

Activision Blizzard (ATVI)

\$82.47 (As of 08/07/20)

Price Target (6-12 Months): **\$87.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/16/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:B

Value: D

Growth: B

Momentum: A

Summary

Activision Blizzard's second-quarter 2020 results were driven by robust performances of *Call of Duty*, *World of Warcraft* and *Overwatch*. Markedly, *Call of Duty* in-game net bookings more than doubled sequentially and were almost five times higher year over year, creating a new quarterly record. Moreover, solid demand for games amid coronavirus-led lockdowns and enforcement of shelter-at-home guidelines was witnessed in the reported quarter. *Candy Crush Saga* was once again the top-grossing franchise in the U.S. mobile app stores. Activision's enviable IP and growth in popular gaming franchises bode well for the long haul. Notably, its shares have outperformed the industry year to date. However, stiff competition from the likes of Electronic Arts and Take Two Interactive is a headwind.

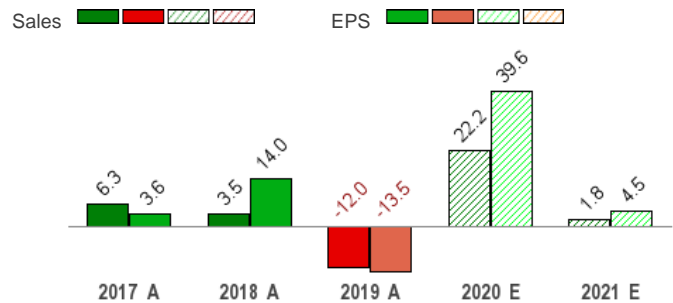
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$87.73 - \$44.91
20 Day Average Volume (sh)	6,552,960
Market Cap	\$63.7 B
YTD Price Change	38.8%
Beta	0.63
Dividend / Div Yld	\$0.41 / 0.5%
Industry	Toys - Games - Hobbies
Zacks Industry Rank	Top 11% (28 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	47.6%
Last Sales Surprise	23.1%
EPS F1 Est- 4 week change	18.5%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	26.6
P/E F1	26.3
PEG F1	2.6
P/S TTM	9.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,567 E	1,893 E	1,666 E	2,778 E	7,948 E
2020	1,522 A	2,078 A	1,681 E	2,514 E	7,805 E
2019	1,258 A	1,207 A	1,214 A	2,708 A	6,388 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.59 E	\$0.78 E	\$0.67 E	\$1.24 E	\$3.28 E
2020	\$0.58 A	\$0.97 A	\$0.61 E	\$1.05 E	\$3.14 E
2019	\$0.31 A	\$0.38 A	\$0.32 A	\$1.23 A	\$2.25 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/07/2020. The reports text is as of 08/10/2020.

Overview

Activision Blizzard, Inc. is a leading developer and publisher of console, online and mobile games. The company's *Call of Duty* is one of the most popular gaming franchises globally. Its *Overwatch League* can be considered a pioneer of the esports concept.

Activision Blizzard benefited from the shift to digital download format. The company's policy of updating games all the year round increased revenue visibility and stability.

Moreover, the acquisition of King Digital in 2016 fortified Activision's footprint in the mobile genre. King's *Candy Crush* was the top-grossing franchise in U.S. app stores during 2019.

Activision reported revenues of \$6.49 billion in 2019. International revenues accounted for 48.5% of revenues.

The Santa Monica, CA-based company operates under three major segments and incorporates studio, media networks and distribution businesses under the "Others" segment.

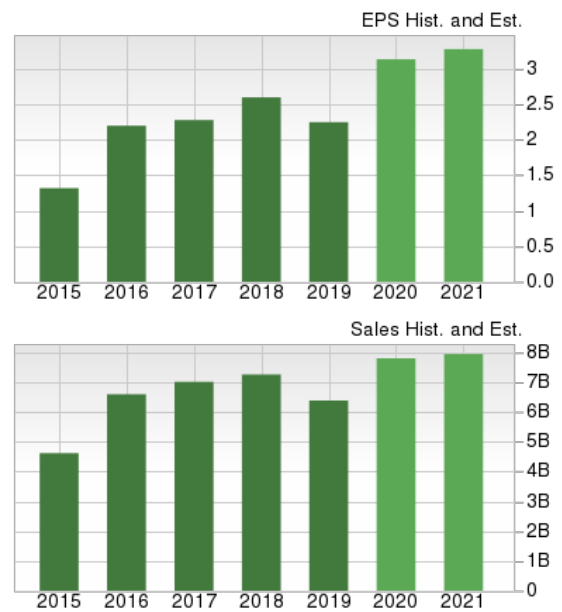
Activision creates and publishes games for consoles, desktops, mobile and tablet. Franchises under this segment include *Call of Duty*, *Crash* and *Spyro*. The segment generated revenues of \$2.22 billion and accounted for almost 37.2% of 2019 revenues.

Blizzard publishes games particularly for the PC format. It also maintains a proprietary online gaming service, Blizzard Battle.net, which facilitates digital distribution of Blizzard content and selected Activision content, online social connectivity, and the creation of user-generated content. The *Overwatch League* comes under this segment. The segment generated revenues of \$1.72 billion and accounted for 28.8% of revenues.

King operates as an independent unit. The segment generated revenues of \$2.03 billion and accounted for 34% of revenues.

The Other division includes Activision Blizzard Studios that makes original film and television content based on the company's huge IP library. The segment also consists Activision Blizzard Distribution business.

Activision faces stiff competition from the likes of Electronic Arts, Nintendo, Zynga and Tencent in the video gaming space.



Reasons To Buy:

- ▲ Activision popularity is primarily driven by its well-known franchises, which will continue to fuel top-line growth. *Call of Duty* is one of the biggest growth drivers for the company. The game has been the top-selling console franchise for Activision in 10 of the last 11 years. The latest title, *Call of Duty: Modern Warfare* has sold more units than *Call of Duty: Black Ops 4*. Activision stated that it will make frequent content updates to *Call of Duty* and expand the franchise's presence across platforms and geographies. *Call of Duty: Warzone* was launched on Mar 10, 2020 and the update has attracted more than 75 million players to date. *Call of Duty Mobile*, launched in October 2019, continues to play an important part in driving user base. The success of *World of Warcraft Classic* also indicates an expanding portfolio, which will benefit the company's top line in the long haul.
- ▲ Compared with the physical platform, digital games are more profitable due to minimum packaging cost. This cost effectiveness will help publishers to use the digital format to keep a popular franchise running profitably over a longer period of time. Notably, Digital revenues contributed 76% of total revenues in 2019. Additionally, Activision has been trying to adopt an all year-round model instead of a launch-based model in which majority earnings and profits are derived in the first week to boost engagement. This bodes well for long-term performance.
- ▲ King's dominance in the lucrative mobile gaming arena has improved Activision's prospects. Per Newzoo, by 2022, more than 50% of game market revenues will come from mobile games. Notably, King's *Candy Crush* remained the top-grossing franchise in U.S. app stores in 2019. Moreover, *Candy Crush Saga* was the top-grossing title in U.S. app stores in 2019, per data from App Annie, cited by Activision. King continues to emphasize on growing *Candy Crush's* reach and monetize the game by providing exciting in-game content. Solid growth in advertising net bookings in the second-quarter, despite coronavirus-led disruption on ad spending is very much encouraging. King's innovative pipeline of games is a key catalyst.
- ▲ Activision Blizzard has long been eyeing the lucrative esports market. With continued increases in viewership, corporate sponsorships and growing media coverage, esports is here to stay. Newzoo expects the esports industry to generate revenues of \$1.8 billion by 2022. The company is ramping up investments in esports, live services and other tools to boost user engagement. In the first quarter of 2020, the *Call of Duty League* was launched with 12 city-based teams and YouTube as Activision's new broadcasting partner for esports leagues and events. Additionally, the *Overwatch League* successfully moved to online play and remote production during the second-quarter due to the coronavirus outbreak.
- ▲ Activision's strong liquidity makes the stock attractive to investors. As of Jun 30, 2020, cash and cash equivalents were \$6.34 billion compared with \$5.91 billion as of Mar 31, 2020. Moreover, long-term debt as of Jun 30, 2020, was \$2.68 billion, flat sequentially. Further, Activision raised dividend payout by 11% compared to 2019-level, which reflects strong liquidity and solid free cash flow generation ability. On a trailing-12 month basis, free cash flow increased 17% to \$2.04 billion.

Activision's enviable IP, innovative gaming pipeline, strength in digital business and foray into esports bodes well for long-term growth.

Reasons To Sell:

- ▼ Video games are hit driven. Though Activision has a powerful line-up of games that can be repeatedly upgraded, there is no assurance that a particular game will be a hit. The video game business is highly cyclical and heavily dependent on time-to-time upgrade/introduction of new game software and hardware systems. Activision's costs are likely to shoot up in the near term as the company is trying to deliver popular franchises quickly than expected to aid top-line results.
- ▼ Activision's dependence on handful of its franchises namely *Call of Duty*, *World of Warcraft*, *Overwatch* and King Digital's *Candy Crush* that make up more than 70% of its revenues remains a concern. Underperformance of any title is bound to negatively impact revenues. Moreover, Blizzard's revenues and monthly active users (MAUs) in 2019 decreased due to the lack of major game releases
- ▼ The video game publishing industry is intensely competitive. Activision faces stiff competition from the likes of Electronic Arts, Nintendo, Zynga and Tencent. The resultant pressure could tell on margins and also lead to market share losses. On the other hand, continued investment in the digital market may also hurt its profitability in the near term.

Activision's dependence on a few franchises is concerning. Plus, hit driven and competitive nature of video game industry may negatively impact the company's growth.

Last Earnings Report

Activision Q2 Earnings & Revenues Beat on Coronavirus Push

Activision Blizzard's second-quarter 2020 non-GAAP earnings of 81 cents per share jumped 52.8% year over year.

Consolidated revenues surged 74.4% year over year to \$2 billion. Adjusting for net effect from the recognition of deferred revenues and elimination of intersegment revenues, total revenues jumped 38.4% to \$1.93 billion.

The Zacks Consensus Estimate for earnings and revenues was pegged at 68 cents per share and \$1.69 billion, respectively.

For the quarter ended Jun 30, 2020, overall Monthly Active Users (MAUs) were 428 million compared with 327 million as of Jun 30, 2019.

Activision Blizzard's net bookings increased 72.2% year over year to \$2.08 billion. Net bookings from digital channels were \$1.82 billion, up 80.2% year over year.

Notably, in-game net bookings were \$1.37 billion, up 76.6% year over year.

Quarter Ending 06/2020

Report Date	Aug 04, 2020
Sales Surprise	23.12%
EPS Surprise	47.62%
Quarterly EPS	0.97
Annual EPS (TTM)	2.95

Top-Line Details

Product sales (27.6% of revenues) were \$533 million, up 48.5% year over year. Subscription, licensing and other revenues (72.4% of revenues) increased 35% to \$1.40 billion.

Based on distribution channels, Activision Blizzard reported retail-channel sales of \$168 million, down 13% year over year. However, digital online revenues of \$1.59 billion were up 46.5% from the year-ago quarter. Other revenues improved 48% year over year to \$173 million.

Further, on the basis of platforms, revenues from mobile and ancillary (32.2% of revenues) rose 21.7% year over year to \$622 million. Additionally, PC revenues (24.9% of revenues) jumped 33.5% year over year to \$482 million. Moreover, revenues from console (33.9% of revenues) surged 61% year over year to \$655 million.

On a geographic basis, revenues from the Americas (57.6% of revenues) increased 45.5% year over year to \$1.11 billion. Europe, the Middle East and Africa revenues (31.8% of revenues) were up 34% year over year to \$615 million. Moreover, revenues from the Asia Pacific (10.6% of revenues) increased 18.5% year over year to \$205 million.

Segment Details

Activision (49.5% of revenues) revenues surged 270.5% year over year to \$993 million. The division had 125 million MAUs as of Jun 30, 2020 compared with 37 million as of Jun 30, 2019.

Call of Duty: Warzone has reached more than 75 million players to date. Further, *Call of Duty* in-game net bookings more than doubled sequentially and were almost five times higher year over year, creating a new quarterly record.

Call of Duty Mobile witnessed strong sequential growth in engagement and player investment, as well as monthly seasonal-content addition in the quarter under review.

Blizzard (23% of revenues) revenues of \$461 million increased 20.1% from the year-ago quarter. Blizzard had 32 million MAUs as of Jun 30, 2020, unchanged year over year.

World of Warcraft's reach and engagement increased sequentially, as shelter-at-home conditions further boosted the franchise's strong trajectory.

Additionally, *Overwatch* engagement grew year over year, including among returning players during the quarter.

King's (27.6% of revenues) revenues of \$553 million increased 10.8% year over year. MAUs were 271 million as of Jun 30, 2020, compared with 258 million as of Jun 30, 2019.

Candy Crush franchise MAUs grew by a double-digit percentage year over year. *Candy Crush* was once again the top-grossing franchise in the U.S. mobile app stores.

Advertising net bookings grew year over year in the second quarter.

Operating Details

Product development expense increased 22.8% year over year to \$280 million. Sales & marketing expenses were \$236 million, up 25.5% year over year.

However, general & administrative expenses decreased 3.2% year over year to \$149 million.

Total costs & expenses on a non-GAAP basis increased 17.6% year over year to \$1.12 billion in the reported quarter.

On a non-GAAP basis, operating income was \$811 million, up 83.1% year over year.

Balance Sheet & Cash Flow

As of Jun 30, 2020, cash and cash equivalents were \$6.34 billion compared with \$5.91 billion as of Mar 31, 2020.

Long-term debt as of Jun 30, 2020, was \$2.68 billion, flat sequentially.

Operating cash flow surged 399% year over year to \$768 million. Free cash flow jumped 494% year over year to \$755 million.

On a trailing-12 month basis, free cash flow increased 17% to \$2.04 billion.

Guidance

For third-quarter 2020, Activision Blizzard expects non-GAAP revenues of \$1.80 billion and earnings of 75 cents per share. Net bookings are expected to be \$1.65 billion.

For 2020, Activision Blizzard anticipates non-GAAP revenues of \$7.28 billion (up from previous guidance of \$6.80 billion) and earnings of \$2.87 per share (up from previous guidance of \$2.62). Net bookings are expected to be \$7.63 billion.

Recent News

On Jun 22, Activision Blizzard announced that *Crash Bandicoot 4: It's About Time* will be available for PlayStation 4 and 4 Pro, Xbox One and One X on Oct 2, 2020.

On May 12, Activision Blizzard announced that *Tony Hawk's Pro Skater 1 and 2* remastered will be available on Sep 4, 2020 for PlayStation 4 & 4 Pro, the family of Xbox One devices from Microsoft, including the Xbox One X, as well as on PC through the Epic platform.

On May 7, *The Overwatch League* and *Call of Duty League*, two Activision Blizzard operated esports leagues, and Sportradar announced an agreement for a comprehensive integrity program to protect both leagues from betting-related corruption.

On Mar 31, Activision announced the availability of *Call of Duty: Modern Warfare 2 Campaign Remastered* on PlayStation 4.

On Mar 17, Activision unveiled the new free-to-play Demon Hunter class for Blizzard's *Hearthstone* game alongside *Ashes of Outland* expansion pack to be released on Apr 7.

On Mar 10, Activision announced the release of free-to-play and free-for-everyone, *Call of Duty: Warzone* available worldwide on PS4, Xbox One, and PC.

Valuation

Activision shares are up 38.8% in the year-to-date period and 75.2% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 26.9%, while the same in the Zacks Consumer Discretionary sector is down 5.3%, in the year-to-date period. Over the past year, the Zacks sub-industry and the sector are up 44.3% and 5.3%, respectively.

The S&P 500 index is up 3.9% in the year-to-date period and 16.4% in the past year.

The stock is currently trading at 25.58X trailing 12-month earnings, which compares to 30.33X for the Zacks sub-industry, 33.58X for the Zacks sector and 22.83X for the S&P 500 index.

Over the past five years, the stock has traded as high as 31.76X and as low as 16.88X, with a 5-year median of 24.44X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$87 price target reflects 26.86X trailing 12-month earnings.

The table below shows summary valuation data for ATVI

Valuation Multiples - ATVI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	25.58	30.33	33.58	22.83
	5-Year High	31.76	30.6	33.58	22.83
	5-Year Low	16.88	19.51	16.12	15.25
	5-Year Median	24.44	25.48	19.84	17.55
P/S F12M	Current	8.04	6	2.39	3.67
	5-Year High	9	6.07	2.95	3.67
	5-Year Low	3.46	3.5	1.68	2.53
	5-Year Median	5.68	4.81	2.5	3.04
P/B TTM	Current	4.65	4.93	3.26	4.58
	5-Year High	6.25	6.64	4.95	4.58
	5-Year Low	2.44	3.11	2.22	2.83
	5-Year Median	3.59	4.17	4.21	3.73

As of 08/07/2020

Industry Analysis Zacks Industry Rank: Top 11% (28 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Electronic Arts Inc. (EA)	Outperform	1
Glu Mobile Inc. (GLUU)	Neutral	4
Hasbro, Inc. (HAS)	Neutral	3
JAKKS Pacific, Inc. (JAKK)	Neutral	3
Mattel, Inc. (MAT)	Neutral	2
Nintendo Co. (NTDOY)	Neutral	3
TakeTwo Interactive Software, Inc. (TTWO)	Neutral	2
Zynga Inc. (ZNGA)	Underperform	5

Industry Comparison Industry: Toys - Games - Hobbies				Industry Peers		
	ATVI	X Industry	S&P 500	EA	HAS	MAT
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	1	3	2
VGM Score	B	-	-	F	D	F
Market Cap	63.66 B	7.23 B	23.30 B	41.57 B	10.52 B	3.94 B
# of Analysts	15	6.5	14	14	7	4
Dividend Yield	0.50%	0.00%	1.76%	0.00%	3.54%	0.00%
Value Score	D	-	-	F	B	D
Cash/Price	0.09	0.14	0.07	0.15	0.10	0.12
EV/EBITDA	27.98	21.88	13.32	21.72	14.84	22.03
PEG Ratio	2.60	2.81	2.94	3.94	1.68	NA
Price/Book (P/B)	4.65	4.52	3.19	5.34	3.98	45.77
Price/Cash Flow (P/CF)	29.38	26.83	12.51	26.83	12.25	28.50
P/E (F1)	26.26	24.67	22.02	26.62	23.05	NA
Price/Sales (P/S)	9.11	3.51	2.53	7.18	2.12	0.92
Earnings Yield	3.81%	3.78%	4.37%	3.76%	4.34%	-1.32%
Debt/Equity	0.20	0.08	0.77	0.05	1.82	33.11
Cash Flow (\$/share)	2.81	2.34	6.94	5.37	6.27	0.40
Growth Score	B	-	-	B	F	D
Hist. EPS Growth (3-5 yrs)	13.15%	14.93%	10.46%	14.93%	2.05%	NA
Proj. EPS Growth (F1/F0)	14.06%	27.02%	-6.80%	91.12%	1,852.63%	-116.29%
Curr. Cash Flow Growth	-23.97%	-3.32%	5.39%	15.43%	-3.32%	-214.17%
Hist. Cash Flow Growth (3-5 yrs)	9.90%	6.23%	8.55%	7.26%	5.21%	-28.91%
Current Ratio	3.02	2.09	1.33	2.61	1.61	1.47
Debt/Capital	16.36%	12.77%	44.50%	4.85%	64.62%	97.07%
Net Margin	25.96%	10.40%	10.13%	34.27%	7.58%	-5.82%
Return on Equity	17.66%	17.69%	14.39%	21.32%	18.71%	-51.03%
Sales/Assets	0.36	0.70	0.51	0.52	0.57	0.83
Proj. Sales Growth (F1/F0)	19.97%	2.59%	-1.51%	14.02%	15.13%	-5.07%
Momentum Score	A	-	-	F	F	B
Daily Price Chg	-5.03%	0.00%	0.90%	-2.01%	-0.18%	-0.57%
1 Week Price Chg	3.30%	0.00%	0.14%	4.72%	-6.23%	-2.03%
4 Week Price Chg	2.27%	2.12%	8.95%	3.74%	7.34%	12.14%
12 Week Price Chg	13.03%	22.94%	18.90%	22.94%	18.77%	40.25%
52 Week Price Chg	67.18%	26.49%	1.18%	51.20%	-34.20%	-15.41%
20 Day Average Volume	6,552,960	612,330	2,057,775	2,054,325	1,122,423	3,484,357
(F1) EPS Est 1 week change	17.25%	0.00%	0.00%	-1.53%	0.00%	0.00%
(F1) EPS Est 4 week change	18.45%	5.11%	1.36%	9.28%	-6.23%	54.33%
(F1) EPS Est 12 week change	19.38%	5.40%	1.57%	10.05%	-6.98%	51.67%
(Q1) EPS Est Mthly Chg	56.82%	-1.79%	0.54%	-140.52%	-3.58%	1.63%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	B
Momentum Score	A
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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