Activision Blizzard, Inc.
(NASDAQ: ATVI)
Sector: Technology

<table>
<thead>
<tr>
<th>Target Price</th>
<th>Current Price</th>
<th>52 Week High</th>
<th>52 Week Low</th>
<th>P/E</th>
<th>Market Cap.</th>
<th>Dividend Yield</th>
<th>Beta</th>
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</thead>
<tbody>
<tr>
<td>$53.08</td>
<td>$45.44</td>
<td>$47.63</td>
<td>$28.65</td>
<td>34.22</td>
<td>$33.69B</td>
<td>0.57%</td>
<td>0.82</td>
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Business Description
Activision Blizzard, Inc., is a worldwide leader in the development and publishing of online, personal computer (PC), video game console, mobile, and tablet games. The company operates through three main segments: Activision Publishing, Blizzard Entertainment, and King Digital Entertainment. Activision, known for franchises such as Call of Duty, develops and publishes interactive software products with a focus on the video game console. Blizzard Entertainment, publishes online subscription-based, multiplayer online role-playing games. King Digital Entertainment produces mobile games such as the Candy Crush series. The company sells their developed and published products through retail and digital channels. The breakdown based on percent of revenue in 2016 is ($6.23 billion total): Activision: 36% | Blizzard: 39% | King: 25%

Industry Trends
The video game market remains one of the fastest growing industries with roughly $100 billion in annual revenues as of 2016, which represents a growth rate of 8.5% relative to 2015. Altogether, the industry is expected to grow at a rate of 6.6% through 2019, which is second in the global entertainment media market. The industry can be broken down into four segments: PC, console, mobile, and tablet. The PC segment represented the largest share with $31.9 billion in sales. Console and mobile game sales were not far behind with $29 billion and $27 billion respectively. The mobile segment is expected to outgrow the other segments in coming years due to the projected growth in smartphone users. It is projected that there will be roughly six billion smartphone users in the world by 2020, compared to the three billion today. The market has also seen a shift towards the digital distribution channel, which is a higher-margin channel when compared to retail due to the reduced costs from packaging, distributing, and storing physical copies of games. Another key driver of growth in the industry is the development of E-Sports. There has been significant growth in audience of the E-Sports market over the past few years. It is predicted that the audience will grow at an 11.2% CAGR through 2019. With this growth in audience, global revenues from E-Sports is expected to double to $1.7 billion by 2019, which represents a 41% CAGR.

Investment Thesis
Activision Blizzard is significantly undervalued due to the company’s continual innovation and transition into the mobile segment of the video game industry. The company’s dominant franchise game and growingly diversified revenue streams make Activision an attractive long-term investment. The successful launch of Overwatch, provides a strong platform as the company pushes into E-Sports. It plans to develop a professional league for competitive Overwatch players. Additionally, with the acquisition of King Digital, the company is expanding into the fastest growing market segment. Lastly, Activision Blizzard stands to gain from an overall increase in the video game industry as well as a shift into the digital distribution channel.

Competitive Analysis
While Activision Blizzard competes with many companies in the entertainment industry that offer services such as video streaming, music and film, Activision’s closest competitors are Electronic Arts and Take Two Interactive. Both companies develop and market entertainment products and own successful franchises, but also have weaknesses when compared to Activision. EA, for example, is dependent on console sales since most of the games they offer do not have the software capabilities to be played on personal computers. On the other hand, Take Two, does not have the same mobile capabilities. Activision has since they are more focused on console and personal computer video games.

Valuation Assumptions
WACC: 6.30%
Terminal FCF Growth Rate: 2.0%

Key Financials
ROA: 5.58%
ROE: 11.2%

Corporate Social Responsibility
ESG Disclosure Score: 47.5 (Industry average: 42.56)
Sustainalytics ESG Score: 88.2 (Industry average: 75.05)
Percent Female Executives: 13.3% (Industry average: 15.34%)
Women Mgmt. to Employee Ratio: 0.83 (Industry average: 0.82)
Average Exec. Salary + Bonus: $964.6K (Industry average: $855.12K)

5-Year Stock Performance

Growth Opportunities
E-Sports: The global E-Sports market is expected to grow to $1B by 2019 and Activision is expecting to compete in that market with its MLG subsidiary. The MLG business unit is expected to stream and organize competitive video game tournament, generating sales through advertising, media rights and ticket sales. The company’s recent hit game, Overwatch, does not have a steady tournament system implemented yet, but is projected to compete with League of Legends (owned by Tencent), the largest game in E-Sports today.

Mobile Gaming: Before Activision acquired King, the company relied on in-game purchases for sales since its advertising model was flawed. Activision is now creating a new model that not only delivers an enjoyable experience for players, but also delivers significant value with advertisers. Management has stated in recent earnings calls that the market tests and feedback are coming back positive.

Risk
Dependence on Small Number of Franchises: As of fiscal year 2016, the franchises games Call of Duty, World of Warcraft, Skylanders and Destiny account for approximately 71% of revenues. Although this portion is large, it has been decreasing and will decrease at a faster rate with Activision’s expansion in mobile video games and its development of micro-transactions for Overwatch.

Report Prepared By:
Tommy Stodolski & Taishi Kato on 2/26/2017
Sources: Bloomberg, Yahoo! Finance