership with Clairvest, a private equity firm. Regarding the East Gaming Bundle, GC will operate through a subsidiary in which GC holds 90.5% equity interest. Together, these bundles represent ten gaming zones and include established gaming sites such as the Woodbine Racetrack, Brantford Casino and Grand River Raceway. As of fiscal 2015, the East, the West GTA and the GTA bundles represent $124.2MM, $339.7MM, $879MM of revenue, respectively. Of the three gaming bundles awarded to GC, only the East Gaming Bundle involves the development of a new gaming facility, which is the responsibility of GC, the GTA and West GTA bundle involve solely the oversight of operations of existing facilities.

OLG began awarding gaming bundles in 2015 and there are two outstanding gaming bundles still to be awarded, the Central and Niagara bundles. Combined, these groups represent five gaming zones and ~$1Bn of revenue. GC has been short-listed for both of these bundles. OLG has cited three main criteria when evaluating potential operators: gaming experience, financial strength and property development experience. As a corporation with 36 years of gaming experience, stable financials (as will be discussed later), and a successful development history, GC can be seen as a viable candidate for both of these bundles. As well, GC's viability as a candidate is proven by its being previously awarded bundles by OLG.

The GTA, West GTA and East gaming bundles, as well as the possibility of being awarded an outstanding bundle, provide GC with a runway for growth in a province which is responsible for over 40% of national gaming revenues. This is a low risk expansion opportunity as almost all casinos, with the exception of those yet to be developed, involved in these bundles have already been proven as profitable.

EXHIBIT IV

OLG Gaming Bundles and their Corresponding Revenues



Investment Thesis II: Checking Off all the Boxes

At the beginning of the 2017-18 year, the QUIC team established an investment strategy to follow for all stock making selections. The strategy entailed the following four-step process:

EXHIBIT V: QUIC's Investment Strategy

1. Discover Companies with a ***Sustainable* Competitive Advantage**
2. With **Management** that are ***Capital Allocation Masters***
3. Ensure a ***Runway for Growth*** Exists
4. Pay a ***Fair* Price**

(1) Sustainable Competitive Advantage

The Canadian gaming environment provides an extremely favourable industry to operate in, which GC has taken advantage of. Great Canadian has committed to **long-term agreements with provincial crown corporations**. Furthermore, GC operates in several segments (New Brunswick, Nova Scotia, and most notably the GTA as of 2018), where the company possesses a **monopoly as the only regional operator.** These characteristics provide Great Canadian Gaming with a sustainable competitive advantage (or in business terms, a **moat**), which GC should continue to capitalize on to outperform its competitors.

(2) "Outsider" CEO and Stellar Management Team

GC is led by CEO Rod Baker, who we believe fits the characteristics of an **Outsider CEO.** Baker rarely meets with the research analysts, nor does he appear on the cover of business magazines. His **sole focus is on capital allocation**, with the intention of growing the business on a per-share basis as much as possible. Baker also owns a significant ownership stake in the business, holding 5% of all outstanding shares. Furthermore, GC's management team has also orchestrated **several successful major acquisitions** in prior years, exhibiting traits of patience and thinking for the long-term. Evidence of the company's successful track record is detailed more in investment thesis III, outlining management's successful ability to grow the business, while maintaining a healthy balance sheet. We have confidence in GC's management and their ability to deliver strong results moving forward.

(3) Runway for Growth

When investing in any company, it's vital to **look ahead** and not get caught staring in the rear-view mirror. Despite GC's tremendous success which has been reflected in significant share price appreciation recently, we are confident the company can still be a multi-bagger over the upcoming decade. GC is putting significant capital to work, modernizing locations across Canada, while capturing bundles in the GTA and several other prime locations. With the company's **stellar track record of capital allocation and high ROIC**, we are confident management will continue to deliver and create value for shareholders.

(4) Paying a Fair Price

Great Canadian trades at a **discount** to several of its competitors despite possessing **stronger margins, revenue growth, and a cleaner balance sheet**. When considering growth opportunities moving forward through modernization of existing facilities and recent bundle acquisitions, we believe the company has the ability to achieve 15%+ returns per annum over the next 5-10 years.

Investment Thesis III: Strong Compounder & Healthy Balance Sheet

We believe that GC's management team is both great at being productive with their capital and managing their balance sheet. We want to invest in companies that yield greater returns on their earnings than what is available in the broader market.

(1) Market Value Generated on Retained Earnings

To evaluate GC's ability to generate returns on their earnings, we use Warren Buffett's $1 Test, which he talks about in his 1984 shareholder letter. This high-level analysis essentially compares how much of a company's earnings are retained to how much market value was generated over the same time period, usually three to five years. Buffett states that in order to pass his $1 Test, "for every dollar retained by the corporation, at least one dollar of market value will be created for owners". In other words, it is only worthwhile for a company to retain their earnings if a dollar in the hands of management is worth more than a dollar in the hands of shareholders.

Over the past five years, GC has retained $191.2MM of earnings and generated $825.7MM of additional market value (see Appendix I & Exhibit VI). Assuming the price appreciation GC has experienced in the markets over the past five years accurately reflects the intrinsic value of the company, **GC has generated $4.3 in value for each dollar it retained**. As such, GC easily passes Buffett's test, which may suggest that management is smart with their capital. In comparison, none of GC's four regional peers pass the $1 Test, with Churchill Downs being the closest, generating only $0.7 in market value for each dollar retained. In doing this exercise, we are evaluating the company's ability to earn a return on its **incremental invested capital (ROIIC)**.

(2) Impressive Return on Invested Capital

Another way to evaluate GC's ability to compound its intrinsic value over time is by analyzing the company's **return on invested capital (ROIC)**. Great Canadian Gaming's management has historically allocated capital to projects that return much more than their cost of capital, and thus generate value for shareholders. We calculated the ROIC of the company since 2005 and found that it has steadily increased to the 24% it is currently (see Exhibit VII). The only way this can happen is if the incremental capital invested in recent years yields a return that exceeds what has been returned in past years. The upward trending ROIC that GC has been able to achieve is important because it shows that the company is currently able to find attractive growth initiatives to invest upon. This can be classified as a **'reinvestment moat'**, which is more favourable than companies that rely on returns from 'old' capital that have few compelling investment opportunities presently, which is called a **'legacy moat'**.

(3) Clean Balance Sheet

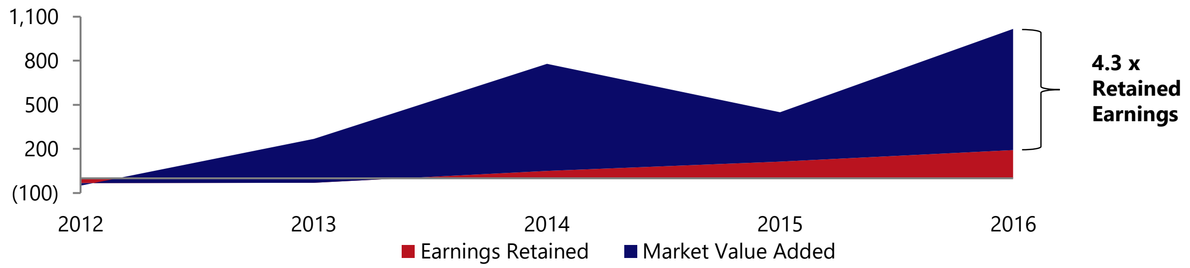
Great Canadian Gaming's management team has been prudent with using debt, which has resulted in an industry-leading leverage profile. When compared to both regional and U.S. peers, GC's Net Debt / EBITDA multiple of 1.3x falls well below the industry average of 4.0x (see Exhibit VIII).

(4) Why Does This Matter?

The gaming industry is mature. As such, it is necessary to grow through development projects. Great Canadian Gaming's strong history of efficiently allocating capital to lucrative projects, as discovered by looking at their ROIIC and ROIC, leads us to believe that they are capable of managing the money investors put in their hands. The range of opportunities to acquire existing facilities with the OLG's modernization process and build new facilities in regions such as Victoria, BC offer exciting prospects to reinvest capital in the future at the high rates of return they have benefitted from in the past. Additionally, the company's low levels of debt will allow them to incur more debt in the future to pursue projects that will help generate value for GC.

EXHIBIT VI

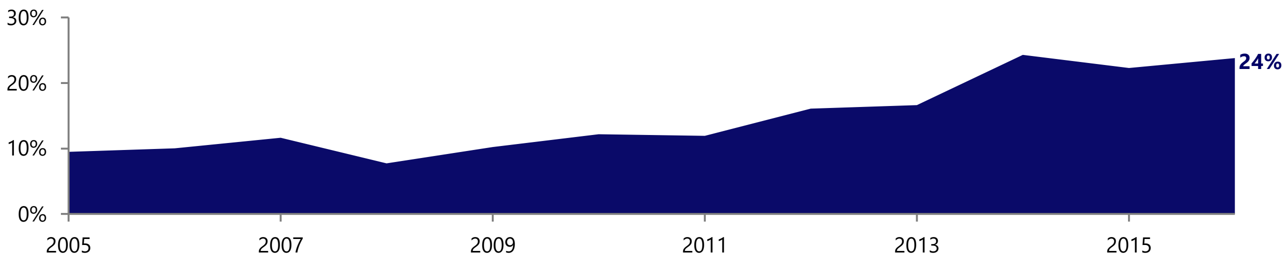
Earnings Retained vs. Market Value Added (2012 – 2016)



Source(s): S&P Capital IQ

EXHIBIT VII

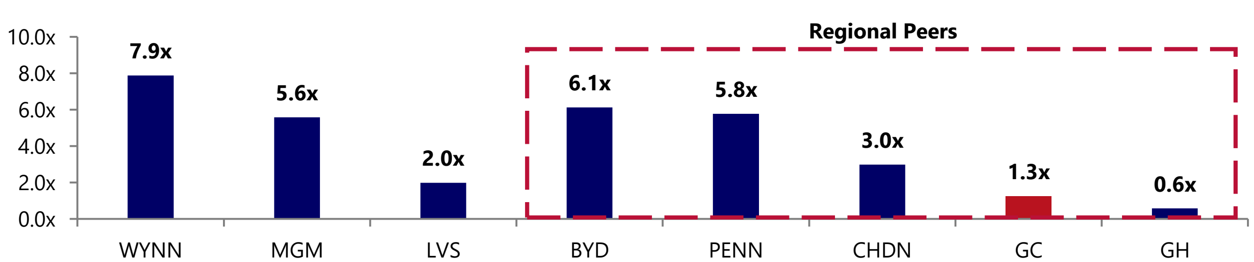
Historical Return on Invested Capital (2005 – 2016)



Source(s): S&P Capital IQ

EXHIBIT VIII

Net Debt / EBITDA Multiples of Comparable Companies (FY2016)



Source(s): RBC Capital Markets, S&P Capital IQ

Valuation

EXHIBIT IX

Historical Return on *Incremental* Invested Capital

	2011	2012	2013	2014	2015	2016	2017
CapEx	$21	$25	$25	$15	$15	$39	$59
Acquisitions	$5	$4	-	-	$96	$38	$1
Incremental Invested Capital	**$26**	**$29**	**$25**	**$15**	**$111**	**$77**	**$61**
EBITDA	$133	$146	$141	$175	$174	$200	$210

Great Canadian's superior business model and exceptional management team provide for strong returns on incremental invested capital

Source(s): S&P Capital IQ

2011 to 2017 Progression	
Total Cumulative Invested Capital	$344
Cumulative Change in EBITDA	$77
Return on Incremental Invested Capital	**22%**

EXHIBIT X

Comparable Companies Analysis

Company Name	Market Cap ($MM)	Enterprise Value ($MM)	EV / EBITDA LTM	EV / EBITDA 2018E	Price / Earnings 2018E	Price / Earnings 2019E	Net Debt / EBITDA 2018E	EPS Growth 2018E	EPS Growth 2019E	ROE	2017 Margin	FCF Yield	Dividend Yield
Boyd Gaming Corporation	$4,139	$7,049	13.0x	11.8x	35.7x	25.8x	4.9x	1.3%	1.1%	9.9%	25.4%	3.1%	0.5%
Churchill Downs Incorporate	$3,650	$4,716	15.2x	13.1x	34.7x	25.9x	3.0x	6.6%	7.1%	19.5%	27.2%	0.2%	0.6%
Penn National Gaming, Inc.	$2,798	$7,405	9.0x	8.4x	3.2x	23.3x	5.2x	1.3%	8.9%	NM	28.4%	9.2%	nmf
Red Rock Resorts, Inc.	$2,327	$4,967	9.8x	9.9x	53.7x	26.6x	5.3x	1.2%	0.4%	9.9%	31.0%	(6.2%)	1.2%
Golden Entertainment, Inc.	$868	$998	29.3x	54.5x	822.5x	365.6x	7.1x	0.0%	0.0%	11.9%	4.2%	2.2%	nmf
Cedar Realty Trust, Inc.	$544	$1,167	52.3x	14.2x	25.9x	21.3x	7.6x	0.1%	0.1%	3.0%	56.2%	26.0%	3.4%
Gamehost Inc.	$265	$277	10.0x	10.2x	16.0x	16.0x	0.5x	0.7%	0.7%	14.3%	40.2%	6.5%	6.4%
Century Casinos, Inc.	$260	$274	10.8x	10.0x	18.2x	20.7x	0.5x	0.4%	0.4%	11.7%	18.1%	5.2%	nmf
Full House Resorts, Inc.	$83	$161	4.7x	8.8x	90.8x	40.3x	4.3x	0.0%	0.0%	(7.0%)	11.3%	(1.1%)	nmf
Mean	**$1,659**	**$3,002**	**17.1x**	**15.7x**	**122.3x**	**62.8x**	**4.3x**	**1.3%**	**2.1%**	**9.1%**	**26.9%**	**5.0%**	**2.4%**
Median	**$868**	**$1,167**	**10.8x**	**10.2x**	**34.7x**	**25.8x**	**4.9x**	**0.7%**	**0.4%**	**10.8%**	**27.2%**	**3.1%**	**1.2%**
Great Canadian Gaming	**$2,061**	**$2,254**	**9.8x**	**10.1x**	**26.7x**	**25.4x**	**0.9x**	**1.8%**	**1.5%**	**21.4%**	**36.9%**	**3.4%**	**nmf**

Despite holding stronger growth characteristics, margins, and financial stability, Great Canadian trades at a discount compared to its peers

Risks and Catalysts

Risks

(1) Discretionary Nature of the Business

Gambling is a discretionary activity for consumers, so an economic downturn could lead players to visit Great Canadian Gaming's facilities less frequently. To offset this risk, GC has been geographically diversifying their portfolio of facilities so they are not as concentrated on the province of British Columbia. Examples include acquisitions of three OLG bundles and opportunities for redevelopment of existing casinos in Nova Scotia.

(2) Competition

Great Canadian Gaming faces high competition in many regards. In the BC market, the new Parq Vancouver casino in the waterfront of Vancouver offers meaningful competition to GC's existing Hastings Racecourse and River Rock Casino Resort facilities. In Ontario, the privatization of casino operators through the OLG's bundle bidding process is a competitive process, which could lead GC to pay a high acquisition premium to win bundles.

(3) Wage Inflation

Casino dealers in Canada typically make slightly above minimum wage, or minimum wage only if they are inexperienced. With minimum wage hikes being a common trend in Canada, GC is at the risk of incurring higher costs. This is especially prevalent in BC facilities such as River Rock, which have unionized employees and are likely to negotiate higher wages to keep pace with rising minimum wages. Human resources make up ~45% of their expenses, however it is unclear how much of this is attributable to low-wage employees.

Catalysts

(1) Ownership Transfer of GTA Bundle

Great Canadian Gaming, through its Ontario subsidiary partnership with Brookfield, was awarded the OLG GTA bundle in August of 2017. The partnership will take ownership of the bundle in spring 2018, and they must retain employees for at least one year in their current positions. Their one year grace period will expire in spring 2019, which may allow GC's Ontario subsidiary to drive efficiencies in their acquired. Given the vast experience their partner, Brookfield Business Partners, has in acquiring and making businesses more profitable, we believe there could be headcount reductions at this time and margins could grow.

(2) Additional OLG Bundles Available

There remains two OLG bundles that have not been awarded to a private operator. These two bundles are the Central and Niagara bundles, which are expected to be sold in spring 2018 and summer 2018, respectively. With the Niagara bundle generating ~$580MM in revenue and the Central bundle generating ~$470MM in revenue, they rank second and third of all OLG bundles in terms of size. The only bundle that is larger than those two is the GTA bundle, which GC has already been awarded. Great Canadian Gaming has been short-listed for a request for proposal, which is the last step before the OLG announces a winner.

Additionally, unlike bundles previously won by GC, the company would be a sole owner and operator for each of the two outstanding bundles. Since they have already bought three bundles with equity partners, they will develop sufficient expertise in acquiring OLG bundles acquire one independently. Consequently, GC will have the opportunity to keep more of the profits if they are selected as the successful bidders for one, or both, of the Niagara and Central bundles.

References

1. Base Hit Investing
2. IBISWorld
3. RBC Capital Markets
4. S&P Capital IQ
5. Scotiabank Global Banking and Markets
6. Seeking Alpha

APPENDIX I

Warren Buffett's $1 Test

TSX:GC	FY2012	FY2013	FY2014	FY2015	FY2016
Retained Earnings (MM)	($32.2)	$2.0	$80.4	$64.5	$76.5
Market Value at Period End (MM)	$672.5	$988.7	$1,419.5	$1,025.3	$1,516.2
Stock Price at Period End	$9.6	$14.6	$20.7	$15.5	$25.0

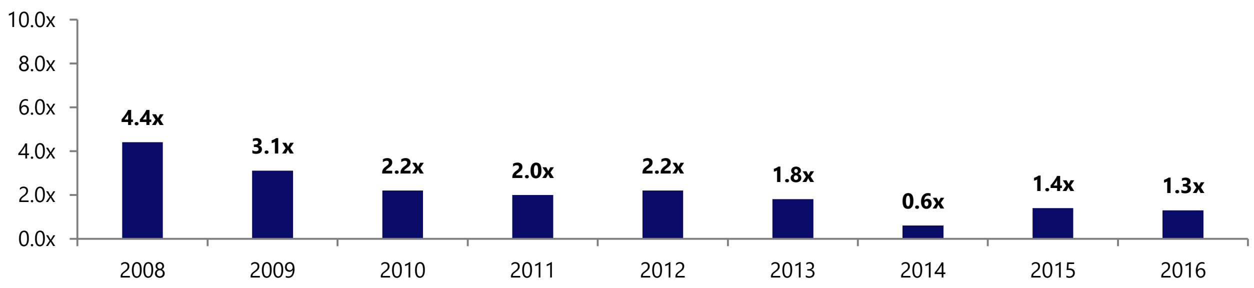
End of 2011	
Stock Price	$8.4
Shares Outstanding (MM)	82.4
Market Value ($MM)	$690.5

End of 2016	
Market Value (MM)	$1516.2
5-Year Total R/E (MM)	**$191.2**
Total Mkt. Val. Added (MM)	**$825.7**

Value generated from each dollar retained:	***$4.3***
5-Year Return:	***198%***

APPENDIX II

Historical Net Debt / EBITDA (2008-2016)



Source(s): S&P Capital IQ