

Electronic Arts Inc. (EA)

\$135.70 (As of 08/11/20)

Price Target (6-12 Months): **\$156.00**

Long Term: 6-12 Months

Zacks Recommendation: **Outperform**

(Since: 08/07/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: F

Summary

EA's first-quarter fiscal 2021 results benefited from continued strength in live services and console platform. As more and more people stayed at home, EA witnessed rise in usage and engagement levels for many of its games including *The Sims 4*, *Madden NFL 20*, *Apex Legends* and *FIFA*. Moreover, 30 new game releases on Steam and *Command & Conquer Remastered* drove user engagement. EA has a strong slate of game releases for 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.

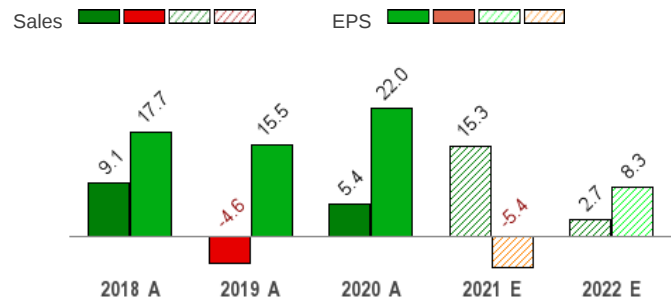
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$147.36 - \$85.69
20 Day Average Volume (sh)	1,955,069
Market Cap	\$39.2 B
YTD Price Change	26.2%
Beta	0.94
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Toys - Games - Hobbies
Zacks Industry Rank	Top 20% (51 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	65.9%
Last Sales Surprise	29.0%
EPS F1 Est- 4 week change	9.3%
Expected Report Date	11/03/2020
Earnings ESP	0.0%
P/E TTM	21.0
P/E F1	25.1
PEG F1	4.3
P/S TTM	6.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	1,036 E	1,410 E	2,300 E	1,412 E	6,174 E
2021	1,390 A	927 E	2,356 E	1,337 E	6,010 E
2020	743 A	1,277 A	1,978 A	1,213 A	5,211 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$0.51 E	\$1.05 E	\$3.11 E	\$1.29 E	\$5.86 E
2021	\$1.36 A	\$0.01 E	\$2.95 E	\$1.12 E	\$5.41 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 08/11/2020. The reports text is as of 08/12/2020.

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.

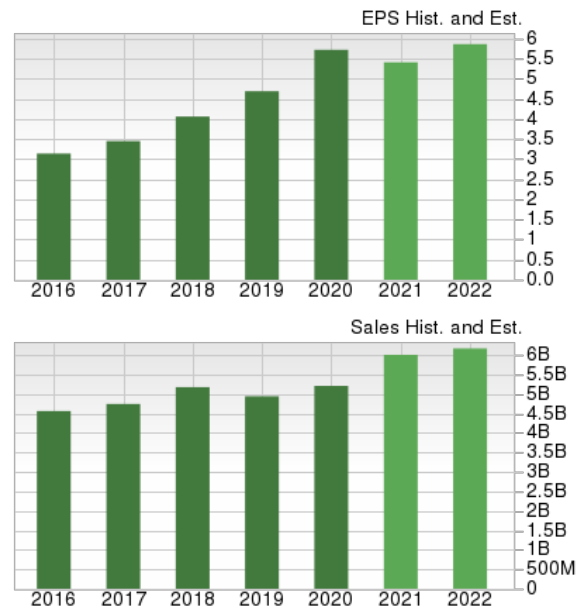
EA games can be played on video consoles, personal computers, mobile devices, tablets and electronic readers. The company generates revenues from the sale of disk-based video game products (known as packaged goods), downloadable contents (DLCs), subscription, micro-transactions and advertising.

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 The Sims 4, Madden NFL 20, Apex Legends and FIFA in the first 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. 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 Jun 30, 2020, the company had \$5.9 billion in cash and short-term investments compared with \$5.7 billion as of Mar 31, 2020. In comparison, EA had \$1 billion senior notes as of Jun 30, 2020, with \$600 million maturing in March 2021 and \$400 million due in 2026.

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 (EA) Q1 Earnings Decline Y/Y, Revenues Rise

Electronic Arts reported first-quarter fiscal 2021 earnings of \$1.25 per share, which declined 73.7% year over year.

Revenues however rose 20.7% year over year to \$1.45 billion. At the beginning of fiscal 2021, EA changed the way in which it reports net bookings. Periods prior to the first quarter of fiscal 2021 have been recast for comparability to align with these changes. Net bookings increased 77.7% year over year to \$1.39 billion.

The Zacks Consensus Estimate for earnings and revenues was pegged at 82 cents per share and \$1.07 billion, respectively.

Quarter Ending 06/2020

Report Date	Jul 30, 2020
Sales Surprise	28.96%
EPS Surprise	65.85%
Quarterly EPS	1.36
Annual EPS (TTM)	6.45

Quarter Details

EA's full game revenues (24.6% of total revenues) grew 37% year over year to \$359 million. Net bookings from full games increased 202% year over year to \$287 million.

Moreover, live services and other revenues (75.4% of total revenues) rose 16.2% year over year to \$1.1 billion. Net bookings from live services increased 61% year over year to \$1.1 billion.

Further segregating full-game revenues, full-game download revenues increased 68% year over year to \$233 million. Revenues from packaged goods increased 5% year over year to \$136 million.

Based on its platforms, revenues from console increased 23% year over year to \$932 million. Net bookings from console increased 98% year over year to \$824 million.

Revenues from PC/browser were up 28% year over year to \$325 million. Net bookings from PC/browser increased 74% year over year to \$340 million.

Revenues from mobile platform increased 3% year over year to \$202 million. Net bookings from mobile increased 32% year over year to \$226 million driven by strong popularity of sports titles in Asia.

Important Game & Player Metrics

The company launched two games during the quarter namely *Command & Conquer Remastered*, which became a top-selling title on Origin and Steam, and *Burnout Paradise Remastered* on Nintendo Switch.

Additionally, EA delivered more than 30 new content updates for console and PC titles, including two major game expansions, as well as more than 50 updates to mobile games.

Moreover, during the quarter, EA launched nearly 30 titles on the Steam platform. Origin business grew 75% year over year by opening up the ability for Steam and Origin players to play together.

Moreover, *Madden NFL 20* is delivering the highest engagement levels with player acquisition growth of nearly 140% year over year.

Further, *FIFA* grew year over year in the fiscal first quarter. Acquisition of new and returning players in *FIFA* grew more than 100% year over year with more than 7 million joining during the quarter.

Moreover, *FIFA Online* continued to perform strongly, engaging nearly 30 million players to date especially in Asia amid coronavirus lockdown.

Notably, fiscal first quarter 2021 saw the most game sessions played and highest revenue total since the launch quarter for *Apex Legends*. Engagement in Season 5 reached the highest levels since its first new season of content. The in-game event, Lost Treasures had more than 96 million hours played in the first two weeks. *Apex Legends* Season 5 outperformed in each of the two prior seasons, even before COVID-19 stay-at-home orders were rolled out.

The Sims 4 now has more than 30 million players life-to-date across all platforms, and daily, weekly and monthly active player totals in the game reached record highs in the first quarter.

Operating Details

EA's GAAP gross profit increased 14.6% from the year-ago quarter to \$1.17 billion. However, gross margin contracted 430 basis points (bps) on a year-over-year basis to 80.3%.

Operating expenses increased 15.3% from the year-ago quarter to \$700 million. As a percentage of revenues, operating expenses contracted 220 bps on a year-over-year basis to 48%.

As a percentage of revenues, marketing & sales (M&S) and research & development (R&D) expenses shrank 80 bps and 1500 bps, respectively. Meanwhile, general & administrative (G&A) expenses expanded 20 bps in the reported quarter.

Operating income on a GAAP basis increased 13.5% year over year to \$471 million. As a percentage of revenues, operating margin contracted 200 bps on a year-over-year basis to 32.3%.

Balance Sheet and Cash Flow

As of Jun 30, 2020, EA had \$5.9 billion in cash and short-term investments compared with \$5.7 billion as of Mar 31, 2020.

Net cash from operating activities in the reported quarter was \$378 million compared with \$1.79 billion in the previous quarter.

EA repurchased 747K shares for \$78 million in the reported quarter completing its \$2.4 billion, two-year repurchase program.

Guidance

For the second quarter of fiscal 2021, EA expects GAAP revenues of \$1.2125 billion. Net bookings are expected to be \$875 million.

EA anticipates earnings to be 21 cents per share.

For fiscal 2021, EA expects GAAP revenues of \$5.625 billion and net bookings of \$5.95 billion.

Additionally, earnings are expected to be \$2.97 per share.

Operating cash flow is estimated to be \$1.85 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 Aug 5, EA's division EA Sports unveiled the Yard, a new backyard football-inspired experience coming to *Madden NFL 21*. It is a small-sided football game with new gameplay mechanics, deep player customization and a new gear.

On Jul 23, Electronic Arts announced new updates to career mode and gameplay realism in *EA SPORTS FIFA 21*, plus new ways for users to team up online with friends.

On Jul 14, Electronic Arts and Final Strike Games announced the release of *Rocket Arena*, an explosive 3v3 shooter where rockets control everything. It is available with cross-play support on PS4, Xbox One and PC via Origin and Steam.

On Jun 24, Electronic Arts and La Liga announced a 10-year partnership under which EA SPORTS will remain the exclusive Official Video Games Partner of La Liga.

On Jun 18, Electronic Arts revealed three new EA Originals games, and confirmed a new partnership with Final Strike Games. Notably, Hazelight Studios' *It Takes Two*, Zoink's *Lost in Random* and Final Strike Games' *Rocket Arena* will be published under the EA Originals Label.

On Jun 12, Electronic Arts and Federation Internationale de Football Association (FIFA) announced a larger, evolved EA SPORTS *FIFA 20* esports ecosystem. This involved adding competitions and resuming football league tournaments as well as online matches in place of the EA SPORTS *FIFA 20* Global Series including the *FIFA eWorld Cup*.

On Jun 5, EA announced the launch of *The Sims 4 Eco Lifestyle*, the ninth expansion pack available for PC, Mac, PlayStation 4 and Xbox One.

The company also announced the availability of *Command & Conquer* Remastered Collection on PC via Origin and Steam.

On Jun 11, EA announced that more than 25 games will be available on Steam this month including the *Battlefield* franchise.

Valuation

Electronic Arts shares are up 26.2% in the year-to-date period and 46.9% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 21.9%, while the same in the Zacks Consumer Discretionary sector is down 4.8% in the year-to-date period. Over the past year, the Zacks sub-industry and sector is up 36.4% and 4.3%, respectively.

The S&P 500 index is up 4.2% in the year-to-date period and 14.9% in the past year.

The stock is currently trading at 25.34X forward 12-month earnings, which compares to 29.12X for the Zacks sub-industry, 33.38X for the Zacks sector and 22.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 35.45X and as low as 18.01X, with a 5-year median of 25.22X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$156 price target reflects 27.99X 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	24.34	29.12	33.38	22.8
	5-Year High	35.45	32.14	33.66	22.8
	5-Year Low	18.01	19.51	16.13	15.25
	5-Year Median	25.22	25.49	19.86	17.58
P/S F12M	Current	6.5	5.78	2.38	3.67
	5-Year High	8.01	6.16	2.95	3.67
	5-Year Low	3.59	3.5	1.68	2.53
	5-Year Median	5.46	4.81	2.5	3.05
EV/Sales TTM	Current	5.74	6.08	3.13	3.23
	5-Year High	8.4	6.82	3.86	3.46
	5-Year Low	3.28	3.43	2.29	2.14
	5-Year Median	4.77	4.74	3.39	2.86

As of 08/11/2020

Industry Analysis Zacks Industry Rank: Top 20% (51 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Activision Blizzard, Inc. (ATVI)	Neutral	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	4
TakeTwo Interactive Software, Inc. (TTWO)	Neutral	2
Zynga Inc. (ZNGA)	Underperform	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)	2	-	-	3	2	2
VGM Score	C	-	-	D	F	D
Market Cap	39.19 B	7.38 B	23.61 B	10.79 B	3.98 B	19.11 B
# of Analysts	14	6.5	14	7	4	21
Dividend Yield	0.00%	0.00%	1.69%	3.46%	0.00%	0.00%
Value Score	F	-	-	B	D	F
Cash/Price	0.14	0.14	0.07	0.10	0.12	0.14
EV/EBITDA	20.28	21.23	13.32	15.12	22.18	23.75
PEG Ratio	4.34	2.72	2.95	1.72	NA	5.04
Price/Book (P/B)	5.03	4.40	3.22	4.08	46.23	7.21
Price/Cash Flow (P/CF)	25.28	25.28	12.79	12.56	28.80	29.00
P/E (F1)	25.08	24.37	22.02	23.64	NA	44.00
Price/Sales (P/S)	6.77	3.61	2.57	2.17	0.93	5.65
Earnings Yield	3.99%	3.98%	4.29%	4.23%	-1.31%	2.27%
Debt/Equity	0.05	0.08	0.77	1.82	33.09	0.06
Cash Flow (\$/share)	5.37	2.34	6.94	6.27	0.40	5.76
Growth Score	A	-	-	F	D	A
Hist. EPS Growth (3-5 yrs)	14.93%	14.93%	10.41%	2.05%	NA	34.56%
Proj. EPS Growth (F1/F0)	-5.44%	24.13%	-6.51%	-18.38%	51.67%	-31.33%
Curr. Cash Flow Growth	15.43%	-3.32%	5.22%	-3.32%	-214.17%	-8.18%
Hist. Cash Flow Growth (3-5 yrs)	7.26%	6.23%	8.55%	5.21%	-28.91%	12.57%
Current Ratio	2.61	2.09	1.34	1.61	1.47	1.72
Debt/Capital	4.85%	12.77%	44.59%	64.62%	97.07%	5.47%
Net Margin	34.27%	10.40%	10.13%	7.58%	-5.82%	13.22%
Return on Equity	21.32%	18.19%	14.59%	18.71%	-51.02%	28.26%
Sales/Assets	0.52	0.73	0.51	0.57	0.83	0.68
Proj. Sales Growth (F1/F0)	14.02%	1.36%	-1.45%	15.13%	-5.07%	-6.07%
Momentum Score	F	-	-	F	B	F
Daily Price Chg	-3.55%	-0.78%	-0.17%	-0.32%	-1.54%	-4.36%
1 Week Price Chg	1.67%	2.25%	2.30%	5.48%	2.25%	6.67%
4 Week Price Chg	-2.04%	0.00%	6.41%	5.49%	9.75%	10.63%
12 Week Price Chg	14.48%	17.49%	15.42%	15.82%	43.14%	17.49%
52 Week Price Chg	46.96%	27.09%	2.88%	-32.28%	-0.26%	31.04%
20 Day Average Volume	1,955,069	512,846	2,007,486	1,126,759	3,578,669	1,432,775
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	9.28%	7.34%	1.84%	-5.44%	53.60%	-1.17%
(F1) EPS Est 12 week change	10.40%	5.20%	2.40%	-6.98%	51.67%	-22.76%
(Q1) EPS Est Mthly Chg	-140.52%	-5.17%	0.72%	-2.76%	2.75%	-7.57%

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.

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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	F
Growth Score	A
Momentum Score	F
VGM Score	C

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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