

NEXON Co., Ltd.

Q2 2021 Earnings Prepared Remarks

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

Thank you, Ara-san, and welcome everyone to Nexon's Second Quarter 2021 Conference Call. Today I will provide a brief update on our second quarter performance and devote the rest of my time to detailing the strategies that position Nexon for significant growth in the coming quarters and years. Following that I will turn the call over to our CFO, Uemura-san, for a detailed financial review of our quarter and the guidance for Q3.

In the second quarter, Nexon delivered revenue that was within our outlook at 56.0Bn yen -- down 13% on an as-reported basis and down 21% on a constant currency basis. *The Kingdom of the Winds*: *Yeon*, *Mabinogi*, and *Sudden Attack* exceeded our expectations while *MapleStory* in Korea came in lower-than-expected. On a platform basis, both PC and mobile revenues were in the range of our outlook. In short, some things went better than expected; others not as well; with the net result putting us within our expected range.

On today's call, I will provide context on how the management team has been investing our time in 2021. We see 2021 as an operational inflection point for improving our live games and polishing multiple new projects – each with the potential for enormous returns. Executing on any...one of these initiatives could dramatically change Nexon's trajectory and bring step-function improvements to our revenue and profitability.

I will start with the actions we've taken to improve the performance of *MapleStory* in Korea, which is facing tough comparisons following the last two years of significant growth, including a 98% jump in year-over-year revenue in 2020. In Q1, we received clear feedback from players on the need for greater communication and transparency on the probability of values assigned to in-game purchases.

Communication on probability and improving player trust has been an industry-wide issue in Korea, and the *MapleStory* team has been aggressively proactive in addressing this issue. Their approach has combined significant investment in time to fully understand players concerns and formulate a thoughtful response, while moving rapidly to implement changes based on this feedback. The objective of this is to get the best long-term solutions in place, as rapidly as possible.

The situation is ongoing, but we are seeing clear signs of progress as we continue to improve. *MapleStory*'s Net Promoter Scores -- an important indicator of player satisfaction – while still below previous levels, have improved significantly. The recently introduced Summer Update has been very well received by players and there's more great content in development.

Investors should be clear that we are highly focused on rebuilding long-term trust and player retention, over short-term monetization. Why? The returns we get over the long-term from focusing on player satisfaction dwarf any near-term benefit from aggressive-monetization now. Investors should be aware that long-term trust and satisfaction of our players is our top priority.

Finally, keep in mind the challenges and efforts are distinctly different than China *Dungeon&Fighter*. China *DnF* is powerful franchise that has recently been in need of a creative spark to re-ignite growth. *MapleStory* Korea is a specific communications challenge around a specific issue. How these challenges affect the respective game and how we are responding are extremely different.

Now to China *Dungeon&Fighter*.

Experience tells us when a team needs new creative leadership to generate dynamic growth, and we recently announced that one of our top creative leaders -- Myeong-jin Yun -- has taken on oversight of development and live-game operations for PC *Dungeon&Fighter* -- including China service. Myeong-jin is also responsible for ongoing development on Mobile *Dungeon&Fighter* and for a new title in the franchise, *Project BBQ*. He led the franchise in China during its best period from 2014–2017, and today he has innovative ideas for shaking up the content plan to re-engage players.

As I said a moment ago, improving execution on Korea *MapleStory* and China *Dungeon&Fighter* are two distinctly different initiatives. Success on one or both would have a dramatically positive impact on Nexon's financial profile.

Next, I will outline our updates for layering new Virtual Worlds and revenue opportunities onto our existing business.

The first is *Mobile Dungeon and Fighter*, a game that generated more than 60 million pre-registrations when it was announced in 2020. While we don't have any news to share with you today, under the direction of Myeong-jin, the team is developing significant additional content ahead of the launch. We remain extremely excited about bringing this game to our fans in China.

Next is *KartRider: Drift*, a new arcade racing title based on another popular Nexon franchise. While we haven't locked on a release date, our ambition is to give this title a simultaneous launch in multiple markets around the world. The team is now focused on polishing

gameplay. As we announced earlier, *KartRider. Drift* is currently being developed for both PC and the XBox. And the team is studying ways to make the game enjoyable for worldwide players without any restrictions on when they play, or on which platform. We will be making additional announcements about the content plan in coming months.

Next is the first game from Stockholm-based, Embark Studios – this game will be a mass market Virtual World targeting a large and well-established player base. In July, Embark hosted a milestone meeting and in-depth testing that included key leaders from Nexon. All were deeply impressed. The team has been making rapid progress, and the game is stunning, reflecting Embark's high artistic standards and, importantly, the high priority they place on fine-tuning the pacing and tension.

To make a AAA online play experience set in a Virtual World would normally require massive investment of many hundreds of people. Fortunately Embark invested heavily in creating tools for rapid content development. This set of tools and technology is valuable both before launch and after. Before launch it results in not just faster development and lower development costs, but faster and deeper iteration in the development process, since ideas can be tested and developed rapidly. Put simply, more iteration results in a better, more unique game. In AAA development, iteration is typically much harder due to the high cost of trying new ideas and throwing out what doesn't work. After launch it means much faster introduction of new content into the live Virtual World, using a fraction of the development team. We think this tech stack will be a game changer for Embark's first title, and for future games across the Nexon development portfolio.

In addition to our previously announced 3 big beats mentioned above, for the first time Nexon unveiled several additional titles in our development pipeline at an announcement event in Seoul last week. Twelve games in development were showcased including *PROJECT MAGNUM*, *Project HP*, *Mabinogi Mobile* and *KartRider. Drift*. The titles under development represent a variety of genres, and target geographies. But all reflect the common theme of focus, on fewer but better online games and Virtual Worlds.

In addition to our robust content pipeline, Nexon is investing in innovative strategies for developing new revenue streams from our deep bench of blockbuster intellectual property. To date we have exploited a small fraction of our potential, given the size and popularity of our IP portfolio.

In July, we announced the appointment of Nick van Dyk as Nexon's Chief Strategy Officer and as President of Nexon Film and Television, a new division of the company focused on

expanding the value and reach of our IP. Nick is well known in the global entertainment industry from his accomplishments as a senior executive at The Walt Disney Company and later at Activision.

By way of context, over the last several months I've had the privilege of talking with our new board member Kevin Mayer about how he, Bob Iger, Nick and others at Disney architected arguably the greatest media flywheel of all time during the 2000's. Their leadership resulted in an explosion of creativity and growth for Disney. Both Kevin and Nick see the same latent, untapped value at NEXON that they saw previously at Disney, but now in a new era, in a fully digital arena. So Nick's appointment is not about NEXON making movies. It's about harnessing the untapped potential of NEXON's intellectual property, reaching new audiences for our core properties, and driving revenue and profitability.

To summarize: NEXON is sharply focused on growth. We are making strategic use of a transitional period to improve our existing blockbusters, to perfect and polish a pipeline of exciting new games, and to maximize the value of our IP. Each of these projects targets a large potential player base with a unique product. That translates to the potential for fast growth into large markets.

The reason we are so focused on the projects I've highlighted today is that any one of these initiatives could deliver a step-function improvement in the revenue, profitability and long-term trajectory of our company.

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

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

Thank you, Owen. Now I'll review our Q2 2021 results.

For additional details, please see the Q2 2021 Investor Presentation available on our IR website.

Group revenues were within the range of our outlook at 56.0 Bn yen, down 13% year-over-year on an as-reported basis and down 21% year-over-year on a constant currency basis.

The Kingdom of the Winds: Yeon exceeded our expectations, which was offset by the lower-than-expected performance of MapleStory in Korea. As a result, revenues were within the range of our outlook.

Looking at the total company performance by platforms, both PC and mobile revenues were in the range of our outlook.

Operating income was 15.4 Bn yen which was in the range of our outlook, while costs including marketing costs, HR costs, and outsourcing costs were slightly lower than the plan.

Net income was 9.0 Bn yen, which was slightly below our outlook.

While we recognized a revaluation gain from fund investments and dividend income as finance income, we recognized a revaluation loss of 4.5 Bn yen due to movements in the market price of bitcoin.

As for bitcoin, we recognize it as an intangible asset in our balance sheet under IFRS.

Bitcoin will be reevaluated according to the market price at the end of each quarter. Gain or loss from the revaluation will be recognized up to the purchase price after the Operating Income line.

On the other hand, reevaluation gain which is recognized above the purchase price will be recorded as other comprehensive income in the consolidated comprehensive income statement.

Let's move on to results by region.

Revenues from our Korea business were in the range of our outlook as the stronger-than-expected performance of *The Kingdom of the Winds:* Yeon was offset by the lower-than-

expected performance of *MapleStory*.

On a year-over-year basis, revenues were flat on an as-reported basis and decreased by 10% on a constant currency basis.

Regarding *MapleStory*, we responded quickly to feedback we received in February regarding probability-based items. We took several steps to address player concerns including compensation, probability disclosures on paid probability-based items, and engagement with players.

As a result, the number of active users -- which had dropped sequentially since February -- started to stabilize in late April, then picked up in late June driven by the Summer update introduced on June 17th.

However, revenue came in below our outlook due to lower-than-expected spending by players.

We are still working on regaining our players' trust, and will continue to focus on making our games better by introducing a probability monitoring system and incorporating player feedback to improve the game experience.

Moving to FIFA ONLINE 4, PC and mobile combined revenues grew year-over-year due to well-received sales promotions.

Sudden Attack maintained its momentum and grew revenue by 136% year-over-year, while *Dungeon&Fighter's* revenue decreased.

Consequently, PC revenues in Korea decreased by 7% year-over-year.

As for the mobile business, *The Kingdom of the Winds: Yeon* outperformed driven by a well-received update and successful item sales targeting new and returning users.

On a year-over-year basis, mobile revenues increased by 14% primarily driven by a contribution from *The Kingdom of the Winds: Yeon* and growth in *FIFA ONLINE 4 M*, partially offset by revenue decreases in *V4* and *KartRider Rush+*.

Revenues from our China business were slightly below our outlook. On a year-over-year basis, revenues decreased by 30% on an as-reported basis and by 37% on a constant currency

basis.

Excluding the impact of 2.3 Bn yen one-off royalty income adjustment recognized in the year-ago quarter, revenues decreased by 20% year-over-year on an as-reported basis and by 28% year-over-year on a constant currency basis.

Dungeon&Fighter's revenue was at the low end of our outlook.

In this second Quarter, we tried to maintain user metrics through the Labor Day update in April and other events to address the drop in user metrics continuing from last quarter. However, active users and paying users continued to decrease until we introduced the 13th Anniversary update on June 17th.

While we saw a small rebound in active and paying users following the 13th Anniversary update and a successful promotion aimed at bringing back users, both active and paying users decreased in Q2 sequentially and year-over-year.

ARPPU and revenue decreased sequentially due to seasonality.

On a year-over-year basis, while ARPPU increased due to a decline in the portion of light users, revenue decreased year-over-year due to a decrease in the number of paying users.

Revenues from Japan decreased by 22% year-over-year due to revenue decreases from *TRAHA* and *MapleStory M*, which more than offset contributions from *V4*, *FIFA MOBILE* and *Blue Archive*.

Revenues from North America and Europe decreased by 13% due to *Choices*' revenue decrease despite the year-over-year growth of *MapleStory* and *MapleStory M*

Despite revenue increases from *MapleStory* and *MapleStory M*, revenues from Rest of World decreased by 29% due to revenue decreases from *KartRider Rush+* and *V4*.

Moving on to our FY2021 third quarter outlook.

Q3 2021 is faced with a challenging year-over-year comparison given the record-breaking Q3 revenues and operating income we achieved in 2020.

As a reminder, in Q3 2020, revenues from our major PC titles including *MapleStory* increased

and our mobile business grew 140% year-over-year driven by contributions from *V4*, *KartRider Rush+* as well as *The Kingdom of the Winds: Yeon* which launched in Q3 2020.

Given this tough comparison, we expect our overall group revenues to decrease year-over-year in Q3 2021.

We expect our Q3 group revenues in the range of 65.4 to 71.5 Bn yen, representing a 18% to 10% decrease year-over-year on an as-reported basis and a 24% to 17% decrease year-over-year on a constant currency basis.

We expect our Q3 operating income to be in the range of 20.1 to 25.3 Bn yen, representing a 27% to 8% decrease year-over-year on an as-reported basis and a 35% to 18% decrease 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 15.0 to 18.9 Bn yen, representing a 8% decrease to 16% increase year-over-year on an as-reported basis and a 19% decrease to 3% increase year-over-year on a constant currency basis.

Last year in Korea, on a constant currency basis we achieved 115% year-over-year growth primarily driven by the strong performance of *MapleStory* and a contribution from *The Kingdom of the Winds: Yeon*. Given that challenging comparison, we expect revenues from our Korea business to be down this year. We are looking for revenue to be in the range of 34.5 to 36.8 Bn yen, representing a 32% to 27% decrease year-over-year on an as-reported basis and a 37% to 32% decrease year-over-year on a constant currency basis.

As for the PC business, we expect *Sudden Attack* to maintain its strong momentum and to grow approximately 2.8 times year-over-year. We also expect *FIFA ONLINE 4* to grow. However, we expect *Dungeon&Fighter's* revenue to be roughly flat year-over-year on a constant currency basis.

As for *MapleStory*, the number of active users is trending lower than last year, and we are focusing on regaining trust of our users rather than focusing on the monetization of the game in the short-term. Therefore, we expect its revenue to decrease compared to Q3 2020 when it grew by 71% year-over-year on a constant currency basis.

While we anticipate growth from *Sudden Attack* and *FIFA ONLINE 4*, we expect this to be more than offset by the decline in *MapleStory*. As a result, we expect PC revenues in Korea to decrease year-over-year.

Regarding the mobile business in Korea, we expect revenues to decrease year-over-year. While we expect to benefit from *KonoSuba*, which is scheduled to launch on August 19, and anticipate growth from *MapleStory M*. However we expect these to be more than offset by revenue decreases in *The Kingdom of the Winds: Yeon, V4* and *KartRider Rush+*, all of which had strong performances in Q3 2020 following their recent launches.

Turning to China, we anticipate *Dungeon&Fighter's* revenue to increase year-over-year. Accordingly, we expect revenues from our China business to be in the range of 19.4 to 22.1 Bn yen, representing a 23% to 40% increase year-over-year on an as-reported basis and a 11% to 27% increase year-over-year on a constant currency basis.

As for *Dungeon&Fighter*, we introduced the Summer update on July 8th. This update includes introduction of a new job for a popular character, as well as avatar package offerings, events and new dungeons.

And as usual, we will release the National Day update in September.

The Summer update was well-received by users. The number of active users and paying users increased following the 13th Anniversary update introduced on June 17th, and has remained solid.

Accordingly, current MAUs and paying users in July have increased since Q2 2021. Year-over-year, MAUs are at a lower level while paying users increased.

Revenue in July increased compared to July 2020 driven by the increase in paying users.

We still need more time to carefully assess whether the current positive trend will continue, but we will try to maintain the momentum.

As for Mobile *Dungeon&Fighter*, it is not included in our Q3 outlook.

In Japan, we expect revenues in the range of 2.2 to 2.6 Bn yen, representing a 14% to 2% decrease year-over-year on an as-reported basis and a 17% to 5% decrease year-over-year on a constant currency basis. We anticipate contributions from *Blue Archive* and *FIFA MOBILE* to be more than offset by decreases from *TRAHA* and *MapleStory M*.

In North America and Europe, we expect revenues to be in the range of 4.0 to 4.4 Bn yen,

representing a 27% to 20% decrease year-over-year on an as-reported basis and a 30% to 23% decrease year-over-year on a constant currency basis, primarily due to decreases in revenues from *Choices* and *V4*.

We expect revenues in the Rest of World in the range of 5.2 to 5.5 Bn yen, representing a 4% to 11% increase year-over-year on an as-reported basis and a 3% decrease to 3% increase year-over-year on a constant currency basis. While we anticipate a contribution from *KonoSuba*, which is scheduled to launch on August 19, as well as growth from *MapleStory* and *MapleStory M*, we expect these to be offset by decreases from *KartRider Rush+* and *V4*.

In Q3 2021, we expect operating income to be in the range of 20.1 to 25.3 Bn yen, representing a year-over-year decrease of 27% to 8%.

Unfavorable factors compared to Q3 2020 regarding the operating income include:

First, a decrease in revenue.

Second, increased stock options costs and HR costs associated with the introduction of our new compensation policy in Korea.

Favorable factors compared to Q3 2020 include decreased variable costs associated with revenue decrease.

Other favorable factors include a decreased impairment loss of 3.0 Bn yen recorded in Q3 2020, which will not be repeated in Q3 2021.

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

Overall, we see Q2 and Q3 2021 as a transitional period for making improvements to our key titles, such as *Dungeon&Fighter* in China and *MapleStory* in Korea, to ensure our long-term growth.

As we've explained before, online games grow in a steady but non-linear pattern with slow or even declining periods followed by rapid growth if we operate well from the long-term perspective.

I referred to *MapleStory* and *Dungeon&Fighter* as an example, but if you look at page 18 of the investor deck, the same trajectory can be seen in *Sudden Attack*.

In this way, online games can evolve over the long-term by conducting proper updates and careful daily operations.

We are not only pursuing short-term quarterly revenues and profits, but also operating our games with a long-term perspective. The measures we have taken on our two major titles will surely contribute to our long-term success and bring us great returns.

Last week we showcased a number of new games in our development pipeline. In addition to highly-anticipated games such as *Mobile Dungeon&Fighter*, *KartRider: Drift* and a new title from Embark, we expect these titles to make a significant contribution to our revenue base and to drive a step-function increase in our earnings power.

Lastly, I would like to give you an update on the shareholder return and capital allocation strategy.

Based on our 2021 shareholder return plan, the Board of Directors today approved the payment of a divided of 2.5 yen per share for the interim period to the shareholders on the shareholder registry as of June 30th, 2020.

We are scheduled to pay the same dividend per share for the year end of FY2021.

Regarding our three-year 100Bn yen share repurchase policy that we announced on November 10, 2020, we have not yet executed on this buyback. We will consider several factors including investment opportunities, financial condition as well as the share price until the current plan ends in November 2023.

As to our investments in global entertainment companies, we have invested 117.8 Bn yen, which accounted for 72% of the 1.5 Bn dollars that the Board of Directors authorized and recorded an unrealized gain of 27.6 Bn yen under other comprehensive income as of Q2.

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 begin QA, let me anticipate one of your questions: When will the first game from Embark and *KartRider: Drift* be released?

I have two answers:

The first is, if you absolutely had to put something in your model, put it in the second half of next year. It could certainly be sooner.

But here's the real answer: It will depend on when our developers feel they have an outstanding game that they are proud to show to their closest friends. Getting there is all about iteration, play-testing and polishing. And any game company that is experienced and who is being honest with you will tell you this is not a linear process. Iteration is about making the game fun, and that is an art challenge, not an engineering challenge.

So, we could give you a date. That would satisfy your near-term need to plug something in to your model. And it would generate near-term excitement from users.

But then it would put the WRONG type of pressure on the game developers. They would have to hit a date regardless of what is right for making the game fun. In our industry that's called Crunch mode, which is industry parlance for "put a game out by a certain deadline, no matter what the costs on the employees." Even after crunch mode the game is often still not ready to launch. The result of all this is frequently disappointed customers, burnt-out, demoralized developers, and damaged brands and impaired financial returns for investors.

Crunch mode is one of the most pernicious problems in our industry. The charade of launch timing serves little purpose except this dance with equity analysts.

Instead, the right thing to focus and push for is a game that blows people's minds. If we achieve that, the game will last many years and the revenues will dwarf what we would have made by launching a quarter or two earlier.

I'm sorry nobody in my industry has explained this to you before. Within the industry, we ALL know it's true and yet few talk about it openly. Everyone should.

So rather than giving you a date, this team is going to give to our customers and employees a commitment to make the best game we can, as soon as we can.

None of this is to imply we are pushing back the date for any of our games, or that we are experiencing delays. It is only to let you know as fully as we can how we make our decisions on product launches. If your primary job is to fill in your Excel model, you'll hate our approach. But if you consider your job definition to be making money by identifying mis-priced assets in the entertainment industry, we think you'll find our way a lot more lucrative.

With that, operator, we are ready to take questions.