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NEXON Co., Ltd. (3659.JP)

Q1 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, everyone, and welcome to Nexon's 2017 First Quarter Earnings Conference Call. Today's call is being recorded. At this time, I would like to turn the call over to Maiko Ara, Head of the Corporate Development and IR team. Please go ahead, ma'am.

Maiko Ara

Corporate Development & IR Team, NEXON Co., Ltd.

Hello, everyone, and welcome. Thank you for joining us today. With me are Owen Mahoney, President and CEO of Nexon, and Shiro Uemura, CFO. Today's call will contain forward-looking statements including statements about our results of operations and financial conditions, such as revenues attributable to our key titles; growth prospects, including with respect to the online games industry; our ability to compete effectively, adapt to new technologies, and address new technical challenges; our use of intellectual property; and other statements that are not historical facts.

These statements represent our predictions, projections and expectations about future events, which we believe are reasonable or based on reasonable assumptions. However, numerous risks and uncertainties could cause actual results to differ materially from those expressed or implied in the forward-looking statements. Information on some of these risks and uncertainties can be found in our earnings-related IR documents. We assume no obligation to update or alter any forward-looking statements.

Please note Net Income refers to net income attributable to owners of the parent, as stated in Nexon's consolidated financial results.

Furthermore, this conference call is intended to provide investors and analysts with financial and operational information about Nexon, not to solicit or recommend any sale or purchase of stock or other securities of Nexon.

We'd also like to remind you that we're taking a new approach to our earnings conference call. We will not be hosting separate conference calls in Japanese and English, but will be combining the two conference calls together with simultaneous translations in Japanese and English.

Our IR team will be available after the conference call to answer questions from those people who don't have a chance to participate in the Q&A session.

This recording will be available on our Investor Relations website, www.ir.nexon.co.jp/en/ following this call. Unauthorized recording of this call is not permitted.

I'd now like to turn the call over to Owen.

Owen Mahoney

President and Chief Executive Officer, NEXON Co., Ltd.

Thank you, Ara-san, and thank you all very much for joining us today.

On today's call, I am going to outline the strong results Nexon delivered in the first quarter as well as our outlook in the second quarter and the full year.

Overall, we are very pleased with how we have started the year, and particularly, how the deep investments we've made in new games is aligning with our broader strategy of sustaining consumer engagement with strong live operations.

Now I'd like to share a few highlights of the first quarter and provide you with some updates on our business worldwide. We delivered another great quarter with revenues ahead of our expectations. The first quarter represented record high quarterly revenues, operating income, and net income since the IPO. This was primarily driven by exceptionally strong performance in China around the important January Lunar New Year season, which continued into March.

Last quarter, we said China Dungeon&Fighter Lunar New Year update, which started in mid-January, got off to a great start. The momentum of this update continued through the rest of the first quarter. Item sales in March were also stronger than we had expected. Together, these factors combined to drive significant outperformance for us in China.

MapleStory also delivered solid results with continued year-over-year revenue growth in Korea and globally.

In last quarter's earnings briefing, I talked about the longevity of our flagship games, which are showing themselves to be incredibly robust over a period of many years. And the first quarter continued that trend, again underscoring this core strength of Nexon.

This ability to grow a live online game over many years is Nexon's core strength. Behind the scenes, we have been working to extend this strength, by developing tools and management approaches that enable us to apply our best live game operations and development capability to more games, and around the world.

I'm pleased with the progress of our Japan business showed in the quarter, with revenues up both sequentially and year-over-year, thanks to the solid performance of mobile games including HIT and HIDE AND FIRE. This is our highest reported revenue in Japan in seven quarters.

As most of you know, we had been generating more mobile revenues from browser games than from native games. In the first quarter, this trend reversed, and revenues from native games accounted for more than half of the mobile revenues in Japan.

A few weeks ago, we launched a new mobile native game Disney Touch Touch in Japan, our first Disney game. This is the first of many really exciting games we are going to be bringing to Japan during this year.

While our Japan business is starting to perform better, we also made the decision recently to terminate the development of LAPLACE LINK after it failed to meet our quality and KPI standards during the Open Beta.

Nonetheless we continue to see a significant opportunity to grow our Japan business. Our perspective is that Japan is one of the great untapped markets for online games, especially in mobile.

But the offerings in games on console and mobile have been largely single player-focused games. Japan has not yet become a major market for multiplayer online games, the kind that Nexon specializes in. This is changing rapidly, as mobile devices with outstanding network technology and advanced Graphics Processing Units enable highly immersive online games.

We believe we can lead in this rapidly developing market opportunity, as we have an outstanding live operations team in Japan that we built over the last 10 years for the PC market, and we can leverage that team for the much bigger mobile market.

This team knows how to make a live game last and grow for a very long time. We intend to combine that capability, with great game development that is close to Japanese tastes.

We have already seen some early successes of this combination with games developed outside Japan, namely HIT and HIDE AND FIRE, and we want to lean into this opportunity with games developed inside Japan.

So we have been beefing up the leadership team in the region. During the quarter, we transferred one of our most senior development leaders to oversee new game development in mobile in Japan, including gloops.

Along with the support of the rest of our global organization, you will see us develop more games in Japan, making Japan a second major internal development hub for us, in addition to Korea.

Turning to the West, I want to highlight an important milestone we reached in the United States, one with strategic importance for our initiative of expanding Nexon's reach with Western consumers.

In April, we announced that our mobile title, DomiNations surpassed lifetime revenues of more than \$100 million. We launched DomiNations in the U.S. roughly two years ago and it has been growing – showing the kind of consistency and longevity in performance that has marked some of our biggest franchises.

Now, I want to shift gears a little and talk about new games. At Nexon, we're in the enviable position of having multiple blockbuster titles that generate solid, recurring revenue. This allows us to take creative risks on new games without endangering our core business.

At the end of March, we launched Dynasty Warriors Unleashed worldwide, excluding Japan and China. This is a mobile action RPG based on the popular Dynasty Warriors 7 IP. The game is off to a good start, especially in Asia and we expect the title to contribute to earnings starting in the second quarter.

Next, LawBreakers will be launching in Western markets this year. LawBreakers is a highly unique take on the classic arena first person shooter and we think its intense action and unique approach is a great offering for the hardcore FPS audience. The game completed its first closed beta test as well as had a great PAX East presence in March.

Nexon is launching many more titles around the world and our operations teams are extremely busy preparing for these launches which we hope will sustain player engagement for months, even years, longer than expected under current industry trends. I look forward to telling you more about the development and the performance of some of these titles as we get further into the year.

Lastly, I'd like to talk about the recent change we made to our dividend policy. As you know, Nexon is highly profitable on a worldwide basis and has a significant cash position. From 2013 year-end until mid 2016, we have been paying a shareholder dividend of ¥5 per share semi-annually.

Our dividend to shareholders gets paid out of NEXON Company, Limited, the listed Japanese corporation, which is the parent company of Nexon Group. While this entity comprises less than 10% of our global sales, its costs include not only our local game operations and development functions in Japan, but also a variety of costs for the global organization, including growth investments in several global entities and related impairments or losses, as well as stock options.

As a result, the amount of retained earnings in this entity at this point in time constrains our ability to support an ongoing dividend. We, therefore, decided to suspend the dividend and retain the flexibility to continue our growth investments in our global operations.

As the Japanese entity rebuilds its reserves, we will continue to reevaluate reinitiating the dividend. Our previously-announced buyback plan of ¥10 billion over a one year period from February 13, 2017, remains intact.

With that, I'll turn the call over to our CFO, Uemura-san.

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

Thank you, Owen. Now, let's move on to Q1 results. For additional details, please see the Q1 2017 investor presentation available on our IR website. We were pleased that revenues exceeded our outlook during the quarter. For Q1, revenues were ¥74.8 billion, up 30% year-over-year on an as-reported basis and up 33% year-over-year on a constant currency basis. Operating income was ¥39.8 billion and net income was ¥19.9 billion.

The first quarter revenue outperformance was primarily due to the exceptionally strong performance of Dungeon&Fighter in China. Operating income also exceeded our outlook and this was primarily due to the revenue outperformance in China, which is higher margin revenue, partially offset by ¥2.7 billion impairment loss on items including subsidiaries, goodwill and game IPs.

While operating income exceeded our outlook, net income was below our outlook due to the FX loss of ¥15.9 billion on our U.S. dollar-denominated cash deposits and accounts receivable related to the appreciation of the Korean won and Japanese yen against the U.S. dollar during the first quarter.

As Owen mentioned, revenues for Dungeon&Fighter in China for the first quarter significantly exceeded our outlook. This was driven by the strong performance at the Lunar New Year update introduced on January 17 and

continued until March 28, which had a strong start and remained robust throughout the quarter in addition to very good item sales in March. Also, the Level Cap update introduced on January 17 was well received by core users. Each of the key performance indicators for Dungeon&Fighter in China included MAUs, paying users and ARPPU increased both quarter-over-quarter and year-over-year.

Revenues from the Korean business in the first quarter exceeded our outlook primarily due to the strong performances of our key titles, including Dungeon&Fighter, FIFA Online 3 and FIFA Online 3 M.

As for Dungeon&Fighter, the new character, Female Priest that we added in January was well-received in addition to the strong package sales in time for the Lunar New Year. FIFA Online 3 and FIFA Online 3 M exceeded our outlook primarily due to the strong sales of the Lunar New Year package. In addition, successful promotions had a positive impact on the revenues.

Revenue from our Korean business exceeded our outlook, but it decreased year-on-year. This was mainly due to the significant year-on-year decreases in revenues from Sudden Attack and HIT.

Now, let me turn to Q2 outlook. For the second quarter, we expect revenues in the range of ¥41.3 billion to ¥44.8 billion, 8% to 18% increase year-on-year on an as-reported basis. On a constant currency basis, we expect revenues in the range of ¥39.7 billion to ¥43.1 billion, 4% to 13% increase year-on-year. We expect the operating income to be in the range of ¥11.2 billion to ¥14 billion, net income to be in the range of ¥10.4 billion to ¥12.8 billion.

We expect revenues to increase year-on-year primarily in Europe and other regions in China. In Europe and other regions, we expect the mobile games, Dynasty Warriors: Unleashed, launched at the end of March, to contribute significantly to our Q2 revenues. This game is performing well, particularly in Taiwan and Southeast Asia.

In China, we introduced a tier 1 content update to our key PC online game Dungeon&Fighter on April 27 in time for Labor Day and it is off to a good start. We are also scheduled to introduce the ninth anniversary update during the Q2. The number of active users and paying users from April have remained high compared to the same period last year. Therefore, we expect the revenues to grow year-on-year.

In the second quarter, we expect operating income to be in the range of ¥11.2 billion to ¥14 billion, a decrease of 17% to an increase of 5% year-on-year. Positive driver for operating income is an increased revenue driven by our high margin China business and the contribution from new mobile games in Europe and other regions.

As for negative drivers, first, greater marketing costs related mainly to the launch of new titles; second, increased variable costs including PG fees related to the year-on-year increase in mobile revenues and royalty costs due to the solid performance of publishing titles including Dynasty Warriors: Unleashed; third, higher HR cost due to the head count increase, primarily in Korea.

When we see upper range of operating income outlook, we expect to impact from the positive driver to be larger than the negative drivers, resulting in operating income growth year-over-year.

Now, we will be happy to take your questions

Maiko Ara

Corporate Development & IR Team, NEXON Co., Ltd.

This is all from our side. We will like to open the floor for Q&A.

QUESTION AND ANSWER SECTION

Operator: Today's question-and-answer session will be conducted live over the phone. [Operator Instructions]
The first person is SMBC Nikko, Maeda-san, please.

Eiji Maeda

Analyst, SMBC Nikko Securities Inc.

Q

I have three questions altogether, so I will ask you one question at a time. Is that okay?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Yes, please do that.

Eiji Maeda

Analyst, SMBC Nikko Securities Inc.

Q

Firstly, I have a question about your dividend policy. You mentioned that you will forgo a dividend for some time. And I want to know what kind of conditions are necessary for you to reinstate your dividend? You need to get cash from your overseas subsidiaries, I believe. And you said that you are going to invest in acquiring new IPs. And on [ph] PL (19:37), will there be any impact? Meaning that are you going to have upfront investment on [ph] PL (19:45) as well, please?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Thank you very much for your question. Regarding our dividend policy, we have been investing for growth and we have been trying to balance this with our shareholders return and that is what we have been mentioning so far. Management reviewed the positioning of Nexon and we decided to forego dividend. And there are several reasons. We are not a mature company, but rather we have much leeway for further growth. And we have listed company in Japan, i.e., Nexon Company, Limited and we do not have sufficient profit in order to provide dividend. So, I believe that we might not be able to invest for growth if we continue paying the dividend. Therefore, we would like to focus on the growth initially. And we need to have much investment for future growth.

Therefore, initially, we will try to focus on spending our cash for our future growth. And once we are on the right path, of course, there will be reserves accumulated in NEXON Company, Limited. And we believe that when time comes, it will be possible for us to provide different means for shareholders return.

Now about [ph] PL (21:26), if we conduct investment and if we have to incur impairment loss, we have to book that as impairment loss on our PL. We believe that we have to be aggressive in making investment, but needless to say, not all investments will be a success. And in those instances, we need to recognize them as losses.

Eiji Maeda

Analyst, SMBC Nikko Securities Inc.

Q

Thank you very much. Second question. It is about Korea. You mentioned that there has been a decrease of HIT in Korea. And looking at the title such as FIFA Mobile, I believe that title other than FIFA Mobile is not on the top-ranking list. And in terms of smartphone/mobile games, what kind of competitive edge do you have?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Yes, you're right. There has been a decrease in HIT, but considering what evolved last year, HIT was a major popular title in Korea last year and a year has passed since then. And therefore, we cannot help deceleration of the game.

Talking about mobile, when you compare it with PC, longevity of mobile game is shorter. Having said that, we need to continuously launch titles such as HIT in the mobile domain. Currently, we do not have any large title launch plan, so FIFA Online mobile is the only title on the top 10 list. But we will try to enrich our pipeline and so that we will be able to launch titles that can be in the top-ranking list.

Eiji Maeda

Analyst, SMBC Nikko Securities Inc.

Q

Thank you very much. Third question. It is about China Dungeon&Fighter. I want to confirm different points. In Q1, in terms of ARPPU and paid users and MAU, these KPIs went up. And, year-on-year, on a constant basis, it grew by 78%. And out of all these KPIs, which was the major contributing factor in Q1?

Talking about Q2, if the environment stays the same, I believe that you can expect a lot in Q1. But I believe that as a sale will decrease in Q2 as compared to Q1 and I guess you believe that, number-wise, Q2 will be lower than Q1, but it's still promising. A long stable operation is important, and I understand that Q1 was very good in terms of performance. And do you think this can continue? But in the Q1 of next fiscal year, do you think we will have a negative rebound as compared to Q1 that test has [ph] ended (25:03)? Can you tell me the details?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

About China Dungeon&Fighter, about Q1, we were able to track very good performance. And what is the backdrop? The Lunar New Year package was very good. We had Dragon Land as a new theme and it was a limited offer content. And, at the same time, level cap was updated. And so far, the maximum level was set and once you reach that point, you cannot further elevate your level. But it has been updated, so you can further go up the ladder.

So, the game was further reintegrated and so I believe that Dragon Land trigger the popularity. So, during the quarter, it outperformed our plan. So, all the KPIs, MAU, ARPPU and paying user number, all these KPIs went up. So, it's not that any one of the KPIs was good, but rather it is across the board improvement of all the KPIs and that is the result of our analysis.

Talking about Q2, of course, as mentioned before, Q1 was a great success because the content update and Level Cap update contributed positively to our performance result. So in a way it was a very special situation. So, in Q2 we can increase Y-o-Y, but we should say that Q1 was a special case.

Talking about the upside, looking at our recent numbers, we have the plan up until the Labor Day and KPI is very robust. And there is nothing to worry about. In May and June, is this momentum continues in Q2? And maybe the result might be better than our forecast. But having said that, Q1 was a superb quarter. So, as mentioned before, a stable operation is the key that we focus on. And so, we want the users to enjoy the in-game play and that will be the measures that we will be taking in Q2. So, in Q1, there was a [ph] Y-o-Y (27:48) dramatic improvement, but in Q2, we will not see that level of improvement.

Eiji Maeda

Analyst, SMBC Nikko Securities Inc.

Thank you very much.

Q

Operator: Next, from Nomura Securities, we have Ms. Yamamura, Junko Yamamura.

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

Thank you very much for the presentation. I am Yamamura. I hope you can hear me.

Q

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

Yes.

A

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

Great results. Congratulations. I have three questions as well. First is about the Chinese government regulation on the Korean games. But the Dungeon&Fighter is an existing game, so it's not going to be affected. But in the future content and events, when you consider those, for example, you might need approval from the government and so you might not be able to do the events in a timely manner.

Q

Are you seeing some of the impacts like that or in the similar way, the PCs in China MapleStory 2 CBT was started? And MapleStory 2, I believe, is one of the new titles and CBT was conducted. So it does that mean that this title did not have any problems about the launch. So, in relation to the China government regulation, could you answer my questions?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

Yes. Thank you for your question. About the regulation in China, about the existing live games and events and content, there will be no impact from the regulations. So, now regulations. As for the MapleStory 2, it is a new title but already it's been approved. So concerning that, it's not going to be regulated.

A

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

I see. Thank you very much. Okay. Then, recently you haven't really seen any impact, is that right?

Q

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

Basically, I want to clarify first, the regulation in China is being reported by the press. But whether there will be actually the regulation or not, we have not yet heard precisely and the government, the Chinese government, has not made any announcement. So, as for the future impact, we are not in a position to make that comment. So right now, we don't know. But there are no facts to show that there are any impact from the regulations.

A

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

Q

Second question. Sangokushi Sousouden Online and also the Dynasty Warriors: Unleashed was released in Korea and Asia and probably you will consider a launch in Japan. So, console IP is the base and when you operate the mobile games like that, how to monetize? Is it difficult or IP is so well-known, is it easier to attract users, players? So, Japanese, a console player's IP was used in the action titles. So, based on that experience, KPI or user preference, have you seen any changes? So, if you have to launch this in Japan, maybe that would be related to your strategy, so any comment on that.

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Yes. Yes, we do use this IP of the Dynasty Warrior. And Korea and also in Southeast Asia, we started very well, but we just started the distribution so we need to do a detailed analysis from now on. But Japanese IP is very popular, especially in Asia. So, we would continue to acquire those IP so that we can analyze this experience and utilize it.

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

Q

Thank you. My final question is about the Lineage II and your titles – tight impact on your title, especially HIT and core RPG mobile titles. There might be some cannibalization. I see some of the signs of that. So, by Lineage II, the users, the attitude, do you think that will be positive for you or core RPG title, do you think that there could be some cannibalization? So, is that going to be a negative? So, Dark Avenger is in the pipeline, so is it positive or negative based on your feeling right now? Any comments on that.

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Yes. Lineage II impact, it's one of the blockbusters, it's a big hit. So, in the same [ph] genre (34:03) title there, we expect some impact. But in Korea, the current status is that several titles or actually the Lineage II is the only winner. So, in the same [ph] genre (34:21) more interesting, higher quality games, we can launch them, so that we can have a ranking number one just as HIT did in the past. So, we'd like to win that way.

Junko Yamamura

Analyst, Nomura Securities Co., Ltd.

Q

I see. Thank you very much.

Operator: The next question comes from Mr. Han-Joon Kim from Deutsche Bank. Please go ahead.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)

Q

Great. Thank you very much for the opportunity to ask questions. I have three as well. The first one is kind of quick. I think in one of the prior questions you mentioned that the KPIs for Dungeon&Fighter China is being sustained in April and May. So, can you just help confirm that that was what the trend is currently.

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Thank you very much for your question. Regarding KPI, I would like to repeat what I said. We have the update for Lunar New Year and we updated the Level Cap and it actually stimulated users. And Y-o-Y, KPI all went up and that was the situation of Q1. So, from January to March that was the situation.

And in April, the momentum is there and there is no change. But coming May and June, we are enjoying very good situation for a month. So, it might slow down in May and June. But at least up until April, we are seeing a very good momentum.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)

Q

Understood. Thank you very much. The second question is about the idea that I think the current shift in places like Korea and China is moving towards MMORPG with obviously Lineage II: Revolution having done as kind of setting the stage there. But if I look at the pipeline that you have on page 18 of your presentation, I would classify most of them as being sort of MMORPG or more of a solitary experience. So, how do we reconcile the fact that I think the industry trend has moved to a much more multiplayer experience versus the fact that I think our pipelines are a little bit less multiplayer than that?

Owen Mahoney

President and Chief Executive Officer, NEXON Co., Ltd.

A

Hi, Han-Joon, this is Owen. Two thoughts for you. Number one is as an overall comment, I think it's important to – when you have what you think as an industry trend, the industry trend has a tendency sometimes to turn on a dime with the launch of a new product. We could – you and I both know lots of examples of a situation where we thought the industry trend was going in one direction, and then a new game came out, and then, suddenly, the industry trend appears to be very different. And that's the reality when you're doing new game development. It's hard to predict – it's easy to observe an industry trend in hindsight. It's very hard to predict where it goes in the future.

Second of all, we have a lot of games in the pipeline, so I feel personally that we're very, I guess I would say, covered although we don't proactively plan it this way. We plan it based of what we think are interesting thing game ideas. But we have a lot of games, especially on mobile in the pipeline. And one of those games is Durango, and this is a deep, rich multiplayer experience that's coming up this year. So, that's one example where we're really pushing the boundaries on full multiplayer experiences. And I think you've heard us talk about it before and you'll hear us talk about it more as we get closer to the launch date.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)

Q

Understood. I appreciate that comment. Lastly, you mentioned that you aim to get more Made in Japan games out in Japan. I don't think we see them on the list of pipeline that you have on the presentation. So, should I assume that we're just not yet in a stage to announce, I mean, that we should be seeing some of them maybe at best, maybe end of this year or more likely 2018, and I just kind of want to confirm how to think about the progress of the self-developed Japanese titles, and how they should ramp up over the next 18 months or so.

Owen Mahoney

President and Chief Executive Officer, NEXON Co., Ltd.

A

The answer to your question is, we haven't made any announcements. We certainly will when they are ready to be made, but that will be based off of game marketing. But we – as I said in the prepared remarks, we have made really a second small, much smaller obviously, but definitely a development hub around a couple of our best developers. So, we plan to be investing in that and we'll be making announcements of that in due course. Thanks.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)



Thank you. That's all my questions.

Operator: [Operator Instructions] The next question comes from Mr. Han-Joon Kim from Deutsche Bank. Please go ahead.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)



Sorry guys, just one more question, if I may. I've noticed in the pipeline chart as well games like Need for Speed: Edge and Durango have actually been moved a little bit to the right. So, can we just maybe talk about why we may be facing some delays, if any, and just kind of the progression of pipeline and where we think we're going to see a lot of our good stuff come through? Thank you.

Owen Mahoney

President and Chief Executive Officer, NEXON Co., Ltd.



Sure. Let me talk broadly about that, Need for Speed: Edge and Durango are two very different situations. Number one is, on Need for Speed: Edge, we're not the developer. EA is. So, we're the publisher. I can't really comment in detail on that one.

On a game like Durango, I can talk it in a little bit more detail. The thing to remember about massively multiplayer online game is that you have to do a lot of iterative testing. We're not making a movie here where you have a script and then you do principal filming, and then you do post production.

There has to be a lot of iteration in the game. And that happens in a MMORPG around a progressively larger group of people in the same game world at the same time. And then, you find out what doesn't work and what you can optimize and then you – because those players out of thousands and thousands of collective hours of testing, it will give you a lot of great feedback.

Now, it's important to remember that any – that if you have some delays in the front end, if you make – if the game does what you want it to do, you're going to have many, many years of live game operations. So, if you go back in our history, some of our best and biggest games had very similar [ph] source of delays (43:20), so it's not that we are cavalier about it, but the nature of the game development process is about iteration and checking.

And sometimes, those delays come up, because things that you didn't realize would happen in this live world environment with its economy and sociology, and interactions between thousands of players, they're hard to anticipate [ph] you want to (43:39) plan for them, so you make sure that you have a great gaming experience once you open it up to the full group of people.

Han-Joon Kim

Analyst, Deutsche Bank AG (Hong Kong)



Okay. Great. Thank you very much.

Owen Mahoney

President and Chief Executive Officer, NEXON Co., Ltd.



Thank you.

Operator: [Operator Instructions] The next question is JPMorgan, Mori-san, please.

Haruka Mori

Analyst, JPMorgan Securities Japan Co. Ltd.

Q

Thank you very much. I have two questions. First question, it is about the China Dungeon&Fighter. I understand that you gave us different explanations, but it's very difficult to grasp what is happening with China Dungeon&Fighter. So, if possible I would like you to explain the following. Several years ago, you lost many MAUs. So compared from that bottom line, how many users do you have right now? So, if you can tell me the quantitative figures, I will appreciate it.

Also, in terms of China market, I don't know much about it, so please enlighten me. What is happening in the Chinese market and why there is a positive momentum for you or do you think this is a unique situation for Dungeon&Fighter? So, in terms of the PC market, it has been changed. So can you enlighten me on the situation in China?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

Thank you very much for your question. Regarding Dungeon&Fighter in China, I would like to explain to you again. Several years ago, MAU went down because we had a bot sanction. So, the situation is quite different from now. But after bot sanction, we had been emphasizing steady operation and that has been the main focus that we had. And, of course, the content is of high quality, so that we will be able to have a firm grasp of the users and have them enjoy our game. And I think that was one of our key success factors.

I repeat myself, about Q1-wise we had content update which was such a great success. At the same time, we updated the Level Cap. So, the core users who reached the maximum level since the Level Cap has being updated, they can elevate their level. And so, people were more active playing our game.

And also, we had a Dragon Land content upgrade, and we had as a package sale that was in line with the concept of Dragon Land. So, the content upgrade was a big success, and it was assisted by the Level Cap update. And so I believe that this game is very healthy, so in Q2, I believe that we will be able to continue enjoying that momentum.

Talking about Chinese market, PC online game-wise, it is hitting the threshold, so to speak. So, the market itself was not changing dramatically, but rather the operation and content of China Dungeon&Fighter was a success. That is our analysis of the situation.

Haruka Mori

Analyst, JPMorgan Securities Japan Co. Ltd.

Q

So, let me ask you again. You said that MAU went up. So, in terms of other KPIs, MAU, as you can continue that in Q2 as well, I believe. On a constant currency basis, I guess you grew by about 80% and what is the driver? Do you think MAU is the best driver?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

In terms of individual KPI, we do not disclose the details. But, in Q1, the main contributors are, of course, MAU and also our paying user, PU, increased as well.

And also, ARPPU went up as well. And so, you put all those factors together, you'll understand why we were able to read such as great performance Dungeon&Fighter.

Haruka Mori

Analyst, JPMorgan Securities Japan Co. Ltd.

Q

Thank you. Going to the second question which is paying user and I understand that the momentum is still there up until April. And you have factored that in, coming up with the guidance for Q2, I joined in the call late, so maybe you said this before, but can you repeat that?

Shiro Uemura

Representative Director and Chief Financial Officer, NEXON Co., Ltd.

A

In terms of April, during the Labor Day vacation, we had covered the situation. So, that has been factored in, in our Q2 as well. And April, we turned it very favorably. But as mentioned before, a key success factor of Q1 is that we succeeded in the update of Lunar New Year and also the Level Cap update.

So, these are very unique situations. So, we do not say that this situation will continue forevermore but rather the situation of Q1 and Q2 are different. And we have enjoyed the continuation of Q1 in April. But in May and June, usually, we see some steadiness, and I believe that that will be the situation this Q2 as well.

Haruka Mori

Analyst, JPMorgan Securities Japan Co. Ltd.

Q

Thank you.

Operator: [Operator Instructions]

Maiko Ara

Corporate Development & IR Team, NEXON Co., Ltd.

Thank you very much. Since there is no more question, I would like to take this opportunity to thank you for your participation in this call. Please feel free to contact Nexon IR team at investors@nexon.co.jp should you have any further questions. And if you're going to contact us by e-mail, please e-mail the investors@nexon.co.jp.

Operator: Thank you. That concludes today's conference. Thank you for your participation. You may now disconnect.

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