

Electronic Arts Inc. (EA)

\$115.32 (As of 05/06/20)

Price Target (6-12 Months): **\$133.00**

Long Term: 6-12 Months

Zacks Recommendation:

Outperform

(Since: 04/05/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: C

Summary

EA's fourth-quarter fiscal 2020 results benefited from continued strength in digital revenues and live services. As more and more people stayed at home, EA witnessed the rising usage and engagement levels for many of its games including *Star Wars Jedi: Fallen Order*, *Madden NFL 20*, *Apex Legends* and *FIFA*. Moreover, *FIFA Online* continued to perform strongly, especially in Asia amid the coronavirus lockdown. EA has a strong slate of game releases in fiscal 2021 including the latest installments of *FIFA* and *Madden NFL*, which are expected drive its top line further. Notably, EA's shares have outperformed the industry on a year-to-date basis. However, intense competition from the likes of Activision and Take-Two Interactive is a significant headwind.

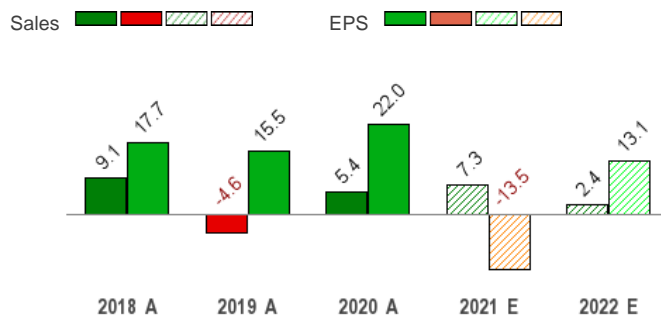
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$120.19 - \$85.69
20 Day Average Volume (sh)	3,243,994
Market Cap	\$33.4 B
YTD Price Change	7.3%
Beta	0.91
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Toys - Games - Hobbies
Zacks Industry Rank	Top 5% (13 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	36.7%
Last Sales Surprise	3.3%
EPS F1 Est- 4 week change	0.1%
Expected Report Date	08/04/2020
Earnings ESP	13.6%
P/E TTM	22.8
P/E F1	23.3
PEG F1	4.0
P/S TTM	6.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	850 E	1,450 E	2,150 E	1,450 E	5,726 E
2021		1,353 E	1,794 E	1,343 E	5,590 E
2020	743 A	1,277 A	1,978 A	1,213 A	5,211 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$0.40 E	\$1.15 E	\$3.00 E	\$1.46 E	\$5.60 E
2021	\$0.35 E	\$1.09 E	\$2.22 E	\$1.22 E	\$4.95 E
2020	-\$0.02 A	\$0.96 A	\$2.79 A	\$1.34 A	\$5.72 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 05/06/2020. The reports text is as of 05/07/2020.

Overview

Headquartered in Redwood City, CA, Electronic Arts 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.

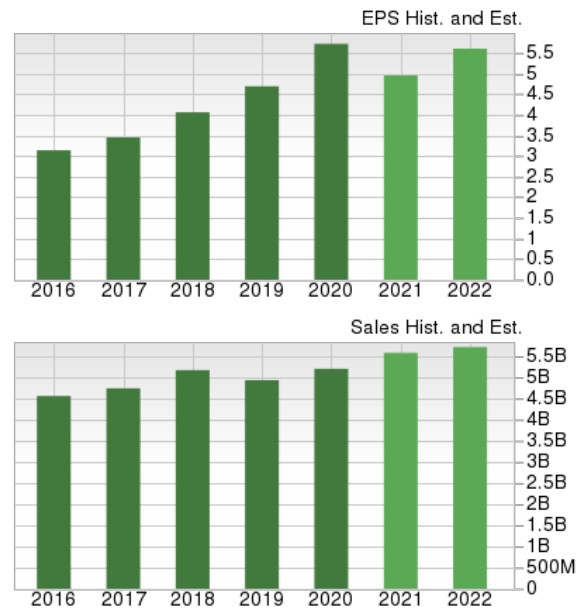
EA games can be played on video consoles, personal computers, mobile devices, tablets and electronic readers. The company generates revenues from the sale of disk-based video game products (known as packaged goods), downloadable contents (DLCs), subscription, micro-transactions and advertising.

EA generated revenues of \$5.54 billion in fiscal 2020, of which digital net revenues contributed 77.9% and the remaining were generated from packaged goods and others.

Moreover, net revenues from live services comprised 50.8% of total net revenues in fiscal 2020.

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.
- ▲ 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. Moreover, coronavirus has been a tailwind for the company. As more and more people were compelled to stay at home due to lockdowns and physical distance measures, EA witnessed rising usage and engagement levels for many of its games including *Star Wars Jedi: Fallen Order*, *Madden NFL 20*, *Apex Legends* and *FIFA* in the fourth quarter.
- ▲ 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.
- ▲ EA's strong liquidity and cash flow-generating ability make the stock attractive to investors. As of Mar 31, 2020, the company had \$5.7 billion in cash and short-term investments compared with \$5.6 billion as of Dec 31, 2019. In comparison, EA has \$1 billion senior notes as of Mar 31, 2020, with \$600 million maturing in March 2021 and \$400 million due in 2026. Moreover, net cash from operating activities in the reported quarter was \$1.79 billion compared with \$1.10 billion, sequentially.

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.

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 now expected to release the next installment of *Battlefield* to fiscal 2022, which is disappointing for players. The company is expected to release 14 games in fiscal 2021, including *FIFA 21* and *Madden NFL 21*. Lack of a new *Battlefield* game is also expected to hurt EA's competitive position against Activision's *Call of Duty* franchise.
 - 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.
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Last Earnings Report

Electronic Arts Q4 Earnings & Revenues Increase Y/Y

Electronic Arts reported fourth-quarter fiscal 2020 earnings of \$1.43 per share, which increased 107.2% year over year.

Revenues rose 12% year over year to \$1.38 billion. Excluding the change in deferred revenues of \$131 million and mobile platform fees of \$43 million, net bookings declined 11.1% year over year to \$1.21 billion.

The Zacks Consensus Estimate for earnings and revenues was pegged at 98 cents per share and \$1.17 billion, respectively.

Quarter Ending **03/2020**

Report Date	May 05, 2020
Sales Surprise	3.28%
EPS Surprise	36.73%
Quarterly EPS	1.34
Annual EPS (TTM)	5.07

Quarter Details

Digital net bookings were \$1.11 billion, increasing 6% year over year and representing 92% of total net bookings.

EA's digital revenues (87.9% of total revenues) grew 14.5% year over year to \$1.21 billion. However, packaged goods and other segment revenues (12.1% of total revenues) were down 2.9% year over year to \$168 million.

Further segregating digital revenues, full game download revenues increased 25% year over year to \$211 million. However, net bookings declined 10.8% year over year to \$190 million.

Live services revenues rose 17% year over year to \$832 million while net bookings declined 6.6% year over year to \$789 million.

Mobile games revenues decreased 3% year over year to \$176 million. Net bookings increased 2.2% year over year to \$138 million.

Based on its platforms, revenues from console increased 12% year over year to \$928 million. Net bookings from console declined 7.9% year over year to \$707 million.

Revenues from PC/browser were up 24% year over year to \$269 million. Net bookings from PC/browser declined 6.2% year over year to \$272 million.

Meanwhile, revenues from mobile platform dropped 3% year over year to \$185 million. Net bookings from mobile improved 2.2% year over year to \$138 million driven by strong popularity of sports titles in Asia.

Other revenues remained flat year over year at \$5 million.

Important Game & Player Metrics

Star Wars: Jedi Fallen Order witnessed strong popularity with more than 10 million unique players joining the game since launch.

Moreover, *Madden NFL 20* is delivering the highest engagement levels in Madden's more than 30-year history.

Further, *FIFA* grew year over year in the fiscal fourth quarter. With approximately 100 million players engaging globally in *FIFA* franchise and more than 25 million unique players joining *FIFA 20* till date, the addition of *VOLTA Football* to *FIFA 20* and the updates to *FIFA Ultimate Team* further boosted player engagement in the reported quarter.

Moreover, *FIFA Online* continued to perform strongly especially in Asia amid coronavirus lockdown.

Notably, *Apex Legends Season 4* had already outperformed in each of the two prior seasons, even before COVID-19 stay-at-home orders were rolled out. Meanwhile, Apex E-sports tournaments generated around two times the average viewing audience compared to other top E-sports leagues.

Further, the company delivered live service content while working from home, including *FIFA Ultimate Team events*, *Madden Ultimate Team* content for the NFL Draft, and new additions to *Star Wars Galaxy of Heroes*.

Operating Details

EA's GAAP gross profit increased 16.2% from the year-ago quarter to \$1.11 billion. Gross margin expanded 290 basis points (bps) on a year-over-year basis to 80.6%.

Operating expenses declined 6.4% from the year-ago quarter to \$771 million. As a percentage of revenues, operating expenses contracted to 51.7% from 61.9% in the year-ago quarter.

As a percentage of revenues, marketing & sales (M&S) and research & development (R&D) expenses shrank 650 bps and 320 bps, respectively. Meanwhile, general & administrative (G&A) expenses expanded 30 bps in the reported quarter.

Operating income on a GAAP basis surged 104.6% year over year to \$401 million. As a percentage of revenues, operating margin expanded to 28.9% from 15.8% in the year-ago quarter.

Balance Sheet and Cash Flow

As of Mar 31, 2020, EA had \$5.7 billion in cash and short-term investments compared with \$5.6 billion as of Dec 31, 2019.

EA has \$1 billion in senior notes as of Mar 31, 2020, with \$600 million maturing in March 2021, and \$400 million due in 2026.

Net cash from operating activities in the reported quarter was \$1.79 billion compared with \$1.10 billion in the previous quarter.

EA repurchased 2.7 million shares for \$291 million in the reported quarter.

Guidance

For the first quarter of fiscal 2021, EA expects GAAP revenues of \$1.22 billion. Net bookings are expected to be \$1 billion.

EA anticipates operating expenses of \$635 million. Earnings are expected to be 93 cents per share.

For fiscal 2021, EA expects GAAP revenues of \$5.525 billion and net bookings of \$5.55 billion.

Moreover, EA anticipates operating expenses of \$2.85 billion for the fiscal.

Additionally, earnings are expected to be \$3.35 per share.

Operating cash flow is estimated to be \$1.575 billion.

Note: The EPS data mentioned in the text of this section differs from the rest of report due to the difference in calculation or consideration of one-time items.

Recent News

On May 6, EA and Maxis announced that The Sims 4 Eco Lifestyle Expansion Pack will be available on PC, Mac, PS4 and Xbox One systems from Jun 5 onward.

On Apr 28, EA and Google announced a partnership to launch five EA games on Stadia, Google's cloud-based gaming platform.

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

Valuation

Electronic Arts shares are up 7.3% in the year-to-date period and 22.9% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 3.9%, while the Zacks Consumer Discretionary sector is down 20.7% in the year-to-date period. Over the past year, the Zacks sub-industry is up 19.6% while the sector is down 15.7%.

The S&P 500 index is down 10.9% in the year-to-date period and 0.5% in the past year.

The stock is currently trading at 23.85X forward 12-month earnings, which compares to 28.78X for the Zacks sub-industry, 24.27X for the Zacks sector and 20.63X 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 \$133 price target reflects 27.43X 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	23.85	28.78	24.27	20.63
	5-Year High	33.49	30.46	24.27	20.63
	5-Year Low	18.01	19.51	16.15	15.19
	5-Year Median	25.21	25.1	19.88	17.44
P/S F12M	Current	6.21	5.28	1.94	3.23
	5-Year High	8.01	5.98	3.19	3.44
	5-Year Low	3.59	3.46	1.67	2.54
	5-Year Median	5.3	4.7	2.52	3.01
EV/Sales TTM	Current	5.39	5.23	2.63	2.84
	5-Year High	8.4	6.72	4.02	3.43
	5-Year Low	3.28	3.32	2.26	2.11
	5-Year Median	4.7	4.58	3.4	2.8

As of 05/06/2020

Industry Analysis Zacks Industry Rank: Top 5% (13 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
JAKKS Pacific Inc (JAKK)	Outperform	1
Nintendo Co (NTDOY)	Outperform	2
Activision Blizzard Inc (ATVI)	Neutral	2
Glu Mobile Inc (GLUU)	Neutral	3
Hasbro Inc (HAS)	Neutral	3
Mattel Inc (MAT)	Neutral	4
TakeTwo Interactive Software Inc (TTWO)	Neutral	3
Zynga Inc (ZNGA)	Neutral	3

Industry Comparison Industry: Toys - Games - Hobbies				Industry Peers		
	EA	X Industry	S&P 500	HAS	MAT	TTWO
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	1	-	-	3	4	3
VGM Score	D	-	-	C	B	D
Market Cap	33.41 B	5.99 B	19.11 B	9.03 B	2.95 B	14.49 B
# of Analysts	13	5	14	7	5	21
Dividend Yield	0.00%	0.00%	2.2%	4.13%	0.00%	0.00%
Value Score	D	-	-	C	B	F
Cash/Price	0.17	0.18	0.06	0.13	0.22	0.18
EV/EBITDA	23.04	23.04	11.69	13.45	17.98	24.47
PEG Ratio	4.04	2.41	2.48	1.40	NA	3.31
Price/Book (P/B)	4.48	4.48	2.58	3.30	18.65	6.03
Price/Cash Flow (P/CF)	21.49	21.39	10.40	10.52	21.30	20.28
P/E (F1)	23.35	26.34	18.81	17.45	NA	29.90
Price/Sales (P/S)	6.03	4.10	1.97	1.77	0.67	5.05
Earnings Yield	4.29%	3.37%	4.99%	5.74%	-1.30%	3.34%
Debt/Equity	0.05	0.19	0.75	1.88	18.04	0.06
Cash Flow (\$/share)	5.37	1.99	7.01	6.27	0.40	6.30
Growth Score	D	-	-	B	B	C
Hist. EPS Growth (3-5 yrs)	16.39%	15.28%	10.87%	4.60%	-42.20%	29.79%
Proj. EPS Growth (F1/F0)	-13.42%	8.79%	-9.86%	-7.46%	63.33%	-8.95%
Curr. Cash Flow Growth	15.43%	19.56%	5.88%	-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	2.45	1.92	1.25	1.92	1.60	1.64
Debt/Capital	5.05%	16.29%	44.23%	65.33%	94.75%	5.93%
Net Margin	54.88%	10.07%	10.87%	8.33%	-5.62%	11.81%
Return on Equity	16.79%	14.94%	16.36%	24.79%	-39.51%	15.30%
Sales/Assets	0.52	0.70	0.55	0.68	0.85	0.63
Proj. Sales Growth (F1/F0)	3.69%	3.69%	-2.18%	21.85%	-2.39%	-6.83%
Momentum Score	C	-	-	F	D	B
Daily Price Chg	-3.59%	0.00%	-1.27%	-1.96%	-1.34%	1.96%
1 Week Price Chg	-2.61%	-2.05%	0.53%	-8.20%	-0.78%	-4.09%
4 Week Price Chg	7.98%	6.23%	0.68%	-11.14%	-0.12%	7.25%
12 Week Price Chg	5.10%	2.55%	-22.30%	-32.90%	-41.49%	12.02%
52 Week Price Chg	22.84%	-6.08%	-11.55%	-34.64%	-26.94%	25.46%
20 Day Average Volume	3,243,994	199,142	2,470,143	1,394,866	4,845,954	1,957,325
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-2.87%	-175.00%	0.00%
(F1) EPS Est 4 week change	0.13%	0.00%	-6.52%	-8.26%	-175.00%	0.00%
(F1) EPS Est 12 week change	-0.53%	-3.53%	-14.84%	-16.36%	-61.77%	-4.16%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	-12.48%	-67.12%	-4.70%	0.00%

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	D
Momentum Score	C
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.

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