

FY2017 Q4 Earnings Presentation (Held on February 8, 2018)

Q&A Summary

【Q】 Regarding *Dungeon&Fighter* in China, particularly what is being well received by users since you conducted content update on February 1? Also, please let us know if you have made any changes from the prior year?

【A】 Due to the timing difference of Lunar New Year, we conducted Lunar New Year update on February 1 in 2018, which is roughly two weeks later than that of the prior year. We can't analyze the KPIs until the update concludes, however, *Dungeon&Fighter* in China grew significantly in 2017 and user base is very robust. This year we do not have the level cap update like we had last year and simply introduced content update and new characters, which was received very well. We've reflected the information we saw to date and expect the year-over-year growth as stated in our Q1 outlook.

【Q】 Please share us how you plan to grow titles with various different genre in Korea including *AxE*, *OVERHIT*, *Yulhyulgangho M*, and *Durango: Wild Lands*.

【A】 Our mobile business in Korea is in a good condition with our games achieving hit when we launch major titles. The challenge for us is to achieve longevity. We need to grow our games which will be played for a long period of time. Strategy differs depending on games, however, we think conducting high-quality content updates with speed is the key to longevity. In terms of overseas expansion, our strategy is to quickly bring titles outside of Korea with primary focus on regions where titles resonate well with local users.

【Q】 From mid- to long-term perspective, do you have any particular technology that you are interested in? Is there any priority in where you want to invest?

【A】 We are interested in various areas. One of the interesting examples would be using AI and voice recognition in *Choices* so that you can talk to virtual characters. If you project out 5 or 10 years from now, this is absolutely possible and we believe such technologies would substantially change the game industry. We're very excited about these opportunities, and are working very actively inside the company to go explore them.

【Q】 You described China *Dungeon&Fighter*'s growth as Software as a Service model or annuity-like curve. This is quite different from typical entertainment industry trend. I'm wondering what signs you saw in the China *Dungeon&Fighter* which led you to use such expression.

【A】 It's because *Dungeon&Fighter* has simply shown that pattern. I think the pattern that is in many people's heads when they look at an online game is that a game goes up and then it goes down and 90% of the revenues are made within the first one or two quarters. It's a commonly held mental model because it's often true. It's been traditionally true in the packaged goods games industry, in the early days of Facebook games, and in the mobile business. But the problem with that mental model is that it's not always true, and the exceptions to that model are massive. *Dungeon&Fighter* is an excellent example. It sometimes goes a little bit down and sometimes it goes up. But it is following general trend that is either very stable or increasing over time. The number one question that was asked to us during the IPO roadshow in 2011 was when *Dungeon&Fighter* was going away. And today, *Dungeon&Fighter* is 2 or 2.5 times bigger than it was during the IPO roadshow in 2011. This mental model throws people off about Nexon's business, and that's why I mention it sometimes over and over.

【Q】 Will you launch *Dungeon&Fighter 2D* mobile by the end of 2018?

【A】 We have not yet made any announcements about the launch schedule.

【Q】 You went into console business with *LawBreakers*. Are there any takeaways from that? Any perspective to the console business in general in the coming years?

【A】 In the longer term over the next five years or more, ultimately, we see probably a consolidation or integration between the three major platforms – mobile, PC and console. The networking layer and graphics layer have been developed and I think you're going to see more sophisticated games on mobile like *Durango*. I also think that the console companies are thinking differently about their business than they were even a few years ago. Games were not expected to be played outside the living room, but this idea has been changing as we consume the bulk of our game or media consumption at anywhere. In the medium term, a console represents a huge opportunity particularly for online games. Console games used to be primarily a single player or a group player games, but there's more and more opportunities connecting online. And so, we see that as a big opportunity, which is why we're going to be bringing more games to console in 2018 or beyond.

【Q】 Looking back in 2017, you recorded 3 to 4 billion yen impairment losses in every quarter and the amount has gotten bigger compared to the past years. In what areas have you recorded impairment losses and what is your perspective on impairment loss in the future quarters?

【A】 We recorded impairment losses primarily on game IPs and prepaid loyalties. As long as we continue to challenge and have multiple titles in our pipeline, it will be hard to avoid these impairment losses. The amount of each impairment loss is not so big, however, it will add up to several billion yen when we add everything in total.

【Q】 How big is the contribution of *MapleStory2* to your China business? Does it account for 10% of the Q1 year-over-year growth outlook in China or is it still much smaller than that?

【A】 Since we didn't have this title last year, *MapleStory2* is contributing greatly year-over-year, but compared to *Dungeon&Fighter*, it is not playing a major role in China's growth. However, if we compare it with titles in other regions such as Japan, its contribution is not insignificant. Regarding PC online business, it's important to grow games over time and make them long-run hits. Thus we do not expect revenues to grow rapidly.

【Q】 Please share us any titles that are launching in Q1 among those listed in the pipeline slide on page 22?

【A】 As for PC, we are targeting to launch *FIFA Online 4* before World Cup. *Astellia* will be launching sometime around June. *Battlerite* will launch in 2018. For mobile, we have *Durango*, which already launched in Korea, and we also plan to launch it globally. *OVERHIT* is going to be launching in Japan, but the schedule is not determined yet. The launch schedule for *Elsword M Shadow of Luna* and *KAISER* in Korea is not determined. *DARKNESS RISES*, which is a global service name for *Dark Avenger 3*, is being prepared for global launch. We are preparing *FINAL FANTASY®XI mobile*, *Dungeon&Fighter 2D mobile*, *Project D*, and *MapleStoryM*. Preparation is under way for *Mabinogi Mobile*, targeting the launch in 2018.

【Q】 What makes *Durango* different from other games which showed good starts and faded for various reasons? Please share any quantitative KPIs that show the trajectory for this game could be different from some of the other ones we've seen recently.

【A】 Short answer to the question is it's too early to tell. The play style implies a much longer period of play for customers. *Durango* is a deep, rich MMORPG, and it's the first time that we try something like this on mobile. And as a result, it's hard to predict using benchmarks that we usually look at because it is so different and unique. We don't know the patterns yet. We're not so interested in looking at what will happen over the several weeks, but much more interested in trying to figure out what will happen over the period of couple years. I think it's too early for us to figure out the answer to that question. Qualitatively, we're very happy with the start and the feedback that we're getting from our customers.

【Q】 Regarding *Dungeon&Fighter* for the first quarter in China, I noticed that MAU and the paying ratio declined in the fourth quarter due to seasonality. For the first quarter, are you seeing signs that user bases, for example, MAU and paying ratios are picking back up and perhaps it's a less function of the ARPPU?

【A】 The Lunar New Year was later than the previous year, therefore we haven't fully analyzed the KPIs. Taking about Q4, MAUs slightly declined while paying users slightly increased and ARPPU increased year-over-year. Decrease in MAUs is attributable to bot sanction as well as the timing difference of Lunar New Year update. Normally we start to warm up the game towards the Lunar New Year. Due to the timing difference, we did not start this in Q4. Until 2017 Q3 paying users had been increasing significantly year-over-year, but it increased just slightly in Q4. Therefore the growth drive in Q4 was ARPPU. Considering this trend, ARPPU may increase to some extent year-over-year in Q1. However, if you compare ARPPUs of other PC titles and mobile games in China, it is not as high as you concern. Total number of paying users increased and those people who were buying small items enjoyed purchasing items, and some started to buy packages. That's how we think ARPPU will grow. We think *Dungeon&Fighter* is in a healthy condition.

【Q】 What is the company's monetization strategy for *Durango* including its global service?

【A】 Considering the genre of *Durango*, we do not think this is a game for us to monetize per se, but rather, we want people to continue playing for a long period of time. So far, retention is good, therefore, we believe we aim to service the game for a long time. We would like *Durango* to contribute to both revenues and operating profits during that long period of time. Currently it is contributing to the profit, but again, it is not the type of game we focus on monetization.

【Q】 Regarding *Dungeon&Fighter* in China, Lunar New Year update impacted the company financials until the end of March last year. Based on the early result, until when do you expect this Lunar New Year update to impact your financials?

【A】 Since the Lunar New Year update was later than last year, we expect it will impact our financials until the end of March. In that sense, It may also give a certain impact on our Q2 financials.

【Q】 What is your approach to e-Sports and how do you think about e-Sports business opportunity?

【A】 I think e-Sports is very interesting. But I think the point that people miss is it's primarily a PC environment, not a console or not a mobile environment, at least as of today. Japan is not particularly a PC-oriented market and I'm not quite sure why that attracts so much attention. Also, if you take one or two of the big games out of e-Sports, people would be a whole lot less enthusiastic. And those games are *League of Legends* and probably *Overwatch* as well. There's a lot of traditional sports franchise owners that are very interested in this topic because those sports are on the decline and they are trying to get something new.

From broader perspective, eSports is about viewing games and viewing games is a pretty fun activity. We watch people who are good at playing games, sometimes two guys on a couch making jokes while they play some game, and they're broadcasting that over Twitch. It can make for some very good viewing. However, a lot of things have to be in place for that to be a real business, not just a lot of investment. I don't have a huge prediction about how that will be, but I am somewhat cautious about this.

As far as Nexon is concerned, Nexon has Nexon Arena in Gangnam, Korea. It seats about 550 people. We have roughly 300 events a year. What we find in e-Sports is that players determine what will become an e-Sports game. The gamers themselves determine that. The company doesn't determine that. And there've been a lot of examples where a company has designed what they thought was an e-Sports game, and it just hasn't worked out. Therefore, when you look at a game, you have to watch what players are doing and whether they are watching it broadcasted online.
