

FY2021 Q4 Earnings Conference Call (February 8th, 2021)

Q&A Summary

【Q】 Regarding China *Dungeon&Fighter*, Q1 outlook seems to reflect meaningful recovery taking into account the initial performance of the Lunar New Year update. Can we expect that we are seeing the early signs of gradual recovery over the long term? Can we say the same thing for Korea *MapleStory*?

【A】 Shiro Uemura (Chief Financial Officer)

As we mentioned in the previous quarter, we have been focused on improving user engagement for China *Dungeon&Fighter* and Korea *MapleStory* by strategically controlling monetization and mainly offering events. As a result, China *Dungeon&Fighter*'s Lunar New Year update, which started from January 20th, is showing good signs and we expect year-over-year growth in Q1. As for Korea *MapleStory*, we expect a decrease in revenue year-over-year due to a challenging comparison with last year's Q1 performance, but various metrics including the Net Promoter Score, a key indicator of player satisfaction, have been improving. Therefore, we believe that the two existing titles are on a recovery track as we had planned.

We would like to make sure to monitor various KPIs and work on daily operations so that we can draw a steady and solid growth trajectory.

【Q】 What is your long-term strategy on the investment in AGBO and the formation of a new Film&Television division? Are you trying to create new IPs, or looking to enter the film and TV business?

【A】 Owen Mahoney (Chief Executive Officer)

The partnership recognizes the enormous untapped value of cross-platform development of global entertainment. Our view is that film, TV, and streaming platforms have a proven ability to drive awareness and engagement in game franchises.

To give you more background, historically, making movies and TV based on games has been spotty at best from a creative perspective. However, it has been very successful from an economic perspective. Our aspiration is to have a creative success that results in both much better short-term and long-term economic success.

AGBO's Russo brother and their team are the most bankable team in Hollywood. As we got to know them better and talked about our plans for the future, we found that we have a very similar view. In other words, it is about world building over a period of years. Also, they are extraordinarily creatively focused. As a result, they have been economically very successful. So, we think that this helps our franchises a lot, not just in one region, but around the world. That is our thinking behind that.

【Q】 Regarding China *Dungeon&Fighter*, is the good performance in January mainly due to an increase in MAU or an increase in ARPPU driven by Lunar New Year package sales? Also, how sustainable is it in the mid to long-term? Furthermore, I recall Level Cap release in the past did not go so well, so I am curious about what makes you confident in the success of Level Cap release scheduled in the first half of 2022?

【A】 Shiro Uemura (Chief Financial Officer)

As a result of our efforts to enhance user engagement in Q4, we are finding more engaged existing users in China *Dungeon&Fighter*. Therefore, rather than an increase in MAU, we believe that the good performance in January was driven by strong package sales. We believe that this is a very good sign as sales naturally increased along with an increase in user engagement.

In terms of Level Cap release in the past, we do not recall that we have not been able to do well, although there may have been times when we were not able to see the full extent of what was expected. One of the objectives of Level Cap release is to revitalize the in-game situation. We believe that by conducting Level Cap release in this current favorable situation, the in-game situation will become even better accordingly.

【Q】 In your presentation deck on page 3, you talked about step-function revenue growth in 2022 and beyond. How do you envision the scale of growth in revenue and operating income?

【A】 **Shiro Uemura (Chief Financial Officer)**

We only disclose our guidance for the next quarter, so we do not have the specific numbers for the full year in 2022. What we can tell you is that for Q1 outlook, we expect existing titles to perform stably. Also, we expect to spend more HR costs¹ and marketing expenses year-over-year as advanced investments. As we plan to launch many new games especially in the latter half of 2022, we will need to secure more talent to operate high-quality games and need to conduct marketing for titles with high expectations.

Although we can not provide specific numbers for 2022, we hope to increase revenues and operating income as we launch new games in the coming quarters.

Owen Mahoney (Chief Executive Officer)

I just want to add on to your question about our phrasing of step-function growth that we will see as a result of the investments we made in 2021 and before. We feel confident in the earnings power of our existing games, and their growth over time in coming years. On top of that, we are entering a very busy period in 2022 and 2023 of new game launches. We are characterizing the layering of new game launches on top of the solid base of existing games and the potential as step-function growth in revenue and earnings power.

【Q】 Why did the HR costs increase significantly in 2021?

【A】 **Shiro Uemura (Chief Financial Officer)**

HR costs increased in 2021 as we increased compensations for our Korean employees to the highest level among the Korean IT industry to secure human resources under fierce competition for talent acquisition in Korea.

As for Q1 2022, the increase in HR costs is mainly due to new hiring. We have a very rich pipeline from 2022 onwards, and we need to secure sufficient human resources not only for development but also for high-quality live operations after the launch.

【Q】 I was wondering if there is any update on *Mobile Dungeon&Fighter* in China or if you have abandoned this game.

【A】 **Owen Mahoney (Chief Executive Officer)**

We have not abandoned our plans for launching *Mobile Dungeon&Fighter* in China. We do not have any major updates for you today, but we remain very committed to getting the game into the hands of our fans as soon as the conditions permit.

¹ HR costs includes HR cost (COGS), HR cost (SG&A) and R&D (SG&A)

【Q】 I would like to ask about your mid- to long-term view for the western markets. What proportion do you think these markets will hold out of your total revenue in the mid- to long-term? I ask this because you are going into the global entertainment space through your investment in AGBO, and we are expecting the release of new titles from Embark Studios. Your current revenue level for these markets is under 20 billion yen. What kind of upside would you be expecting?

【A】 Owen Mahoney (Chief Executive Officer)

I would say we have big ambitions for the West and that it is going to be led by our efforts in new game development. We are very excited about *ARC Raiders*, the first game from Embark Studios, and their following titles. Also, we are excited about games coming out of our Korean studios, such as *KartRider: Drift*, which we think has a real global opportunity.

The investment in AGBO is about augmenting the IP that we have in our portfolio and we are creating and lending ourselves to any other opportunities that they originate. Our ambition is about a global footprint and global opportunity. If we can make a Virtual World last and grow for decades in the West as we have done for *MapleStory* and *Dungeon&Fighter*, that would be a very exciting idea.

【Q】 Recently, we are seeing an acceleration of consolidations in the game space, especially in the US, as in the example of Microsoft acquiring Activision. Non-game companies are acquiring game companies and competition for obtaining good content and IP is getting fierce. As the number of players in the game industry increases and the competition environment changes, do you think there needs to be a shift in your strategy? Please share your view on the recent trend.

【A】 Owen Mahoney (Chief Executive Officer)

To comment on what is going in the industry at large, I think what you are seeing here is what we have been talking about for some time, which is a secular shift in the entertainment industry. A couple of years ago, most media coverage was about linear entertainment, and it was considered non-traditional thinking to talk about interactive content. Today, clearly, there has been a significant shift to interactive, and every media and tech company is talking about interactive openly. This makes companies that have great ability to make Virtual Worlds and interactive entertainment companies that have great IP extraordinarily valuable. I think there is a growing recognition of this shift, and it puts us in a very strong position in the global entertainment industry.
