

## Zynga Inc. (ZNGA)

**\$6.70** (As of 01/09/20)

Price Target (6-12 Months): **\$7.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 07/30/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:C

Value: F

Growth: B

Momentum: A

## Summary

Zynga is benefitting from strength in live services, product introductions and growth in international markets. Robust performance of popular five franchises — *CSR Racing*, *Words With Friends*, *Zynga Poker*, *Empires & Puzzles* and *Merge Dragons!* — is driving the company's top line. In addition, *Game of Thrones Slots Casino* became the fastest growing slots title in its first full quarter after launch. The company's portfolio strength is a key catalyst for the long haul. Shares have outperformed the industry in a year's time. 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.

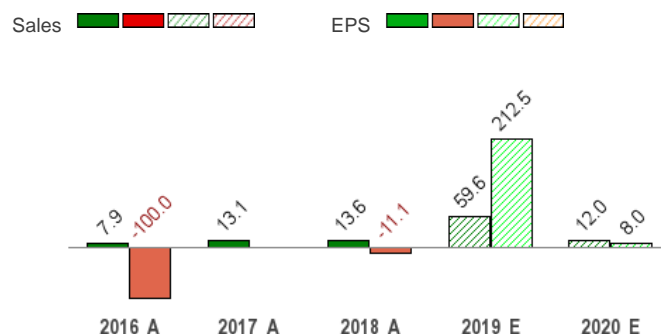
## Price, Consensus & Surprise



## Data Overview

52 Week High-Low	<b>\$6.78 - \$4.21</b>
20 Day Average Volume (sh)	<b>11,698,998</b>
Market Cap	<b>\$6.3 B</b>
YTD Price Change	<b>9.5%</b>
Beta	<b>0.29</b>
Dividend / Div Yld	<b>\$0.00 / 0.0%</b>
Industry	<b>Gaming</b>
Zacks Industry Rank	<b>Bottom 28% (182 out of 254)</b>

## Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	<b>-100.0%</b>
Last Sales Surprise	<b>2.0%</b>
EPS F1 Est- 4 week change	<b>5.9%</b>
Expected Report Date	<b>02/05/2020</b>
Earnings ESP	<b>27.3%</b>

P/E TTM	<b>NA</b>
P/E F1	<b>24.8</b>
PEG F1	<b>1.7</b>
P/S TTM	<b>5.4</b>

## Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	412 E	422 E	441 E	458 E	1,734 E
2019	359 A	376 A	395 A	417 E	1,548 E
2018	219 A	234 A	249 A	267 A	970 A

## EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.06 E	\$0.06 E	\$0.07 E	\$0.07 E	\$0.27 E
2019	-\$0.12 A	-\$0.04 A	\$0.00 A	\$0.06 E	\$0.25 E
2018	\$0.02 A	\$0.02 A	\$0.03 A	\$0.02 A	\$0.08 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 01/09/2020. The reports text is as of 01/10/2020.

## 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.

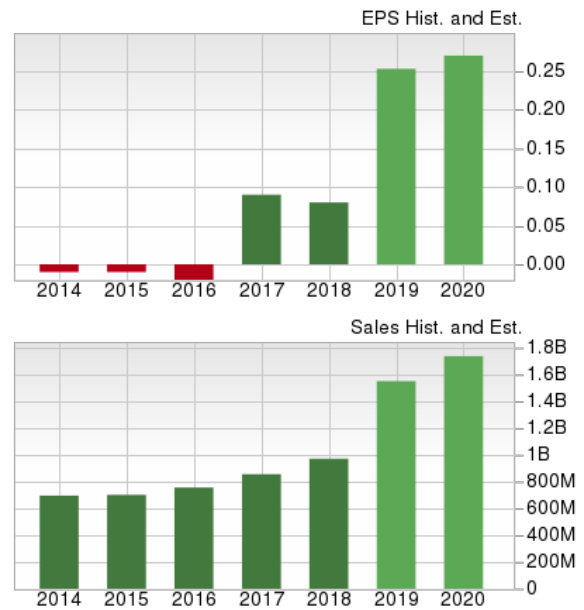
Zynga earns revenues from the sale of advertisement-free versions of mobile games, virtual currency that players use to buy in-game virtual items, licensing and advertising services.

The company reported revenues of \$907.2 million in 2018. International revenues accounted for approximately 35% of revenues.

Zynga's top three online revenue-generating games were *Zynga Poker*, *CSR Racing 2* and *Hit It Rich! Slots*, which accounted for 45% of online game revenues in 2018.

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 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.



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## 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% of total revenues for Zynga in third-quarter fiscal 2019.
- ▲ 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 has a strong balance sheet and generates significant cash flow, which makes it an attractive stock for investors. The company had cash and cash equivalents of \$1.45 billion at the end of third-quarter 2019. Free cash flow amounted to \$59.8 million. We believe that its ability to generate strong cash flows will help it to make further investments in product development and acquisitions in the long haul.

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

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### 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 daily active users in third-quarter 2019 were about 20 million, down 1% year over year. Monthly active users declined 13% to 67 million in a year's time.
- ▼ 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 \$1.4 billion by 2020.

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 Q3 Earnings Beat Estimates, Revenues Up Y/Y

Zynga reported GAAP earnings of 24 cents per share for third-quarter 2019 compared with earnings of a penny in the year-ago quarter.

Revenues increased 48% year over year to \$345 million driven by strength in live services, product introductions and growth in international markets.

Total bookings came in at \$395 million, up 59% year over year. Bookings beat the Zacks Consensus Estimate by 3.1% driven by strong mobile bookings.

The Zacks Consensus Estimate for earnings and revenues was pegged at 5 cents and \$387 million, respectively.

#### Quarter Details

Zynga's online game revenues (81.6% of total revenues) increased 67.9% year over year to \$281.7 million on the back of its popular five franchises — *CSR Racing*, *Words With Friends*, *Zynga Poker*, *Empires & Puzzles* and *Merge Dragons!*.

Mobile revenues (94.9% of total revenue) and mobile bookings increased 54.2% and 64.2%, respectively year over year to \$327 million and \$377.6 million. The increase was driven by robust live services performance.

In addition, *Game of Thrones Slots Casino* became the fastest growing slots title in its first full quarter post-launch.

Notably, the company published *Empires & Puzzles* in South Korea and Japan in the reported quarter.

Advertising revenues (18.4% of total revenue) and advertisement bookings decreased 2.9% and 2.6%, respectively year over year to \$63.6 million and \$63.8 million.

Zynga's average mobile daily active users (DAUs) decreased 1% year over year to 20 million. Average mobile monthly active users (MAUs) decreased 13% year over year to 67 million in the reported quarter.

#### Operating Details

Non-GAAP operating expenses (58.9% of total revenue) increased 57.8% year over year to \$203.4 million primarily due to the increase in market investments.

GAAP research & development (R&D), sales & marketing (S&M) and general & administrative (G&A) expenses on a reported basis increased 93.3%, 117.3% and 15.8% year over year, respectively.

Adjusted EBITDA declined 28.2% year over year to \$28 million. Adjusted EBITDA margin contracted 860 basis points on a year-over-year basis.

#### Balance Sheet

Cash and investments were approximately \$1.45 billion

As of Sep 30, 2019, Zynga had cash and cash equivalents & short-term investments of approximately \$1.45 billion compared with \$831 million as of Jun 30, 2019.

Operating cash flow in the quarter was \$69 million while free cash flow was \$59.8 million.

#### Guidance

For fourth-quarter 2019, Zynga expects revenues to be \$365 million and bookings to be \$415 million.

Management expects the top line to benefit from mobile live services with an expected sequential growth across its five forever franchises, as well as initial contributions from Merge Magic!

Operating expense is expected to increase sequentially. Adjusted EBITDA is expected to be \$16 million. Net loss is expected at \$21 million.

For 2019, management has raised its prior revenue guidance by \$42 million to \$1.28 billion, indicating 41% year-over-year increase.

Moreover, the company raised its bookings guidance by \$46 million to \$1.55 billion for 2019.

Quarter Ending **09/2019**

Report Date	<b>Oct 30, 2019</b>
Sales Surprise	<b>2.03%</b>
EPS Surprise	<b>-100.00%</b>
Quarterly EPS	<b>0.00</b>
Annual EPS (TTM)	<b>-0.14</b>

## Recent News

On Dec 4, Zynga launched an event series in partnership with the hyper sports car manufacturer Bugatti in its mobile drag racing game, *CSR2*. The event series, which celebrates Bugatti's 110th anniversary, will give players the opportunity to collect and compete with the world's most powerful and exclusive hyper sports cars in *CSR2*.

On Nov 22, Zynga announced an in-game license deal with Adult Swim to bring characters from the Emmy Award-winning TV series, *Rick and Morty* to Gram Games' *Merge Dragons!*.

On Nov 18, Zynga's subsidiary Small Giant Games launched Hero Costumes, a new feature for its popular franchise *Empires & Puzzles*. The feature provides the heroes in the game with new costumes that grant exclusive skills and increased power.

On Nov 6, Zynga launched a 'Best of British' event series in *CSR2* featuring British hypercars such as the McLaren Senna, Noble M600 Carbon Sport, Ginetta Akula, Ultima RS and TVR Sagaris among others. The event comprises a 50-race ladder on a brand new track, ending with a finale that unlocks the McLaren Speedtail exclusively in *CSR2*.

## Valuation

Zynga's shares are up 7% in the six-months period and 55.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are up 8.3% and 4.5%, respectively, in the six-months period. Over the past year, the Zacks sub-industry and the sector are up 14.3% and 21.1%, respectively.

The S&P 500 index is up 9.8% in the six-months period and 25.3% in the past year.

The stock is currently trading at 3.64X forward 12-month sales, which compares to 2.45X for the Zacks sub-industry, 2.37X for the Zacks sector and 3.51X for the S&P 500 index.

Over the past five years, the stock has traded as high as 4.14X and as low as 2X, with a 5-year median of 3.26X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$7 price target reflects 3.8X 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	3.64	2.45	2.37	3.51
	5-Year High	4.14	3.28	3.19	3.51
	5-Year Low	2	1.77	1.81	2.54
	5-Year Median	3.26	2.3	2.54	3
P/B TTM	Current	3.27	4.35	3.57	4.47
	5-Year High	3.53	5	5.04	4.47
	5-Year Low	0.92	2.22	3.13	2.85
	5-Year Median	1.89	3.61	4.29	3.61
EV/Sales TTM	Current	4.32	3.39	3.32	3.28
	5-Year High	6	4.39	4.02	3.3
	5-Year Low	0.85	2.51	2.7	2.16
	5-Year Median	2.85	3.32	3.44	2.8

As of 01/09/2020

## Industry Analysis Zacks Industry Rank: Bottom 28% (182 out of 254)



## Top Peers

Activision Blizzard, Inc. (ATVI)	Outperform
Electronic Arts Inc. (EA)	Neutral
Facebook, Inc. (FB)	Neutral
Microsoft Corporation (MSFT)	Neutral
Nintendo Co. (NTDOY)	Neutral
Take-Two Interactive Software, Inc. (TTWO)	Neutral
Glu Mobile Inc. (GLUU)	Underperform
Tencent Holding Ltd. (TCEHY)	Underperform

Industry Comparison Industry: Gaming				Industry Peers		
	ZNGA Neutral	X Industry	S&P 500	ATVI Outperform	EA Neutral	TTWO Neutral
<b>VGM Score</b>	<b>C</b>	-	-	<b>F</b>	<b>F</b>	<b>D</b>
Market Cap	6.34 B	2.75 B	23.94 B	45.59 B	31.93 B	14.51 B
# of Analysts	7	4	13	14	14	21
Dividend Yield	0.00%	0.00%	1.78%	0.62%	0.00%	0.00%
<b>Value Score</b>	<b>F</b>	-	-	<b>F</b>	<b>D</b>	<b>F</b>
Cash/Price	0.24	0.11	0.04	0.11	0.16	0.16
EV/EBITDA	81.71	12.07	13.97	14.68	22.91	24.99
PEG Ratio	1.72	1.72	2.03	1.79	1.72	2.10
Price/Book (P/B)	3.27	3.03	3.33	3.72	4.50	6.65
Price/Cash Flow (P/CF)	100.31	11.33	13.73	15.93	24.33	20.33
P/E (F1)	24.89	21.45	18.79	23.34	23.27	26.36
Price/Sales (P/S)	5.44	1.44	2.64	6.62	6.28	4.55
Earnings Yield	4.03%	4.42%	5.32%	4.28%	4.30%	3.80%
Debt/Equity	0.36	1.18	0.72	0.22	0.14	0.05
Cash Flow (\$/share)	0.07	1.79	6.94	3.72	4.50	6.30
<b>Growth Score</b>	<b>B</b>	-	-	<b>F</b>	<b>F</b>	<b>B</b>
Hist. EPS Growth (3-5 yrs)	NA%	6.08%	10.56%	15.57%	16.76%	33.73%
Proj. EPS Growth (F1/F0)	6.78%	29.14%	7.49%	14.22%	0.18%	-19.47%
Curr. Cash Flow Growth	1.02%	13.25%	14.83%	2.15%	11.18%	98.75%
Hist. Cash Flow Growth (3-5 yrs)	22.57%	6.61%	9.00%	17.97%	17.13%	0.39%
Current Ratio	2.12	1.09	1.23	3.43	3.32	1.48
Debt/Capital	26.43%	57.79%	42.99%	17.93%	12.20%	5.16%
Net Margin	3.94%	1.41%	11.08%	23.66%	54.01%	11.14%
Return on Equity	-11.86%	4.85%	17.16%	13.91%	17.54%	26.81%
Sales/Assets	0.40	0.46	0.55	0.39	0.53	0.72
Proj. Sales Growth (F1/F0)	12.02%	4.89%	4.20%	8.02%	3.75%	-2.86%
<b>Momentum Score</b>	<b>A</b>	-	-	<b>F</b>	<b>D</b>	<b>D</b>
Daily Price Chg	1.67%	0.00%	0.53%	-0.90%	-0.12%	0.16%
1 Week Price Chg	-0.32%	0.00%	-0.30%	-0.87%	-1.13%	-1.82%
4 Week Price Chg	8.06%	1.52%	1.92%	1.33%	4.06%	2.20%
12 Week Price Chg	7.37%	11.66%	6.54%	6.75%	13.02%	4.30%
52 Week Price Chg	56.18%	13.53%	22.58%	15.56%	20.16%	16.38%
20 Day Average Volume	11,698,998	60,867	1,580,816	4,258,908	1,660,676	951,729
(F1) EPS Est 1 week change	5.85%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	5.85%	0.00%	0.00%	-0.30%	0.00%	0.00%
(F1) EPS Est 12 week change	7.50%	-7.80%	-0.50%	-0.19%	0.37%	2.05%
(Q1) EPS Est Mthly Chg	8.33%	0.00%	0.00%	0.00%	0.00%	0.00%

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## 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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### 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	F
Growth Score	B
Momentum Score	A
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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