

Discovery, Inc.(DISCA)

\$22.28 (As of 03/12/20)

Price Target (6-12 Months): **\$23.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 11/13/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: A

Growth: A

Momentum: D

Summary

Discovery's fourth-quarter 2019 results reflected strong domestic advertising growth, driven by increase in pricing and continued monetization of digital content offerings and inventory. International advertising growth was driven by contribution from the UKTV Lifestyle business and progress in direct-to-consumer initiatives. Moreover, the uptick in distribution revenues was owing to content licensing arrangements and higher affiliate rates in Discovery's Latin America business unit. Moreover, higher affiliate rates and monetization of direct-to-consumer initiatives in Europe and Asia boosted revenues in the reported quarter. However, incremental spending on direct-to-consumer initiatives and international business is expected to keep margins under pressure. Discovery shares have underperformed the industry in the past year.

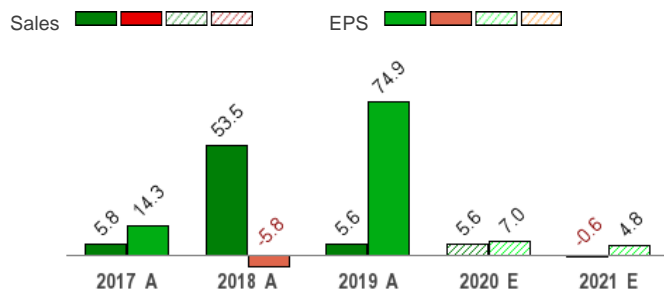
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$33.65 - \$20.88
20 Day Average Volume (sh)	6,868,519
Market Cap	\$11.7 B
YTD Price Change	-32.0%
Beta	1.53
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Broadcast Radio and Television
Zacks Industry Rank	Top 32% (82 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	5.4%
Last Sales Surprise	0.1%
EPS F1 Est- 4 week change	-2.4%
Expected Report Date	05/07/2020
Earnings ESP	0.0%
P/E TTM	6.0
P/E F1	5.6
PEG F1	0.3
P/S TTM	1.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,900 E	3,085 E	2,845 E	3,068 E	11,699 E
2020	2,797 E	2,979 E	3,045 E	2,963 E	11,769 E
2019	2,707 A	2,885 A	2,678 A	2,874 A	11,144 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$4.14 E
2020	\$0.89 E	\$1.03 E	\$0.76 E	\$0.93 E	\$3.95 E
2019	\$0.87 A	\$0.98 A	\$0.87 A	\$0.98 A	\$3.69 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 03/12/2020. The reports text is as of 03/13/2020.

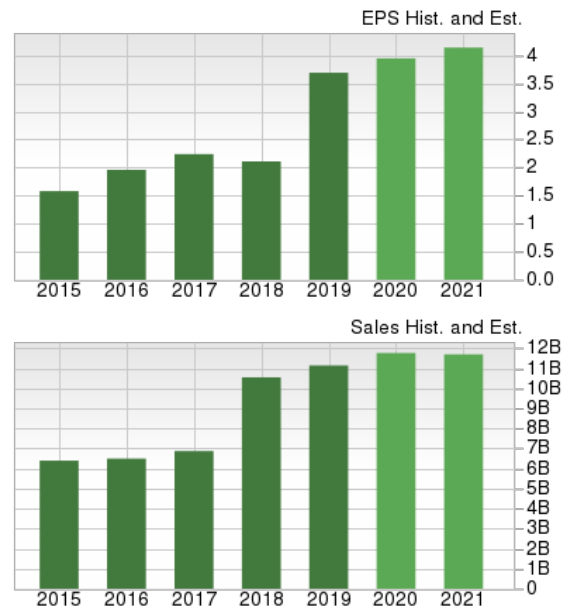
Overview

Discovery Communications is now known as Discovery, Inc. following the completion of the acquisition of Scripps Networks Interactive on Mar 6, 2018. The company offers original and purchased content as well as live events to 3.8 billion cumulative subscribers plus viewers worldwide. Discovery distributes content in the United States and to 220 other countries plus territories in more than 50 languages.

The company's global portfolio of networks includes non-fiction television brands, such as Discovery Channel, HGTV, Food Network, TLC, Animal Planet, Investigation Discovery, Trvl Channel, OWN, Science Channel and MotorTrend (previously known as Velocity, domestically and currently known as Turbo in most international countries).

Moreover, the company's international portfolio constitutes Eurosport, a leading sports entertainment provider and broadcaster of the Olympic Games across Europe, TVN, a Polish media company, as well as Discovery Kids, a leading children's entertainment brand in Latin America.

Discovery also participates in joint ventures including Group Nine Media. The company is a participant in the multi-platform venture with Chip and Joanna Gaines, which plans to launch linear networks, SVOD and TV Everywhere (TVE) products in 2020.



Discovery reported revenues of \$11.14 billion in 2019. It operates through two reportable segments: U.S. Networks and International Networks.

U.S. Networks segment owns and operates 18 national television networks. In 2019, the segment contributed to 63.6% of the company's total revenue base. Moreover, advertising, distribution and other revenues were 60%, 39% and 1%, respectively, of the total segmental revenues.

International Networks segment primarily consists of the national pan-regional TV networks of the company. In 2019, the segment accounted for 36.3% of the company's total revenue stream. Moreover, advertising, distribution and other revenues were 45%, 52% and 3%, respectively, of the total segment revenues.

Other revenues were \$11 million in 2019. On Apr 30, 2018, Discovery sold 88% controlling equity stake in the Education Business to Francisco Partners.



Reasons To Buy:

- ▲ Discovery is one of the world's largest pay-TV programmers, with approximately 4 billion cumulative subscribers. The company is benefiting from content portfolio strength, post the Scripps Networks' buyout. The acquisition also helped the company to expand its international footprint, especially in regions like Europe, Latin America and the Nordics. Cost synergies from the merger drove profitability as adjusted OIBDA grew 12% in 2019. For 2020, Discovery currently expects solid mid-single-digit revenue growth on constant currency basis from 2019-levels.
- ▲ Discovery is a dominant name in the pay-TV market. The company's expanding market share driven by solid viewership of multiple channels including Discovery Channel, Animal Planet, Food, HDTV MotorTrend, Science, TLC, ID, Oprah, and Eurosport is a key catalyst. Notably, Discovery generated more than \$700 million of direct-to-consumer revenues in 2019 and is well-poised to exceed \$1 billion (roughly 10% of total revenues) in 2020.
- ▲ Moreover, expanding sports coverage based on partnership with the likes of PGA TOUR, Tiger Woods and Olympics is a major growth driver. In Oct 2018, the company entered a 12-year agreement with PGA Tour worth about \$2 billion to manage TV and digital rights for golf events in territories outside the United States. Additionally, GOLFTV inked a partnership with the European Tour to broadcast and stream a number of golf events. Apart from GOLFTV, Discovery's European sports network, EuroSport won European multi-platform broadcast and distribution rights for four Olympic Games between 2018 and 2024. Additionally, the platform has rights to prominent pro leagues in soccer and tennis, among others.
- ▲ Apart from PGA and European Tour, partnerships with the likes of AT&T, Hulu, Sling TV and Bilibili are helping Discovery rapidly penetrate the online viewing market. Moreover, the company's expanding direct-to-consumer offerings are expected to aid its top line in the long haul. Through the Eurosport Player video streaming service, the company is offering premium and localized sports content to fans across 52 markets in Europe. Dplay, the company's real-life entertainment streaming service, is now available in 10 markets including the U.K., Ireland, Spain, the Nordics, Japan and Italy. In Germany, Discovery partnered with ProSiebenSat.1 to launch the streaming service, Joyn. In Poland, it teamed up with Cyfrowy Polsat to create a video streaming platform for disseminating Polish content.
- ▲ Discovery's strong free cash-flow generation capability makes it an attractive stock. The company ended 2019 with \$3.1 billion of free cash flow compared with its targeted \$3 billion, which represented a free cash flow conversion of more than 67% of adjusted OIBDA. Moreover, management expects to generate healthy free cash flow in 2020 courtesy adjusted OIBDA growth and continued margin expansion.

Discovery's acquisition of Scripps significantly expands content portfolio and international footprint, which along with an expanding sports coverage and partnerships are key catalysts.

Reasons To Sell:

- ▼ The internal dynamics of the U.S. pay-TV industry has been gradually shifting from cable TV operators to large telecom operators and low-cost over-the-top service providers. Online video streaming service providers such as Netflix, Hulu and YouTube, among others, have become a severe threat to legacy pay-TV content providers because of their extremely cheap source of TV programming and solid content. This doesn't bode well for Discovery, as loss of domestic subscribers is a major concern.
- ▼ Discovery's top-line growth has also been negatively impacted by softness in certain international markets. Cancellation of gaming events globally due to the coronavirus outbreak is a major headwind to the company. Moreover, unfavorable foreign exchange is expected to hurt the top line (by \$120 million) and adjusted OIBDA (by \$60 million) in 2020.
- ▼ High costs continue to limit Discovery's bottom-line growth. The company expects to spend an additional \$300 million on direct-to-consumer initiatives in 2020. Moreover, the company expects to incur an Olympics-driven adjusted OIBDA loss in the third quarter of 2020.
- ▼ Discovery's highly leveraged balance sheet is a significant concern for investors. As of Dec 31, 2019, the company had \$15.42 billion of consolidated debt with a net-debt position of \$13.87 billion. Further, leverage is expected to increase in 2020 due to the Olympics and continued share repurchases. Moreover, the Olympics event is expected to reduce free cash flow in 2020.

The continuing loss of U.S. subscribers due to competition, sluggishness in International Networks, unfavorable foreign exchange and high leverage are major concerns.

Last Earnings Report

Discovery Q4 Earnings Beat Mark, Revenues Rise Y/Y

Discovery reported fourth-quarter 2019 adjusted earnings of 98 cents per share, beating the Zacks Consensus Estimate by 5.4% and also increasing 19.5% year over year.

Revenues increased 2.3% year over year to \$2.87 billion and beat the consensus mark by 0.1% as well. Also, excluding the foreign exchange impact, revenues increased 4%.

This year-over-year growth was driven by an increase in advertising (55.6% of revenues) and distribution (41.9% of revenues) revenues.

Quarter Ending **12/2019**

Report Date	Feb 27, 2020
Sales Surprise	0.11%
EPS Surprise	5.38%
Quarterly EPS	0.98
Annual EPS (TTM)	3.70

Top-Line Details

Advertising revenues grew 1.5% year over year to \$1.60 billion. Distribution revenues increased 4.8% from the year-ago quarter to \$1.20 billion.

Other revenues were \$73 million, down 15.1% from the year-ago quarter.

U.S. Networks (61% of revenues) revenues rose 1.7% from the year-ago quarter to \$1.75 billion. Advertising and distribution revenues were up 1% and 4.5%, respectively.

Advertising growth was driven by increases in pricing, continued monetization of digital content offerings and inventory. Rise in distribution revenues was driven by increased contractual affiliate rates and additional carriage on streaming platforms.

International Networks revenues (38.9% of revenues) rose 3.2% year over year to \$1.12 billion. Advertising and distribution revenues were up 2.4% and 5.1%, respectively.

However, excluding the foreign exchange impact, International Networks revenues grew 7% as advertising revenues increased 5% and distribution revenues 10% on a year-over-year basis.

Advertising growth was driven by contribution from the UKTV Lifestyle business and progress in direct-to-consumer initiatives.

Moreover, the uptick in distribution revenues was owing to content licensing arrangements and higher affiliate rates in Discovery's Latin America business unit. Moreover, higher affiliate rates and monetization of direct-to-consumer initiatives in Europe and Asia boosted revenues in the reported quarter.

Operating Details

In the fourth quarter, selling, general and administrative (SG&A) expenses increased 20.7% from the year-ago quarter to \$793 million.

Adjusted operating income before depreciation & amortization (OIBDA) decreased 7.7% from the year-ago quarter to \$1.11 billion. Excluding foreign exchange impact, OIBDA grew 9%.

U.S. Networks adjusted OIBDA decreased 4% from the year-ago quarter to \$925 million.

Moreover, International Networks adjusted OIBDA declined 10% from the year-ago quarter to \$315 million. Excluding forex impact, adjusted OIBDA increased 5%.

GAAP operating income dipped 0.8% year over year to \$705 million.

Balance Sheet

As of Dec 31, 2019, cash & cash equivalents were \$1.55 billion compared with \$813 million as of Sep 30, 2019.

Moreover, as of Dec 31, 2019, long-term debt was \$14.81 billion, higher than \$14.76 billion as of Sep 30, 2019.

Free cash flow was \$1.13 billion, up from \$884 million reported in the previous quarter.

Discovery repurchased nearly 12 million shares for \$337 million in the reported quarter. In February 2020, the company authorized an additional common stock repurchase program worth \$2 billion.

Recent News

On Oct 28, Discovery and Comscore announced a number of multi-year strategic agreements for the use of the latter's audience measurement and consumer insights tools.

On Sep 25, Discovery announced the launch of Food Network Kitchen, a first-of-its-kind direct-to-consumer product, in late October 2019 in the United States. It will also be available across iOS (iPhone and iPad) and Android mobile devices. Food Network Kitchen will be rolled out across additional platforms and devices in 2020. Moreover, Discovery and Amazon have collaborated to offer Food Network Kitchen through Amazon Alexa and Echo Show, Fire Tablets, Fire TV streaming media devices and Fire TV Edition smart TVs.

Valuation

Discovery shares are down 20.3% in the past six-month period and 18.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are down 12.7% and 25.6% in the past six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are down 17.4% and 22.2%, respectively.

The S&P 500 index is down 8.2% in the past six-month period and 3.4% in the past year.

The stock is currently trading at 5.57X forward 12-month earnings, which compares to 20.3X for the Zacks sub-industry, 16.03X for the Zacks sector and 15.84X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.10X and as low as 5.57X, with a 5-year median of 10.46X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$23 price target reflects 5.75X forward 12-month earnings.

The table below shows summary valuation data for DISCA

Valuation Multiples - DISCA					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	5.57	20.3	16.03	15.84
	5-Year High	18.1	34.44	23.23	19.34
	5-Year Low	5.57	20.3	16.03	15.18
	5-Year Median	10.46	25.86	19.88	17.42
P/S F12M	Current	0.99	7.54	1.8	2.91
	5-Year High	2.22	13.42	3.19	3.44
	5-Year Low	0.73	6.61	1.8	2.54
	5-Year Median	1.44	9.66	2.53	3
EV/Sales TTM	Current	2.24	7.83	2.63	2.76
	5-Year High	3.94	15.82	4.01	3.46
	5-Year Low	2.07	7.83	2.63	2.14
	5-Year Median	2.82	11.11	3.41	2.82

As of 03/12/2020

Industry Analysis Zacks Industry Rank: Top 32% (82 out of 253)



Top Peers

DISH Network Corporation (DISH)	Outperform
Amazon.com, Inc. (AMZN)	Neutral
Cable One, Inc. (CABO)	Neutral
Comcast Corporation (CMCSA)	Neutral
The Walt Disney Company (DIS)	Neutral
Fox Corporation (FOXA)	Neutral
Netflix, Inc. (NFLX)	Neutral
AT&T Inc. (T)	Neutral

Industry Comparison Industry: Broadcast Radio And Television				Industry Peers		
	DISCA Neutral	X Industry	S&P 500	CMCSA Neutral	DIS Neutral	NFLX Neutral
VGM Score	A	-	-	B	F	F
Market Cap	11.70 B	486.54 M	17.38 B	159.08 B	165.76 B	138.33 B
# of Analysts	6	2	13	13	6	13
Dividend Yield	0.00%	0.00%	2.51%	2.40%	1.92%	0.00%
Value Score	A	-	-	B	D	F
Cash/Price	0.12	0.16	0.05	0.03	0.03	0.03
EV/EBITDA	3.41	5.61	10.90	7.43	10.32	12.33
PEG Ratio	0.29	0.46	1.54	1.01	3.37	1.71
Price/Book (P/B)	1.02	0.82	2.35	1.90	1.75	18.25
Price/Cash Flow (P/CF)	1.67	2.42	9.60	5.81	11.61	12.37
P/E (F1)	5.64	6.42	13.98	10.86	17.19	51.43
Price/Sales (P/S)	1.05	0.58	1.89	1.46	2.21	6.86
Earnings Yield	17.73%	11.74%	7.07%	9.22%	5.82%	1.94%
Debt/Equity	1.29	1.29	0.70	1.23	0.40	1.95
Cash Flow (\$/share)	13.32	2.13	7.01	6.01	7.91	25.49
Growth Score	A	-	-	A	F	F
Hist. EPS Growth (3-5 yrs)	11.87%	11.87%	10.85%	16.77%	5.67%	82.45%
Proj. EPS Growth (F1/F0)	6.96%	18.53%	5.99%	2.75%	-7.42%	48.41%
Curr. Cash Flow Growth	14.01%	0.53%	6.15%	21.54%	4.37%	26.74%
Hist. Cash Flow Growth (3-5 yrs)	17.30%	12.75%	8.52%	11.76%	7.57%	30.03%
Current Ratio	1.61	1.80	1.24	0.84	0.80	0.90
Debt/Capital	56.96%	56.96%	42.57%	55.43%	33.19%	66.06%
Net Margin	18.57%	7.70%	11.64%	11.98%	13.81%	9.26%
Return on Equity	24.05%	8.23%	16.74%	18.25%	10.23%	28.45%
Sales/Assets	0.34	0.37	0.54	0.42	0.37	0.66
Proj. Sales Growth (F1/F0)	5.61%	2.84%	3.54%	4.68%	15.53%	20.97%
Momentum Score	D	-	-	F	D	D
Daily Price Chg	-7.40%	-8.06%	-10.03%	-7.83%	-12.99%	-9.91%
1 Week Price Chg	-1.01%	-5.76%	-0.67%	-0.15%	-2.02%	-0.02%
4 Week Price Chg	-26.54%	-30.12%	-28.22%	-24.16%	-34.84%	-17.34%
12 Week Price Chg	-31.99%	-29.20%	-25.63%	-19.94%	-37.18%	-5.11%
52 Week Price Chg	-18.78%	-38.61%	-16.72%	-12.37%	-19.80%	-12.14%
20 Day Average Volume	6,868,519	76,313	3,061,271	30,665,552	19,594,080	6,861,402
(F1) EPS Est 1 week change	-0.42%	0.00%	0.00%	-0.29%	0.00%	1.12%
(F1) EPS Est 4 week change	-2.39%	0.00%	-0.32%	-0.65%	-0.96%	1.43%
(F1) EPS Est 12 week change	2.07%	0.00%	-0.65%	-3.15%	-4.81%	11.92%
(Q1) EPS Est Mthly Chg	-2.99%	0.00%	-0.62%	-1.21%	-2.83%	-0.05%

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	A
Growth Score	A
Momentum Score	D
VGM Score	A

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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