

Zynga Inc. (ZNGA)

\$9.05 (As of 06/04/20)

Price Target (6-12 Months): **\$9.50**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/09/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: A

Summary

Zynga is benefiting from strength in live services, product introductions and growth in international markets. Robust performance of five popular franchises — CSR Racing, Words With Friends, Zynga Poker, Empires & Puzzles and Merge Dragons! — is driving the company's top line. The company's strengthening portfolio with Words With Friends and Empires & Puzzles witnessing record revenues and bookings, and recent releases including Merge Magic! and Farmville 3 are key catalysts for the long haul. However, intensifying competition from the likes of EA and Activision is compelling the company to spend more on software development and marketing. This is keeping margins under pressure. The company's shares have underperformed the industry on a year-to-date basis.

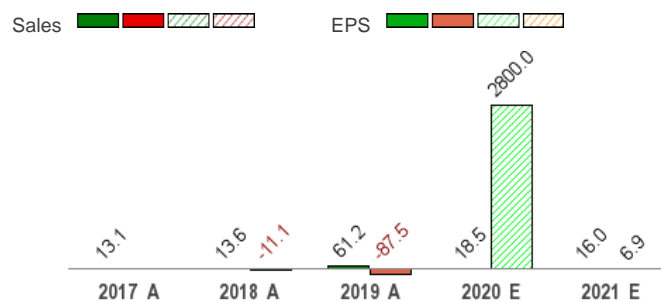
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$9.92 - \$5.51
20 Day Average Volume (sh)	23,451,876
Market Cap	\$8.7 B
YTD Price Change	47.9%
Beta	0.35
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Gaming
Zacks Industry Rank	Top 34% (86 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-80.0%
Last Sales Surprise	4.8%
EPS F1 Est- 4 week change	70.1%
Expected Report Date	07/29/2020
Earnings ESP	0.0%
P/E TTM	905.0
P/E F1	31.2
PEG F1	2.2
P/S TTM	5.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	539 E	580 E	551 E	592 E	2,150 E
2020	425 A	493 E	444 E	483 E	1,854 E
2019	359 A	376 A	395 A	433 A	1,564 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.08 E	\$0.10 E	\$0.08 E	\$0.08 E	\$0.31 E
2020	\$0.01 A	\$0.07 E	\$0.04 E	\$0.05 E	\$0.29 E
2019	-\$0.12 A	-\$0.04 A	\$0.00 A	\$0.04 A	\$0.01 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 06/04/2020. The reports text is as of 06/05/2020.

Overview

Based in San Francisco, CA, Zynga Inc. is a leading developer, marketer, and publisher of social game services.

Zynga's gaming portfolio includes *CSR Racing 2*, *Empires & Puzzles*, *FarmVille*, *Merge Dragons!*, *Words With Friends*, *Mafia Wars*, *Zynga Poker* and *Treasure Isle*.

Zynga operates social games as live services, which means that it continues to support and update games after launch and gather daily, metrics-based player feedback that enables it to continually enhance games by adding new content and features.

The company publishes games on a number of global platforms including Facebook, MySpace, Yahoo, iPad, iPhone and Android devices.

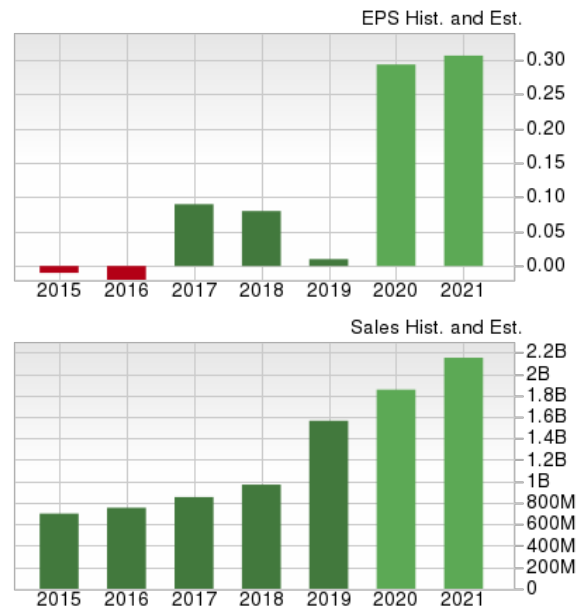
Zynga earns revenues from the sale of advertisement-free versions of mobile games, virtual currency that players use to buy in-game virtual items, licensing and advertising services.

The company reported revenues of \$1.32 billion for 2019. International revenues accounted for approximately 37% of revenues.

In the mobile and social gaming market, Zynga competes with the likes of Glu Mobile, NetEase Games, SciGames Interactive and EA Mobile.

The company also faces substantial competition from console and personal computer game publishers and diversified media companies including Sony, Microsoft, Nintendo, Activision Blizzard, Take-Two Interactive, THQ Ubisoft Time Warner and Viacom.

Zynga acquired 80% of Small Giant Games for \$560 million in a deal that closed at the beginning of 2019, thus adding Empires & Puzzles as a new forever franchise to its live services portfolio.



Reasons To Buy:

- ▲ Zynga's growth is primarily driven by strength in its diversified portfolio of live services. Also known as forever five franchises — *CSR Racing*, *Words With Friends*, *Zynga Poker*, *Empires & Puzzles* and *Merge Dragons!* — are the key growth drivers for the company.
- ▲ Zynga's expanding mobile gaming portfolio is expected to drive growth. Tremendous initial response from soft launches of games such as *Farmville 3* and *Merger Magic!* from Gram Games and *Puzzle Combat* from Small Giant Games are positives. Mobile sales accounted for 95.8% of total revenues for Zynga in first-quarter fiscal 2020.
- ▲ Zynga has been benefiting from acquisitions and partnerships. The company's stellar sales growth in 2019 can be attributed to two acquisitions. Zynga acquired Gram Games for \$250 million in May 2018 and 80% of Small Giant Games for \$560 million in a deal that closed at the beginning of 2019. The latter purchase alone added \$130 million of revenues to Zynga's top line, boosting its year-over-year growth. Moreover, Zynga introduced *Fast & Furious: Hobbs & Shaw* in partnership with Universal Games and Digital Platforms. Such key partnerships and continued featuring of exclusive content from automotive brands made *CSR2* a popular and engaging racing game.
- ▲ China, South Korea, and Japan are among the biggest markets in the world for mobile gaming. The company recently entered the Asian markets launching *Empires & Puzzles* with self-publishing model in South Korea and Japan. International expansion thus creates huge growth opportunities for Zynga in the near term.
- ▲ Zynga had cash and cash equivalents & short-term investments of approximately \$1.26 billion as of Mar 31, 2020 compared with \$1.36 billion as of Dec 31, 2019. However, the company's net cash of \$542 million on Mar 31, 2019 and total debt-to-capital of 28% which is lower than the industry's 71.6% gives an indication that its debt level is manageable. Zynga continues to invest in developing its platform and products.

Zynga benefits from the popularity of *CSR Racing*, *Words With Friends* and *Merge Dragons!* franchises, expanding mobile gaming portfolio and global footprint.

Reasons To Sell:

- ▼ Active user addition is key to healthy growth of any gaming company. Zynga's top line is driven by increase in user spending rather than a growing player base, which is a concern. The company's average mobile daily active users in first-quarter 2020 were about 21 million, down 7% year over year. Average mobile monthly active users declined 5% in a year's time to 68 million.
- ▼ The video game industry is inherently hit driven and highly competitive. Though Zynga 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. This keeps the margins under pressure
- ▼ Zynga is losing opportunities in the rapidly growing e-sports market to the likes of Take Two Interactive and Activision Blizzard. With continued increase in viewership, corporate sponsorships and growing media coverage, e-sports is here to stay. Per the latest report from Newzoo, e-sports industry will reach \$1.8 billion by 2022.

The video game industry is inherently hit driven and highly competitive. Zynga faces significant competition from the likes of Take Two Interactive and Activision Blizzard.

Last Earnings Report

Zynga's Q1 Loss Narrows Year Over Year, Revenues Rise

Zynga reported first-quarter 2020 loss of 11 cents per share. The figure was narrower than a loss of 14 cents reported in the year-ago period.

Revenues jumped 52.1% year over year to \$403.8 million driven by strength in live services, and robust growth in international markets.

In particular, *Merge Dragons!*, *Empires & Puzzles*, and contributions from *Merge Magic!* and *Game of Thrones Slots Casino* drove top-line growth in the reported quarter.

The Zacks Consensus Estimate for earnings and revenues was pegged at 5 cents per share and \$406 million, respectively.

Total bookings came in at \$425 million, up 18.1% year over year driven by strong mobile bookings. The consensus mark for bookings was pegged at \$406 million.

Quarter Details

Zynga's online game revenues (85.3% of total revenues) increased 72% year over year to \$344.4 million on the back of its five popular franchises — *CSR Racing*, *Words With Friends*, *Zynga Poker*, *Empires & Puzzles* and *Merge Dragons!* and strong player engagements across titles as a result of coronavirus induced self-quarantine by users globally.

Notably, *Empires & Puzzles* and Social Slots portfolio witnessed record revenues and bookings in the reported quarter.

Advertising revenues (14.7% of total revenue) and advertisement bookings (13.9% of total bookings) decreased 8.9% and 8.7%, respectively year over year to \$59.4 million and \$59.2 million attributed to lower advertising demand as a result of coronavirus lockdown.

Mobile revenues (95.8% of total revenue) and mobile bookings increased 57.3% and 19.7%, respectively year over year to \$387 million and \$405.5 million. The increase was driven by robust live services performance.

CSR2 was a solid contributor in the first quarter with the successful launch of Elite Customs — a new feature allowing players to customize and upgrade their car collections using new liveries, interiors, wheel upgrades and more — and a second Legends pack.

On a geographic basis, revenues from the United States (60.1% of total revenues) increased 41.3% year over year to \$243 million.

Moreover, International revenues (39.9% of total revenues) increased 73.1% to \$161 million. The company benefited from self-publishing of *Empires & Puzzles* in South Korea, Japan and Taiwan in the first quarter.

User-Base Details

In the first quarter, user pay revenues were \$344 million, up 72% year over year, and user pay bookings were \$366 million, up 24% year over year.

However, Zynga's average mobile daily active users (DAUs) decreased 7% year over year to 21 million. The addition of *Empires & Puzzles* and *Merge Magic!* was more than offset by decreases in older mobile titles such as *Zynga Poker* and chat games.

Moreover, average mobile monthly active users (MAUs) decreased 5% year over year to 68 million in the reported quarter, primarily due to declines in *Zynga Poker*, chat games and older mobile titles, partially offset by the additions of *Empires & Puzzles*, *Merge Magic!* and *Merge Dragons!*.

On a sequential basis, both mobile DAUs and mobile MAUs increased modestly, led by growth in the company's *Casual Cards* portfolio and *Words With Friends*.

Average mobile daily bookings per average mobile DAU (ABPU) grew 27% year over year to \$0.216 in the reported quarter.

Operating Details

GAAP gross margin as a percentage of revenues expanded to 64% from 54% in the year-ago quarter due to a lower net increase in deferred revenues.

Non-GAAP operating expenses (51.6% of total revenue) increased 13.6% year over year to \$208.4 million in the reported quarter primarily due to increase in sales and market investments.

Non-GAAP research & development (R&D), general & administrative (G&A) and sales & marketing (S&M) expenses increased 3.8%, 8.6% and 21% year over year, to \$67.1 million, \$21.2 million and \$120.1 million, respectively.

Adjusted EBITDA was \$68.5 million against a negative \$18.1 million in the year-ago quarter.

Balance Sheet

As of Mar 31, 2020, Zynga had cash and cash equivalents & short-term investments of approximately \$1.26 billion compared with \$1.36 billion as of Dec 31, 2019.

Quarter Ending 03/2020

Report Date	May 06, 2020
Sales Surprise	4.78%
EPS Surprise	-80.00%
Quarterly EPS	0.01
Annual EPS (TTM)	0.01

Cash flow used in operating activities in first-quarter 2020 was \$35.1 million compared with \$94 million cash flow provided from operating activities in fourth-quarter 2019. Free cash flow was negative \$43.7 million in the first quarter compared with \$89.2 million in the previous quarter.

Guidance

For second-quarter 2020, Zynga expects revenues of \$400 million and bookings of \$460 million.

Management expects the top line to benefit from mobile live services with expected sequential growth across its five forever franchises as well as the year-over-year additions of *Merge Magic!* and *Game of Thrones Slots Casino*.

Operating expense is expected to increase sequentially. Adjusted EBITDA is expected to be \$32 million. Net loss is expected to be \$60 million.

For 2020, management expects revenues of \$1.65 billion and bookings of \$1.8 billion.

Recent News

On Jun 1, Zynga announced that it has entered into a definitive agreement to acquire Peak, one of the most globally successful mobile gaming companies, for \$1.8 billion.

On May 15, Zynga announced the release of the first official trailer of Harry Potter: Puzzles & Spells, soft launched in select markets on Mar 5. The magical match-3 mobile game is officially licensed from Warner Bros. Interactive Entertainment.

On May 6, Zynga announced that Garth Brooks, the best-selling solo artist in U.S. history, has collaborated with Amazon to bring free content to Amazon Prime members in *Words With Friends*.

On Mar 28, Zynga announced collaboration with 17 global games industry leaders to launch a program, encouraging players to follow health and safety guidelines against coronavirus.

On Mar 5, Zynga announced the soft launch of Harry Potter: Puzzles & Spells in select markets. The magical match-3 mobile game is officially licensed from Warner Bros. Interactive Entertainment.

On Feb 26, Zynga released Elite Customs feature in its mobile drag racing game, CSR2. Elite Customs gives players access to exclusive custom paints, liveries and interior options, license plate mods and wheel upgrades.

Valuation

Zynga's shares are up 4.2% in the year-to-date period and 15.3% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 6.1% while the same in the Zacks Consumer Discretionary sector are down 9.9% in the year-to-date period. Over the past year, the Zacks sub-industry is up 22.9% while the sector is down 1.4%.

The S&P 500 index is down 3.6% in the year-to-date period while up 9.4% in the past year.

The stock is currently trading at 4.56X forward 12-month sales, which compares to 2.75X for the Zacks sub-industry, 2.24X for the Zacks sector and 3.3X for the S&P 500 index.

Over the past five years, the stock has traded as high as 4.87X and as low as 2X, with a 5-year median of 3.32X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$9.5 price target reflects 4.79X forward 12-month sales.

The table below shows summary valuation data for ZNGA

Valuation Multiples - ZNGA					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	4.56	2.75	2.24	3.3
	5-Year High	4.87	2.89	3.19	3.3
	5-Year Low	2	1.4	1.67	2.37
	5-Year Median	3.32	2.29	2.52	2.86
P/B TTM	Current	4.66	3.66	2.97	5.08
	5-Year High	4.98	5.09	5.05	5.35
	5-Year Low	0.92	1.87	2.20	3.43
	5-Year Median	1.99	3.75	4.22	4.5
EV/Sales TTM	Current	5.13	3.23	2.93	3.04
	5-Year High	6	4.39	4.05	3.46
	5-Year Low	0.85	1.98	2.26	2.13
	5-Year Median	3.07	3.36	3.38	2.83

As of 06/04/2020

Industry Analysis Zacks Industry Rank: Top 34% (86 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Activision Blizzard, Inc. (ATVI)	Outperform	1
Nintendo Co. (NTDOY)	Outperform	2
Tencent Holding Ltd. (TCEHY)	Outperform	1
TakeTwo Interactive Software, Inc. (TTWO)	Outperform	3
Electronic Arts Inc. (EA)	Neutral	2
Facebook, Inc. (FB)	Neutral	3
Glu Mobile Inc. (GLUU)	Neutral	2
Microsoft Corporation (MSFT)	Neutral	3

Industry Comparison Industry: Gaming				Industry Peers		
	ZNGA	X Industry	S&P 500	ATVI	EA	TTWO
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Neutral	Outperform
Zacks Rank (Short Term)	3	-	-	1	2	3
VGM Score	D	-	-	F	D	B
Market Cap	8.66 B	1.76 B	22.58 B	53.79 B	33.94 B	14.47 B
# of Analysts	6	4	14	14	13	23
Dividend Yield	0.00%	0.00%	1.87%	0.59%	0.00%	0.00%
Value Score	D	-	-	D	D	D
Cash/Price	0.15	0.23	0.06	0.11	0.16	0.16
EV/EBITDA	56.12	10.35	12.93	23.41	17.25	17.38
PEG Ratio	2.12	1.78	3.06	1.35	3.23	5.89
Price/Book (P/B)	4.66	3.27	3.09	4.13	4.55	5.70
Price/Cash Flow (P/CF)	352.37	10.83	12.17	24.87	21.83	22.14
P/E (F1)	30.55	21.32	22.17	25.47	23.52	33.28
Price/Sales (P/S)	5.93	1.23	2.41	8.34	6.13	4.68
Earnings Yield	3.20%	-5.57%	4.27%	3.92%	4.25%	3.00%
Debt/Equity	0.38	2.09	0.76	0.21	0.05	0.06
Cash Flow (\$/share)	0.03	1.12	7.01	2.81	5.37	5.76
Growth Score	D	-	-	F	D	A
Hist. EPS Growth (3-5 yrs)	NA%	4.94%	10.87%	13.15%	15.11%	29.50%
Proj. EPS Growth (F1/F0)	2,833.30%	-120.83%	-10.79%	21.84%	-12.91%	-30.66%
Curr. Cash Flow Growth	-57.58%	0.37%	5.48%	-23.97%	15.43%	-8.18%
Hist. Cash Flow Growth (3-5 yrs)	19.28%	9.36%	8.55%	9.90%	7.26%	12.57%
Current Ratio	1.89	1.76	1.29	2.78	2.45	1.71
Debt/Capital	27.47%	69.19%	44.75%	17.04%	5.05%	5.65%
Net Margin	4.58%	-5.62%	10.59%	24.21%	54.88%	13.09%
Return on Equity	-3.55%	-2.30%	16.26%	14.57%	16.79%	18.22%
Sales/Assets	0.42	0.43	0.55	0.35	0.52	0.65
Proj. Sales Growth (F1/F0)	18.20%	-24.75%	-2.61%	10.60%	6.36%	-10.73%
Momentum Score	A	-	-	B	B	A
Daily Price Chg	-2.58%	0.00%	-0.08%	-0.16%	-0.64%	-1.32%
1 Week Price Chg	9.19%	5.55%	4.60%	-1.51%	2.55%	-3.09%
4 Week Price Chg	18.46%	18.03%	12.07%	-4.50%	0.33%	-0.92%
12 Week Price Chg	49.83%	41.28%	25.17%	27.95%	25.53%	17.75%
52 Week Price Chg	39.44%	-8.71%	0.34%	58.37%	21.57%	15.29%
20 Day Average Volume	23,451,876	151,674	2,537,324	7,720,555	3,106,567	2,974,303
(F1) EPS Est 1 week change	18.76%	0.00%	0.00%	0.00%	0.35%	0.00%
(F1) EPS Est 4 week change	70.13%	-108.64%	-0.08%	6.53%	3.51%	-25.83%
(F1) EPS Est 12 week change	26.59%	-135.71%	-16.19%	10.18%	-1.52%	-26.08%
(Q1) EPS Est Mthly Chg	165.71%	-171.93%	0.00%	4.07%	302.08%	475.86%

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	A
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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