Electronic Arts Inc. (EA)

$106.51 (As of 04/06/20)

Price Target (6-12 Months): **$122.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 04/05/20) Prior Recommendation: Neutral	**Outperform**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**2-Buy**
	Zacks Style Scores:	VGM:D
	Value: D | Growth: C | Momentum: D	

Summary

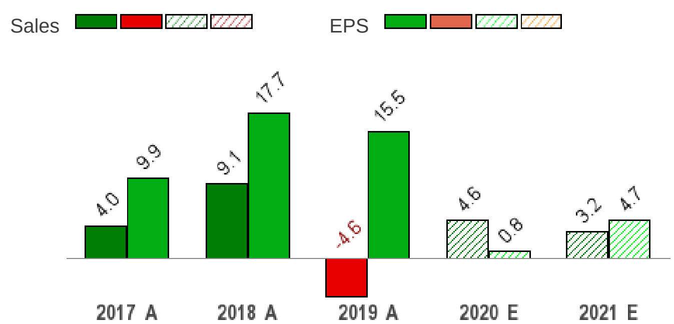
EA's net bookings and live services revenues are expected to benefit from portfolio strength and solid performance from titles like *Apex Legends*, *FIFA*, *Madden NFL*, *The Sims 4*, *Need For Speed Heat* and *Star Wars Jedi: Fallen Order*. EA SPORTS titles along with *Battlefield*, *Titanfall* and *Star Wars* are some of its biggest franchises driving active player accounts. Moreover, EA has a strong slate of releases for fiscal 2021 that includes four sports titles and four titles from smaller developers. Moreover, next-generation consoles and a new Battlefield game are expected to fuel growth in fiscal 2022. EA's shares have outperformed the industry on a year-to-date basis.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$114.13 - $85.69**
20 Day Average Volume (sh)	**5,422,375**
Market Cap	**$30.9 B**
YTD Price Change	**-0.9%**
Beta	**0.88**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**Toys - Games - Hobbies**
Zacks Industry Rank	**Top 6% (14 out of 253)**
Last EPS Surprise	**10.7%**
Last Sales Surprise	**0.7%**
EPS F1 Est- 4 week change	**-0.3%**
Expected Report Date	**05/05/2020**
Earnings ESP	**0.0%**
P/E TTM	**20.7**
P/E F1	**21.5**
PEG F1	**3.7**
P/S TTM	**5.7**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	826 E	1,379 E	1,770 E	1,352 E	5,338 E
2020	743 A	1,277 A	1,978 A	1,173 E	5,171 E
2019	798 A	1,222 A	1,609 A	1,364 A	4,944 A

EPS Estimates

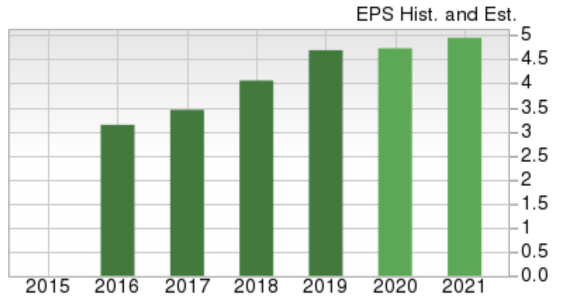
	Q1	Q2	Q3	Q4	Annual*
2021	$0.33 E	$1.12 E	$2.16 E	$1.20 E	$4.95 E
2020	-$0.02 A	$0.96 A	$2.79 A	$0.98 E	$4.73 E
2019	$0.26 A	$0.98 A	$2.08 A	$1.41 A	$4.69 A

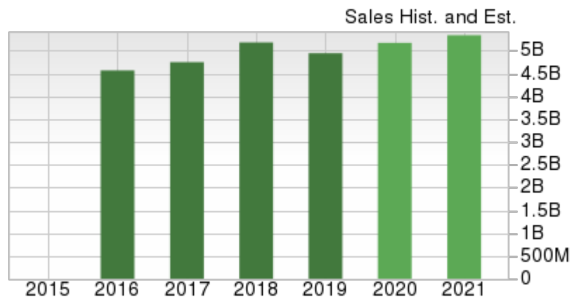
*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/06/2020. The reports text is as of 04/07/2020.

Overview

Headquartered in Redwood City, CA, Electronic Arts Inc. (EA) is a leading developer, marketer, publisher and distributor of interactive games (video game software and content).





Electronic Arts, popularly known as EA, distributes its gaming content and services through multiple distribution channels as well as directly to consumers (online and wirelessly) through its online portals — Origin and Play4Free.

EA games can be played on video consoles, personal computers, mobile devices, tablets and electronic readers. The company generates revenues from the sale of disk-based video game products (known as packaged goods), downloadable contents (DLCs), subscription, micro-transactions and advertising.

EA generated revenues of $4.95 billion in fiscal 2019, of which digital net revenues contributed 74.9% and the remaining were generated from packaged goods and others.

Moreover, net revenues from live services comprised 45% of total net revenues in fiscal 2019. Most popular live service is the Ultimate Team mode that accounted for 28% of revenues.

The company operates in three divisions — EA Studios, Maxis and EA Mobile. EA Studios includes DICE (Sweden), EA Canada (Canada), Tiburon (the United States), BioWare (Canada and the United States) and Visceral (the United States).

EA faces substantial competition from console and personal computer game publishers and diversified media companies that include Sony, Microsoft, Nintendo, Activision Blizzard, Take-Two Interactive and Ubisoft. In the mobile and social gaming market, the company competes with Glu Mobile and Zynga.

Reasons To Buy:

- EA has been the primary beneficiary of the ongoing shift from physical to digital versions of video games. Notably, contribution of the digital business to EA's revenues increased from 57% in fiscal 2017 to 67% in fiscal 2018 and 75% in fiscal 2019. The company expects the digital business to continue to grow primarily on the back of live services and a strong mobile business. Moreover, compared with the physical platform, digital games are more profitable due to minimum packaging cost. In addition, the company's freemium and extra content services are generating significant market traction, which is driving the top line.

EA has been the primary beneficiary of the ongoing shift from physical to digital versions of video games.Core franchises like *FIFA* and *The Sims* are driving growth.

- Esports is also helping EA to grow internationally in regions like China, Korea, the Middle East and more. Apart from expanding its presence, esports is enabling the company to expand global user base.

- EA's popularity is primarily driven by its well-known franchises, which will continue to fuel the top line. EA SPORTS titles along with *Battlefield*, *Titanfall* and *Star Wars* are some of its biggest franchises. Additionally, the video game company is gaining traction with *The Sims* franchise, which is a positive. Notably, *The Sims 4* now has more than 20 million unique players worldwide on a life-to-date basis.

- EA's expanding mobile gaming portfolio is expected to drive growth. Moreover, the company is receiving sponsor engagements and partnerships with industry leaders such as Eleague, Gfinity and PGL for *FIFA* Global series, which bode well. EA is also foraying into the world of AR/VR games.

- EA's latest battle royale (BR) game — *Apex Legends* — is an instant hit. The game has smashed the records of Epic Game's *Fortnite* in this genre. Notably, *Apex Legends* was the company's first free-to-play console game. The company is in talks with Tencent to bring the game to China. Notably, EA lacks significant presence in China apart from *FIFA* and a few mobile games. Thus, *Apex Legends* will boost EA's footprint in China's PC-gaming market, which is a positive. On Feb 4, 2020, the company is set to release Season 4 of *Apex Legends*.

Risks

- Video games are hit driven. Though EA has a powerful line up of games that can be repeatedly upgraded, there is no assurance that a particular game will be a hit. Moreover, the video game business is highly cyclical and heavily dependent on time-to-time upgrade/introduction of new game software and hardware systems.

- The video game publishing industry is intensely competitive. EA faces significant competition from the likes of Take Two Interactive and Activision Blizzard. The resultant pressure can exert pressure on margins and lead to market share losses. Lower volume of packaged goods sales are a drag on margins. EA's continued investment in the digital market may also hurt profitability in the near term.

- EA is dependent on few well-known franchises like *FIFA*, *Battlefield* and *Star Wars* for revenue generation. This doesn't bode well for the company. Notably, its much-awaited shooter looter game — *Anthem* — received lukewarm response from critics as well as players. The PC version of *Anthem* had average critic score of 61 out of 100 on Metacritic compared with Apex Legends score of 88. The company's failure to expand its game franchise is a major concern amid rising competition.

Last Earnings Report

Electronic Arts Q3 Earnings & Revenues Increase Y/Y

Quarter Ending	12/2019
Report Date	**Jan 30, 2020**
Sales Surprise	**0.71%**
EPS Surprise	**10.71%**
Quarterly EPS	**2.79**
Annual EPS (TTM)	**5.14**

Electronic Arts reported third-quarter fiscal 2020 earnings of $1.18 per share, which increased 37.2% year over year and comfortably beat management's guidance by 26 cents.

Revenues rose 23.6% year over year to $1.59 billion. Product revenues (44% of total revenues) were up 27% to $701 million. Service and other revenues (56% of total revenues) grew 21% to $892 million.

Excluding the change in deferred revenues of $428 million and mobile platform fees of $43 million, net bookings improved 22.9% year over year to $1.98 billion.

The Zacks Consensus Estimate for earnings and revenues were pegged at $2.52 per share and $1.96 billion, respectively.

Quarter Details

Digital net bookings were $1.44 billion, increasing 20% year over year and representing 77% of total net bookings.

EA's digital revenues (70.6% of total revenues) grew 23.8% year over year to $1.12 billion. Packaged goods and other segment revenues (29.4% of total revenues) were up 23.1% year over year to $469 million.

Further segregating digital revenues, full game download revenues increased 16% year over year to $286 million. Net bookings increased 16% year over year to $317 million.

Live services revenues rose 41% year over year to $677 million. Net bookings improved 27% year over year to $993 million, driven by *Apex Legends*, *FIFA* and *Madden NFL* Ultimate Teams (double-digit growth), and *Star Wars Jedi: Fallen Order*. *FIFA Online* performed well in Asia.

However, mobile games revenues decreased 11% year over year to $161 million. Including IP licensing deals, mobile revenues grew year over year at constant currency (cc). Net bookings declined 6% year over year to $134 million.

Based on its platforms, revenues from console increased 31% year over year to $1.16 billion. Net bookings from console rose 25% year over year to $1.05 billion.

Revenues from PC/browser were up 18% year over year to $257 million. Net bookings from PC/browser improved 21% year over year to $258 million.

However, revenues from mobile platform dropped 7% year over year to $169 million. Net bookings from mobile were down 6% year over year to $134 million.

Other revenues plunged 33% year over year to $4 million.

Important Game & Player Metrics

EA launched three games in the reported quarter — *Need for Speed Heat*, *Plants Versus Zombies: Battle for Neighborville*, and *Star Wars Jedi: Fallen Order*.

Sales of *Star Wars: Jedi Fallen Order* surpassed EA's fiscal year unit sales expectations of $6-8 million, the higher end of which was hit by the game in the third quarter itself. EA now anticipates selling more than 10 million units in the fiscal.

Moreover, *Madden NFL 20* is delivering the best performance in Madden's more than 30-year history.

Further, *FIFA* grew year over year in the third quarter. The addition of *VOLTA Football* to *FIFA 20* and the updates to *FIFA Ultimate Team* have boosted player engagement, with FUT matches up nearly 40% year over year since launch through the reported quarter.

Notably, *FIFA 20* is also the #1 most-engaged title in EA's subscription services. The company is set to launch South American club tournaments, CONMEBOL Libertadores and CONMEBOL Sudamericana as well as the eLibertadores — a new expansion to FIFA 20 Global Series esports competitions.

Additionally, *The Sims 4* now has more than 20 million unique players worldwide on a life-to-date basis.

Operating Details

EA's GAAP gross profit increased 23.9% from the year-ago quarter to $1.09 billion. Gross margin expanded 20 basis points (bps) on a year-over-year basis to 68.1%.

Operating expenses rose 14.2% from the year-ago quarter to $724 million. As a percentage of revenues, operating expenses contracted 370 bps to 45.4%.

As a percentage of revenues, marketing & sales (M&S) shrank 180 bps. Research & development (R&D) and general & administrative (G&A) expenses also contracted 150 bps and 30 bps, respectively.

Operating income on a GAAP basis surged 49.2% year over year to $361 million. Operating margin expanded 390 bps to 22.7% in the reported quarter.

Balance Sheet and Cash Flow

As of Dec 31, 2019, EA had $5.60 billion in cash and short-term investments compared with $4.88 billion as of Sep 30.

Net cash from operating activities in the reported quarter was $$1.10 billion compared with $37 million in the previous quarter.

EA repurchased 3.1 million shares for $305 million in the reported quarter. The company has $674 million available under its current program.

Guidance

For the fourth quarter of fiscal 2020, EA expects GAAP revenues of $1.325 billion. Net bookings are expected to be $1.152 billion.

EA anticipates operating expenses of $724 million. GAAP earnings are expected to be $1.05 per share.

For fiscal 2020, EA expects GAAP revenues of $5.475 billion (up from the previous guidance of $5.410 billion) and net bookings of $5.150 billion (up from the previous guidance of $5.125 billion).

Digital net revenues are expected to be $4.255 billion. Packaged goods & other net revenues are anticipated to be $1.220 billion.

Moreover, EA anticipates operating expenses of $2.730 billion for the fiscal.

Additionally, earnings are expected to be $9.90 per share.

Operating cash flow is estimated to be $1.725 billion.

Recent News

On Mar 26, EA and Nintendo announced that *Burnout Paradise Remastered* will be available on Nintendo Switch consoles in 2020.

On Mar 13, EA announced that it is suspending all live events for the company's competitive gaming series including the Apex Legends Global Series, EA SPORTS FIFA 20 Global Series, FIFA Online 4 Live Events and Madden NFL 20 Championship Series due to the coronavirus outbreak.

On Dec 17, EA and Respawn Entertainment announced the launch of the Apex Legends Global Series, the first International e-sports tournament for the franchise.

Valuation

Electronic Arts shares are down 0.9% in the year-to-date period but up 8.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are down 7.8% and 32.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is up 6% while the sector is down 26.7%.

The S&P 500 index is down 22.6% in the year-to-date period and 14.1% in the past year.

The stock is currently trading at 21.48X forward 12-month earnings, which compares to 25.15X for the Zacks sub-industry, 16.2X for the Zacks sector and 15.73X for the S&P 500 index.

Over the past five years, the stock has traded as high as 33.49X and as low as 18.01X, with a 5-year median of 25.21X. Our Outperform recommendation indicates that the stock will perform better than the market. Our $122 price target reflects 24.60X forward 12-month earnings.

The table below shows summary valuation data for EA

Valuation Multiples - EA

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	21.48	25.15	16.2	15.73
	5-Year High	33.49	30.46	23.23	19.34
	5-Year Low	18.01	19.51	16.15	15.19
	5-Year Median	25.21	25.1	19.87	17.44
P/S F12M	Current	5.96	4.66	1.6	2.72
	5-Year High	8.01	5.98	3.19	3.44
	5-Year Low	3.59	3.4	1.6	2.54
	5-Year Median	5.26	4.66	2.52	3
EV/Sales TTM	Current	4.69	4.6	2.35	2.47
	5-Year High	8.4	6.72	4.02	3.46
	5-Year Low	3.18	3.12	2.26	2.16
	5-Year Median	4.67	4.56	3.4	2.83

As of 04/06/2020

Industry Analysis **Zacks Industry Rank:** Top 6% (14 out of 253)

Top Peers

Mattel, Inc. **(MAT)**	Outperform
Activision Blizzard, Inc **(ATVI)**	Neutral
Glu Mobile Inc. **(GLUU)**	Neutral
Hasbro, Inc. **(HAS)**	Neutral
JAKKS Pacific, Inc. **(JAKK)**	Neutral
Nintendo Co. **(NTDOY)**	Neutral
Take-Two Interactive Software, Inc. **(TTWO)**	Neutral
Zynga Inc. **(ZNGA)**	Neutral

Industry Comparison Industry: Toys - Games - Hobbies

Industry Peers

	EA Outperform	X Industry	S&P 500	HAS Neutral	MAT Outperform	TTWO Neutral
VGM Score	D	-	-	D	A	F
Market Cap	30.85 B	6.31 B	18.06 B	9.75 B	2.86 B	13.76 B
# of Analysts	13	6	13	7	5	21
Dividend Yield	0.00%	0.00%	2.34%	3.82%	0.00%	0.00%
Value Score	D	-	-	C	B	F
Cash/Price	0.19	0.20	0.06	0.50	0.23	0.18
EV/EBITDA	21.44	20.49	11.15	9.58	17.67	23.00
PEG Ratio	3.72	2.03	1.87	1.37	NA	3.09
Price/Book (P/B)	4.30	3.70	2.46	3.00	5.81	5.73
Price/Cash Flow (P/CF)	23.69	21.31	9.59	11.36	20.67	19.26
P/E (F1)	21.52	23.76	15.66	16.99	142.07	27.99
Price/Sales (P/S)	5.73	3.44	1.92	2.07	0.63	4.80
Earnings Yield	4.65%	4.09%	6.30%	5.88%	0.73%	3.57%
Debt/Equity	0.14	0.20	0.70	1.35	5.79	0.06
Cash Flow ($/share)	4.50	1.99	7.01	6.27	0.40	6.30
Growth Score	C	-	-	D	A	C
Hist. EPS Growth (3-5 yrs)	16.39%	15.28%	10.92%	5.80%	-42.20%	29.79%
Proj. EPS Growth (F1/F0)	4.59%	12.86%	0.33%	2.73%	119.33%	-7.47%
Curr. Cash Flow Growth	11.18%	19.56%	5.93%	-3.32%	-214.17%	98.75%
Hist. Cash Flow Growth (3-5 yrs)	17.13%	5.21%	8.55%	5.21%	-28.91%	0.39%
Current Ratio	2.84	2.50	1.24	5.37	1.76	1.64
Debt/Capital	12.09%	16.41%	42.36%	57.46%	85.27%	5.93%
Net Margin	52.52%	11.42%	11.64%	11.03%	-4.90%	11.81%
Return on Equity	18.86%	14.23%	16.74%	25.57%	-23.30%	15.30%
Sales/Assets	0.53	0.75	0.54	0.77	0.86	0.63
Proj. Sales Growth (F1/F0)	3.22%	3.22%	1.00%	31.30%	0.82%	-6.56%
Momentum Score	D	-	-	C	D	D
Daily Price Chg	3.58%	0.51%	7.93%	6.36%	6.60%	2.36%
1 Week Price Chg	7.82%	0.00%	-4.40%	1.98%	-11.96%	6.08%
4 Week Price Chg	5.53%	4.01%	-6.89%	7.50%	-19.37%	6.51%
12 Week Price Chg	-3.01%	-5.57%	-24.81%	-32.10%	-42.90%	-5.57%
52 Week Price Chg	8.74%	-17.36%	-17.63%	-17.72%	-39.10%	28.64%
20 Day Average Volume	5,422,375	282,083	4,147,873	2,395,370	6,868,359	2,740,563
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.32%	-0.28%	-4.97%	-0.24%	-9.38%	-0.33%
(F1) EPS Est 12 week change	0.39%	-8.15%	-6.79%	-8.73%	155.24%	-7.57%
(Q1) EPS Est Mthly Chg	20.64%	0.84%	-7.32%	-2.12%	0.00%	-1.40%

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	C
Momentum Score	D
VGM Score	D

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.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock.The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment.This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time.ZIR is not a broker-dealer.ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients.Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.