

NEXON Co., Ltd.

Q1 2020 Earnings Prepared Remarks

May 13, 2020

Owen Mahoney, Representative Director, President and Chief Executive Officer, NEXON Co., Ltd.

Thank you, Ara-san and thank you all for joining Nexon's first quarter 2020 earnings conference call today.

Before we get into discussing our results, I'd like to acknowledge the horrifying global impact of the COVID-19 crisis. Our first thought is to all our employees, partners, and customers around the world who have been affected by this terrible virus.

In the early stage of the crisis, Nexon instituted various measures – such as travel bans and work-from-home policies – to protect our global workforce. As of today, few of our employees were directly affected, and that in Korea and China, where local officials took strong and decisive actions, most of our employees are back in the office while adhering to strict rules on health and safety.

Throughout the COVID-19 crisis, Nexon has been spared the turbulence due to minimal physical contact with consumers. Unlike most other segments of the leisure and entertainment industry, online games enable millions of people to come together virtually with their friends while still practicing social distancing.

There are three fundamental assumptions which guide us, and which are particularly relevant now:

First, we are in an industry that is not exposed to disruption from COVID-19. On the demand side, online games already assume social distancing, that millions of people from around the world connect and play in a virtual, not a physical world. On the supply side, unlike linear entertainment like TV and movies, which face shocks to their production capability, game developers can work effectively from home, developing new content and providing live services to players around the world without missing a beat. And, when we produce new content, games have content leverage – an hour of new content offers several hours of entertainment for the customer, as opposed to linear entertainment, in which an hour of content rarely translates to more than an hour of consumption.

Second, our focus on deeply immersive online games and virtual worlds will become increasingly powerful. Technology advances now make virtual world experiences available to everyone around the world, through advances in mobile and cloud – an increase in Total Addressable Market of at least 10x from just a few years ago. And, as travel and leisure become potentially unaffordable or infeasible due to geopolitical or economic issues, virtual worlds stand out as a highly compelling and robust alternative. All of this is being demonstrated in our business right now.

And third, Nexon has specifically structured an all-weather business to work in any economic environment, rain or shine. Our bench of IP franchises, while not as recognized in the West, are some of the very biggest in the entire global entertainment industry. We have proven time and again that we can grow these franchises for many years on end. And they have provided Nexon with strong and predictable cash-flows to fund our all-weather balance sheet, which in turn, provides us with strategic flexibility to strengthen and grow our business.

In short while many of the most basic assumptions about our economy, our institutions, and our daily lives are now called into question, the robustness of Nexon's business is not one of those questions. We are stronger than ever and getting stronger.

Now, I'll turn to discussing our First Quarter performance. Uemura-san will provide more detail on our Q1 financial results and our Q2 outlook later in his section.

In the First Quarter, group revenues were 82.8 Bn yen, which came in ahead of our expectations. The better-than-expected revenues were primarily driven by the strong performance across our portfolio in Korea. In China, revenues were in line with our expectations. I'll discuss these more shortly.

During the quarter, we generated EBITDA of 49.9 Bn yen. Our cash position as of March quarter end is 517.6 Bn yen, or about 4.8 Bn USD.

Our performance in Q1 highlights the strength of our franchises coupled with our change in strategy last year to focus on a smaller number of bigger franchises that leverage our core strengths, as well as the direction of the entertainment industry. We expect these benefits to accumulate and grow over time as our strategy plays out in more territories.

Let's start in Korea. In Q1, the *MapleStory* franchise, which just celebrated its 17th anniversary in Korea, delivered yet another outstanding quarter, generating record revenue on both PC and mobile. Constant currency revenue on PC grew 132 percent year-over-year, following 69 percent revenue growth in Q1 2019. The mobile version of *MapleStory* grew 184 percent this Q1, on top of the 22 percent growth a year ago. Certainly, this success reflects Nexon's best-in-class live operations, combined with outstanding content updates. Growth in a live game that accelerates, to triple-digit levels, after 17 years of growth is – to our knowledge, completely unheard of in the online games business.

FIFA ONLINE 4 had a terrific start to the year, growing significantly year-over-year and delivering record quarterly revenue.

Dungeon&Fighter in Korea – a 14-year old franchise – received the new major content update in January ahead of the China service. The update was very well-received by our players in Korea, and revenue grew 53% YoY on constant currency basis, well ahead of our expectations.

Q1 was also a strong quarter for *Sudden Attack*. This franchise, which launched in Korea in 2005, grew 52 percent year-over-year on a constant currency basis. This was driven by the successful introduction of the new season pass, new characters and successful Lunar New Year sales promotions.

V4 – the new mobile MMORPG we released in Korea last November, also exceeded our expectation driven by the successful content update and promotions. Following the successful introduction in Korea, we expanded the geographies and launched the game last month in Taiwan, Hong Kong and Macau.

As a result of these strong performances, we've achieved our highest quarterly revenue in Korea.

Revenue from our China business was within the expected range, driven primarily by *Dungeon&Fighter* on the PC. We launched two, well received, content updates in the first quarter as the game delivered within our forecast. However, many PC cafes in China closed due to COVID-19 which negatively affected our ability to increase engagement and recapture churned users to the levels that we had hoped for.

When looking at the much-anticipated March update, it was well received by our players generating great reviews from our existing base and driving improved engagement.

In short, even with the temporary impact of PC café closures in China, our performance was in line with our expectations. The return-to-growth for the game is developing as we had expected, and we continue to be optimistic about the health of the game and its long-term growth.

Now I'd like to briefly update you on some of the operational changes we made to our global business.

In April, we appointed Simon Cheong as our global Chief Operating Officer. Prior to this, Simon served as our Chief Business Development Officer.

In North America, we assigned Kenny Chang as the head of Nexon America. Kenny has held various leadership positions across Nexon group, most recently, he served as head of Nexon Europe.

We also placed a new leader, Chan Park, to rebuild our PC and mobile business in Japan. Chan has significant experience in both the Japanese game market and in online games.

We believe the leadership changes will further strengthen our global operations and align our global teams to execute on our group strategy.

Turning to our new games, we are making significant progress with our development pipeline that strongly reflects our focus on deep online multiplayer games, on multiple platforms.

First is *KartRider Rush+*. *KartRider Rush+* is the mobile version of our beloved racing game *KartRider*. First launched in China in 2013, the game received a major update last July, which significantly deepened the online experience. Since that update, the game has been performing well in China, and yesterday we launched it in all other global regions excluding Japan and Vietnam. We expect the mobile *KartRider* will add many more fans to this 15 year-old franchise which has a fan base that exceeds 380 million registered users on the PC platform alone.

Second is *FIFA MOBILE*. In March, we announced a new publishing agreement with Electronic Arts to launch and operate a new *FIFA MOBILE* standalone game in Korea. In addition to *FIFA ONLINE 4*, we'll service this new game to deliver an authentic soccer experience which can be played on mobile devices. We recently completed the closed beta test and will launch the game this year in the Korean market.

And last but not the least is *Dungeon&Fighter 2D Mobile* – the mobile version of Nexon's biggest multi-billion dollar franchise, and one of the biggest franchises in the entire global media industry. In February, we completed the second closed beta test, and the results were very encouraging. We have continued to further polish the game and tech; and together with our local partner, Tencent, we'll be releasing the game to the Chinese market in the summer of 2020 with their highest level of game marketing and operational support. While this is slightly later than our original launch schedule, which was in 1H 2020, we're extremely happy about how the development is progressing. We have already pre-registered more than 34 million players since pre-registration began in late December. We are thrilled to bring *Dungeon&Fighter's* deep immersive multiplayer online world to a massive audience on mobile platforms. This represents enormous opportunity for Nexon.

Each of these games – *DnF 2D Mobile*, *FIFA MOBILE*, and *KartRider Rush+* reflect our deeply held conviction that advances in platform technology represent a massive growth opportunity for Nexon. Now, deeply immersive virtual worlds can be experienced not just on the few hundred million game-playable PC's in the world, but on the several billion recent-model iPhone and Android devices that are finally able to support a fully online virtual world. These workstation-level devices in billions of consumers' pockets unlock Nexon's total addressable market. As innovators in virtual worlds and online games, we are highly focused on seizing this historic opportunity.

And our teams are hard at work on several major launches we will be talking about later in the year. One is *KartRider: Drift* – the next generation of our online PC game that will be cross-platform. The other is the first game from Embark Studios, the team in Stockholm Sweden we acquired last year. We think their first game represents a new generation of online games in the West, as well as a massive advance in the technology of game making.

With that, I will turn the call over to our CFO Uemura-san. Thank you.

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

Now, let's move on to the Q1 results.

First, I would like to inform you that we have reclassified two regions which were formerly categorized as "North America" and "Europe and Others". In Q1 2020, we reclassified these regions to "North America and Europe" and "Rest of World".

Recently, the regional characteristic between North America and Europe has increased similarities as we provide the same services to our customers in these territories. Therefore, we have decided to reclassify the reporting segmentation to provide more clarity to our performances.

Prior years' financial performances have also been restated in accordance with the new reporting segmentation.

Now on to the Q1 results. Revenues were 82.8 Bn yen, down 11% year-over-year on an as-reported basis, and down 6% year-over-year on a constant currency basis. These results exceeded our outlook primarily driven by the strong performances of our major PC and mobile titles in Korea.

Looking at the total company results on a platform basis, both PC and mobile revenues exceeded our outlook.

Operating income was 41.5 Bn yen, which was within our expected range. Revenues exceeded our outlook and costs including HR costs were lower than our plan, however, these were partially offset by a 6.1 Bn yen impairment loss primarily on Nexon GT's goodwill and Pixelberry's game IP.

Net income was 49.9 Bn yen, which exceeded our outlook largely driven by an 18.7 Bn yen FX gain related to the depreciation of the Korean Won against the U.S. dollar during the quarter and its corresponding impact on U.S. dollar-denominated cash deposits.

While revenues from our China business in Q1 decreased year-over-year, the performance was within our expected range.

On a local-currency basis, China *Dungeon&Fighter's* revenue was in-line with our expectations.

We introduced the Lunar New Year update on January 14th. This included limited-time-offer dungeons, as well as avatar package offerings, and continued until April 9th.

As we had anticipated, this year's Lunar New Year update was well-received by our players. However, sales from its avatar package offerings declined compared to the year ago quarter when *Dungeon&Fighter* had a higher base of users and paying users.

Since late January, due to the spread of COVID-19, PC cafés in a number of regions in China have suspended their operations.

We launched the new key update which addressed the primary feedback that we had received from our players on March 19th. This update included the level cap release and the third awakening which allows players to gain new skills for their characters. The primary focus of the update was to increase the engagement of the existing players, as well as to regain the churned users, however, the closure of PC cafés negatively affected the game's momentum.

However, the update received great reviews from the existing players, which led to better user engagement following its introduction.

Based on our analysis on our players, including their participation in the in-game events related to the key update prior to its introduction, we believe that there are players who have not been able to return to the game after introduction of the March update due to the closure of PC cafés.

We expect the number of users, as well as other KPIs, will continue to recover as PC cafés re-open and their businesses return to their usual cadence.

While MAUs and paying users decreased quarter-over-quarter due to the negative impact from the shut-down of PC cafés, revenues and ARPPU increased due to typical seasonality.

MAUs decreased year-over-year primarily due to the churn of users in the second half of 2019 as well as the reduced number of bots following the implementation of a stricter measure to verify player identity.

Due to the shut-down of PC cafés and its corresponding negative impact on active users, we did not experience a major improvement in the number of paying users since the second half of 2019. Paying users decreased year-over-year and remained at low level. Revenues and ARPPU also decreased compared to Q1 2019 when we had strong sales from the Lunar New Year package offerings.

In Q1, revenues from our Korea business exceeded our outlook primarily driven by stronger-than-expected performances of our major PC titles including, *MapleStory*, *FIFA ONLINE 4*, *Dungeon&Fighter* and *Sudden Attack* as well as mobile titles including *V4*, *MapleStory M* and *FIFA ONLINE 4 M*.

MapleStory's Q1 revenue exceeded our expectation driven by sustained momentum following the successful Winter update which had continued from the end of last year, as well as the January sales promotions.

User metrics including MAUs, paying users and ARPPU increased year-over-year. The game's revenue grew 132% year-over-year on a constant currency basis marking its highest quarterly revenue in Korea. *MapleStory* has recorded double-digit growth for five consecutive years since 2016 and consistently grew for a remarkable seventh consecutive year. Its revenue is up more than 11x compared with its Q1 2013 performance.

FIFA ONLINE 4's revenues also exceeded our expectations driven by the well-received Lunar New Year package offerings and promotions.

Q1 user metrics including MAUs, paying users and ARPPU increased year-over-year. Combined PC and mobile revenues grew significantly versus a year ago. *FIFA ONLINE 4* also achieved record-high quarterly revenues in Q1.

On January 9th ahead of its release in China, we introduced the major update for *Dungeon&Fighter* in Korea. This included the Level Cap release and the third awakening. The update received positive reviews by our players and generated improved user metrics. The positive momentum continued throughout the quarter, resulting in the game's revenue exceeding our expectation and growing 53% year-over-year on a constant currency basis.

Sudden Attack's revenue also exceeded our expectation and grew 52% year-over-year on a constant currency basis, driven by the successful introduction of the new season pass and characters, as well as the successful Lunar New Year promotions.

As for the mobile business, *V4* performed stronger than our expectation driven by the successful major update introduced in early February.

MapleStory M's revenue also exceeded our expectation driven by the successful introduction of new characters and item sales. On a constant currency basis, revenue grew 184% year-over-year and the game generated its highest quarterly revenue of all time.

MapleStory has grown double-digit for its three consecutive year since the service began in Korea in October 2016. Q1 2020 revenue was more than 5x greater than three years ago – Q1 2017 – which was shortly after the game launched.

Due to these strong performances, both our PC and mobile businesses in Korea grew year-over-year, resulting in an increase in our business.

Revenues from our Japan business were slightly below our outlook.

On a year-over-year basis, while we benefitted from *MapleStory M*, which launched in Q2 2019, this was more than offset by decreases in *FAITH*, *Dynasty Warriors: Unleashed* and *OVERHIT*, all of which launched in 2018, as well as the disposition of gloops which was completed in February. Consequently, revenues decreased year-over-year.

Revenues from North America and Europe in Q1 was down year-over-year, due to declines in *Choices*, *Darkness Rises* and *AxE*. However, this performance was better than we had expected as *Choices* and *MapleStory* both exceeded our outlook.

Revenues from Rest of World exceeded our outlook primarily driven by the stronger-than-expected performance of *MapleStory*.

On a year-over-year basis, *MapleStory's* revenue increased. In addition, we also benefitted from *World of Dragon Nest*, which launched in Southeast Asia on January 8th as well as *V4* which launched in Taiwan, Hong Kong and Macau on March 25th. However, these were more than offset by the deceleration of *AxE*, *MapleStory M* and *Moonlight Blade*. The yen appreciation also negatively impacted the as-reported performance resulting in Q1 Rest of World revenues to be flat year-over-year. However, revenues were up on constant currency basis.

Now turning to our Q2 2020 outlook.

In the quarter, we expect the Chinese Yuan and Korean Won, both major currencies in our business, to depreciate against the Japanese yen and, therefore, to negatively impact the as-reported basis performance of our results.

For Q2 2020, we expect revenues in the range of 59.0 to 64.0 Bn yen, representing an 10% to 19% increase year-over-year on an as-reported basis and a 16% to 26% increase year-over-year on a constant currency basis.

We expect revenues in Korea and China to increase versus the year ago quarter. We anticipate that revenues in Japan, North America and Europe will decrease and that revenues from Rest of World will be roughly flat versus Q2 2019.

We expect our Q2 operating income to be in the range of 21.9 to 26.2 Bn yen, representing a 69% to 102% increase year-over-year on an as-reported basis and an 80% to 115% increase year-over-year on a constant currency basis.

I'll discuss the details of this shortly.

We expect net income to be in the range of 20.3 to 23.7 Bn yen, representing a 6% to 24% increase year-over-year on an as-reported basis and a 13% to 32% increase year-over-year on a constant currency basis.

Turning to China, we expect revenue from *Dungeon&Fighter*, our key PC online game, to increase year-over-year resulting in our China revenues to be in the range of 21.3 to 23.8 Bn yen, representing a 0% to 12% increase year-over-year on an as-reported basis and a 6% to 18% increase year-over-year on a constant currency basis.

We introduced the Labor Day update for *Dungeon&Fighter* on April 23rd. This update includes a new content release, events and avatar package offerings. In addition, we will release the 12th Anniversary update in June.

Following the key update in March, which generated better engagement among the existing users, our KPIs – including active users and paying users – improved.

As a result, we expect *Dungeon&Fighter* Q2 revenue, on a local-currency basis, to be roughly flat year-over-year, even compared to the high base set in Q2 2019.

Also, we expect to record a one-off royalty income related to *Dungeon&Fighter* in Q2.

In 2014, we began selling game items for *Dungeon&Fighter* on Tencent's QQ platform, which is a communication platform, as we increased our sales channels. Sales generated on the QQ platform are small as compared with traditional in-game sales. For this reason, we did not reconcile the sales and royalty for operational effectiveness, however, we recently reviewed those sales for the past six-year period. As a result, we expect to recognize an estimated adjustment of a 2.3 Bn yen royalty income related to the sales from QQ platform.

Including this 2.3 Bn yen royalty income, we expect *Dungeon&Fighter's* revenue in Q2 to increase year-over-year.

We will launch *Dungeon&Fighter 2D Mobile* in the summer of 2020. Accordingly, we have not included its royalty income in our Q2 outlook.

Turning to our Korea business. For *MapleStory*, we have started the 17th anniversary event in late April, and it is off to a good start. We expect the game's strong momentum to continue into Q2 as its revenue yet again grows triple-digits year-over-year.

We also expect our other major franchises, including *FIFA ONLINE 4*, *Sudden Attack* and *Dungeon&Fighter* to post year-over-year growth.

We expect our mobile business in Korea to grow versus Q2 2019, benefiting from *V4* which launched in Q4 2019, as well as the new mobile racing game *KartRider Rush+* which went live yesterday. Moreover, we expect *FIFA ONLINE 4 M* to grow year-over-year and *MapleStory M* to grow triple-digits year-over-year in line with the PC version of *MapleStory*.

We anticipate both PC and mobile revenue to each grow year-over-year. Overall, we anticipate revenues from our Korea business to be in the range of 27.9 to 29.5 Bn yen, representing a 44% to 52% increase year-over-year on an as-reported basis and a [54]% to 62% increase year-over-year on a constant currency basis.

In Japan, we expect to benefit from the new mobile MMORPG *TRAHA*, which launched on April 23rd. However, we expect this to be more than offset by the disposition of gloops and a decrease in revenue from *MapleStory M* due to the difficult comparison with Q2 2019 which was right after the game launched. As a result, we expect revenues in the range of 2.3 to 2.5 Bn yen, representing a 51% to 46% decrease year-over-year on an as-reported basis and a 49% to 44% decrease year-over-year on a constant currency basis.

In North America and Europe, we expect revenues in the range of 4.3 to 4.7 Bn yen, representing a 16% to 8% decrease year-over-year on an as-reported basis and a 13% to 5% decrease year-over-year on a constant currency basis. While we expect to benefit from *KartRider Rush+*, which launched yesterday, we expect this to be more than offset by decreases collectively in *OVERHIT*, *AxE* and *Darkness Rises*.

We expect revenues in the Rest of World in the range of 3.2 to 3.5 Bn yen, representing a 8% decrease to 2% increase year-over-year on an as-reported basis and a 3% decrease to 8% increase year-over-year on a constant currency basis. We expect to benefit from *V4*, *World of Dragon Nest* which launched in Q1, as well as *KartRider Rush+*, which launched yesterday, however, growth from these titles will be offset by decreases in *OVERHIT*, *Moonlight Blade*, *AxE* and *MapleStory M*.

In Q2 2020, we expect operating income to be in the range of 21.9 to 26.2 Bn yen, representing a year-over-year increase of 69% to 102%.

The primary driver for the higher operating income in Q2 2020 is the year-over-year revenue increase.

Other favorable factors include a decreased impairment loss of 3.6 Bn yen recorded in Q2 2019, which will not be repeated in Q2 2020, as well as decreased marketing costs.

Unfavorable factors include an increased variable cost associated with revenue growth.

The high end of the range reflects the fact that we expect the impact of positive drivers to be larger than that of negative drivers, resulting in a year-over-year operating income increase.

Lastly, I would like to update you on our outlook on FY2020 shareholder return.

In accordance with the change of dividend policy approved by the Board of Directors in February, we reinitiated a dividend of 2.5 yen per share in the end of FY2019. We plan to pay the same dividend per share for the interim and year end of FY2020.

We will remain disciplined in delivering shareholder value by growing our business globally and maintaining consistent dividends.

This ends my comments. Back to you Owen.

Owen Mahoney, Representative Director, President and Chief Executive Officer, NEXON Co., Ltd.

Thank you, Uemura-san.

Before we take questions, let me quickly summarize:

While the world is going through unprecedented challenges, the secular shift in the entertainment industry that has already been driving the growth of online games has become even more pronounced. Our teams migrated to working from home efficiently and effectively, allowing us to not only maintain our live service operations but to also continue to create, and release, new content. In fact, we just released one of our biggest franchises *KartRider* to mobile platforms, including iOS and Android."

We have a solid foundation that consists of a substantial IP bench that is bigger or as big as the world's biggest entertainment franchises.

Our teams are making great progress on games and services and today our franchises are stronger than ever.

Growth in Nexon's sweet spot, deeply immersive online games, has sharply accelerated. New technology is allowing us to offer PC-like deep multiplayer online games on multiple platforms, including mobile, the world's biggest platform, which expands our Total Addressable Market by minimally 10x. Finally, our fortress balance sheet provides us with enormous strategic flexibility that we can use to help accelerate our growth.

With that, we'll open the call to your questions.