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CORPORATE PARTICIPANTS

Seungwoo Choi *NEXON Co., Ltd. - CEO, President*

Owen Mahoney *NEXON Co., Ltd. - CFO*

Hanako Muto *NEXON Co., Ltd. - Head of Corporate Communications*

CONFERENCE CALL PARTICIPANTS

Atul Bagga *Lazard Capital - Analyst*

Mark Moore *Brookside Capital - Analyst*

Mia Nagasaka *Morgan Stanley - Analyst*

PRESENTATION

Hanako Muto - *NEXON Co., Ltd. - Head of Corporate Communications*

Hello, everyone, and welcome to Nexon's Second Quarter Financial Results Q&A session. With me today are Seungwoo Choi, CEO and President of Nexon, and Owen Mahoney, CFO.

Before we get started, I'd like to remind you that 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 technologies, and address new technical challenges, use of intellectual property, and other statements that are not historic facts.

These statements represent our predictions and expectations as to 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 release. We assume no obligation to revise or update any forward-looking statements.

Our financial results for Q2, as well as our quarterly letter to shareholders from Seungwoo and Owen, are available on the Company's investor relations website at <http://ir.nexon.co.jp/>. A replay of this Q&A session will be available following this call. I'd now like to turn the call over to Seungwoo and Owen for a brief introduction, and then we will begin our Q&A session.

Seungwoo Choi - *NEXON Co., Ltd. - CEO, President*

Thank you very much, Muto san. Welcome, everyone, to our second quarter 2012 financial results call. As most of you know, each quarter we post a shareholder letter on our website, along with our financial results. Beginning this quarter, we will also be summarizing the key financial information in a press release issued in Japanese, Korean, and English.

The intent of the shareholder letter is to give investors detail on the Company's performance and outlook in commentary from the management team that you can read at your convenience. The letter is followed by this hosted Q&A call, which offers you the opportunity to ask questions and hear from us directly.

Prior to starting the Q&A session, I would like to provide a few comments on our second quarter results and where the business is today. First of all, I'm very pleased with our second quarter results. We met our expectations for both revenue and operating income, driven by growth in our existing games, which continue to perform well. Our revenues grew 12% over the second quarter of 2011. On a constant currency basis, that is, taking out the effects of the exchange rates fluctuations, this growth was 20%, year over year.



Our operating income grew 24%, and net income grew 32%. On a constant currency basis, our operating income grew 34%, and net income grew by an impressive 45%. The major driver of these results, as we have talked about on previous calls, is that our large existing titles continued to grow, fueled by our new -- fueled by our ongoing large development efforts and a very large and very loyal base of players.

In addition to the continued growth from our existing titles, our newer free-to-play titles, such as Mabinogi Heroes and Cyphers, are demonstrating the kind of growth we hope to see from recently launched games and have the potential to join the ranks of our largest game franchises.

Meanwhile, we continue to create and innovate. Our development teams have been hard at work ramping up for the launches of several new free-to-play games in the second half of the year. These include Counter-Strike Online 2, Epic of the Three Kingdoms, and Mabinogi 2.

We're very excited for these launches, which we think will break new creative ground through significant innovations in game play that people will love. As with all of our new launches, we'll watch their performance closely to ensure they are following the same growth trajectory that our major existing titles did when they first launched.

Another key development which we announced after the close of the quarter is our partnership with EA to publish FIFA Online 3 in Korea, set to launch next year. We're thrilled to be working with the world's premier sports franchise, as well as one of the biggest online franchises in Korea.

Overall, it's as clear to us as ever that the internet is transforming today's video game market, as it did with other industries. If anything, the pace of this transformation is accelerating. Last decade, we saw consumer media industries, like music and books, transition from offline to online and build compelling business models, which continue to generate strong returns for shareholders.

This shift is clearly occurring in video games. We believe free-to-play is the business model that is unlocking the iconic value of the internet for games. Nexon is strongly positioned to capitalize on this transformation, as evidenced by our expectations to deliver 22% revenue growth on a constant currency basis, year over year, coupled with operating margins of 45%.

I'll now ask our CFO, Owen Mahoney, to provide some additional detail on the quarter and our outlook for the year.

Owen Mahoney - NEXON Co., Ltd. - CFO

Thanks, Seungwoo. Let me provide some additional detail on the quarter, and then we'll take your questions. First, revenue, operating income, and net income all showed strong growth for the quarter. As Seungwoo mentioned, revenue was up 12% to JPY22.8 billion. On a constant currency basis, our revenue growth was 20%.

Operating income was JPY10.6 billion, an increase of 24% on an as reported basis and 34% on a constant currency basis, and net income was JPY6.7 billion, an increase of 32%, or 45% on a constant currency basis.

We ended the quarter with JPY129 billion in cash. The growth this quarter represents continued growth across a wide range of our existing titles, where we continue to reach new MCCU records for Dungeon Fighter, as well as the growing contributions from some of our newer titles in the robust Chinese market.

Second, we've had a very active quarter on the strategic front. Prior to the FIFA Online 3 announcement that Seungwoo mentioned, during Q2, we announced that we'd become the largest shareholder of NCsoft, with a 14.7% ownership state. We also announced our acquisition of mobile games developer, inBlue Inc, to further accelerate our efforts on the mobile front.

I should also note that we recently announced that we raised JPY50 billion in debt financing at a very favorable rate, which gives us additional strategic flexibility in this very fast moving market.

Finally, we slightly lowered our outlook for the full year 2012 in giving an outlook for Q3. Our revenue guidance for the full year is now JPY104.3 billion, representing a 19% increase over 2011. On a constant currency basis, again, if the currency did not fluctuate, that would be a 22% increase.

As we mentioned in the letter, our outlook reflects our internal plan, which is based on a rigorous bottoms-up review of our titles by region and multiple planning scenarios for MAUs, pay rates, and ARPPU.

We're currently in the very dynamic summer months, in which we are introducing content updates to several of our major games around the world. While our titles are delivering solid results in revenue and operating metrics, based on very early indications in July, we believe that a small downward revision in our full year outlook is prudent.

As Seungwoo mentioned, we're very happy with our results in Q2, and we believe the Company and our model are in great shape, well positioned for what we think will be a very exciting period of growth in our industry and for our Company. With that, we'd like to open it up to the Q&A session.

Some of you have sent us questions, so we'll start going down that list, and then we'll open it up to live Q&A after that. Let's begin with the first question.

QUESTIONS AND ANSWERS

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. The first few questions are about guidance. What is your reason behind the downward revision for the full year?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. So, this is Owen. As we talked about in our prepared remarks, there was really several things at work here. I note that we just -- we tweaked our revenue number down slightly by 3.7% to just over JPY104 billion. So it's not a major change; it's a minor change. We're looking at very early results from July, and -- around the world, and we felt that -- we had, frankly, debated internally about it.

We thought long and hard about not changing our guidance, and we decided that it was best to move the guidance down slightly, because that's what our internal plan shows. I would not say it's any surprise -- any major surprises or issues of any particular games or any particular regions. We're just looking at the early number across the board. I'd emphasize that it's early in the quarter, however, and so, it's early in the quarter and early in the second half of the year. So it's very early today.

One other thing just to note on this. Under TSE rules, we're required to provide a number for revenue, operating income, and net income and not a range. If we were providing a range or had we been in the position to provide a range, our range would not have changed.

So this is certainly within the ranges of what we thought was the appropriate case, but given that we are required to provide a number and given our commitment to have all shareholders understand exactly how we're thinking about the quarter, we thought it was prudent and best to communicate that we're tweaking our numbers down.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Okay. Next question.

Owen Mahoney - NEXON Co., Ltd. - CFO

Next question, please.



Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. Is it correct to understand that growth in China and Korea are part of this reason?

Owen Mahoney - NEXON Co., Ltd. - CFO

Well, what I'd say overall is we continue to be a -- in a very strong position in Korea and in China. It looks like we're continuing to take share from companies in -- from other companies in Korea, so we're happy about our performance there. I'd note that in Q2, we were up 9% on a constant currency basis in Korea.

And also, in China, we continue to see it as a very robust market. So -- now the growth rate that we experienced in Q2 is lower than we experienced in Q1, but that was exactly as we expected, which is why we made our number. And so -- but overall, yes, China and Korea both contribute a large portion of our revenue so that's part of the reason.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. Why would you make a downward revision at this timing? Is the reason temporary, or is it something that we need to be taking into consideration going forward?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. So, we're making it a downward revision at this time, because, again, we think that the appropriate way to communicate with our shareholders is very openly and to provide you the information that we're seeing when we see it. Again, we'd looked at our numbers that are coming in very, very early in the second half. We saw that it was a little bit less robust than we had expected, and so we decided to tweak the numbers down, and we have an earnings call today, so we wanted to communicate that outward. And again, it's within the range of what we expected. Next question.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. How should we think about China revenues growth in Q3?

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

This is Seungwoo. As Owen mentioned, despite general sentiment, we foresee a strong robust and dynamic market in China. We continue to see opportunities there because of increasing broadband penetration; also increasing PC penetration, as well as strong GDP growth. And China market is resonating very well with our games, and we like what we see there, and we continue to be very bullish on China. Next question, please.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. Why would your quarter fluctuate so much? Are there issues that need to be addressed in the way you forecast, or are there some kind of a mechanism that we don't understand?

Owen Mahoney - NEXON Co., Ltd. - CFO

If the question is about quarter over quarter changes, I'd say that the quarter over quarter -- we expect fluctuations. That's a core part of our business. Q1 and Q3 are typically the strongest quarters because of the seasonality, and Q2 and Q4 are typically lighter quarters, all other things being equal.



Of course, there's several other factors that drive into this. The other two big ones are the timing of content updates of our biggest games and, related to that, how well those content updates resonate with users. And then, the second -- meaning how well they're done.

And then, the second component of that is timing of new content or new introductions and new launches. We're coming out of a period that changes the numbers somewhat from what a standard seasonality would be. In Q1, we had extraordinary -- our content resonated extraordinarily well with our customers, particularly in China, and so, we had bigger than expected performance. That sometimes happens.

And then, in the tail end of this year, the back end of Q3 and then, into Q4, we have several product introductions of major new product launches that we have. So that's basically how the fluctuations work. Those are the main parts to know about how, certainly, we forecast our business and how we would recommend people think about our business.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

You say you experienced a solid quarter. Having said that, it's lower than consensus. Please comment.

Owen Mahoney - NEXON Co., Ltd. - CFO

Well, let me be clear. We made our number for the quarter. We forecasted the number for the quarter of JPY22.8 billion. We made our revenue number and our operating income number, so we're very proud of that. That puts us on a growth trajectory for the year of 24% -- excuse me -- 22% on a constant currency basis. That's right in line with our organic growth rate. So we feel extraordinarily happy with that.

As for what consensus is and what analysts had us at, I can't speak for that. All we can do is communicate as clearly and as detailed as we possibly can about both our number and our forecasting and also, how we come to that forecasting. And I would reiterate something that we said in past calls that our internal number is our external number. In other words, our guidance is exactly what we have internally as a number. So it reflects our best thinking, and we have a detailed model that helps us come to those numbers.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

What is the main reason for the 29% sequential decline in China revenues in Q2?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. This is Owen again. Again, the key way to think about our business, first of all, is through seasonality, and seasonality is the first big factor. So Q2 is -- as far back as many years, is down from Q1. That's always how it works. So you're going to see sequential decline in Q2 very naturally.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

We know you mentioned Q2 would not be strong, due to seasonality, but the numbers do not look good year on year. Year on year sales have slowed down across all regions compared to Q1. Please explain what happened in each region.

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. So, first of all, our numbers for Q2, again, would be -- were exactly what we expected, so this is what we communicated last quarter. We were right on top of our numbers. And, as I mentioned, there's three sort of key factors. One is seasonality, as the questioner mentioned. The second is content updates of existing games, and the third is content updates -- or is introduction of new games.

And so, as we plan out the year, we know that some quarters are going to be stronger than others as a factor of seasonality, of content updates of existing games, and launch of new games, and so that's why we came in at what we expected. We looked at the content launch update plan that we did for existing games. That typically drives higher revenues, and it's a lighter quarter for that, and in upcoming quarters, we have heavier content updates scheduled. And then, in this year, we've got a fairly heavy launch cycle of new games, especially loaded in end of Q3 and Q4.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

With the assumption of MAU and ARPPUs in your expectations, do you think the trend will continue in Q3? Can you provide us more color in each region?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. We look at three numbers when we're looking at our financials, very closely, on both a per game basis as well as on a regional basis, and then, of course, finally, on a worldwide basis. Just to reiterate the numbers, MAUs went from 83.1 million a year ago to 77.4 million this year in Q2. Pay rate increased significantly from 7.8% to 10.3%. That is 10.3% of our 77.4 million monthly active users' purchased items in the games. And ARPPU was essentially flat. It went from JPY1,538 to JPY1,521. And so, again, we -- some companies focus on one of those numbers. We actually focus on all three. We think they're all very important.

As we've looked at MAU, what really drives large MAU growth is the launch of new games, and we haven't had a significant launch of a major new game in the last several quarters, so this was certainly within the range of our expectations. Pay rates were up what we consider a pretty substantial amount, and ARPPUs were flat, so, as we look at the combination of all three, this was -- this actually was right in our model.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Please comment on how Dungeon&Fighter is doing in China. Any comments on the trends of MAU and pay rates?

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Again, we do not break it up by region or by title, but I can say D&F has achieved a new record for MCCU's maximum concurrent user numbers in Q2, and once again, it appears to be item number one and number two in terms of revenue in China, and we're very happy to see this kind of trend and hope it will continue. Next question, please.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Yes. Are the new titles expected to launch in Q3 and Q4 still on schedule? How much positive impact can you possibly see on MAU and ARPPU?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. So I'll take both of those in turn. So let's think about our new product pipeline for a second. The three titles that are launching towards the end of the year that are our major titles -- we've got a large slate of upcoming titles, but three that are our big ones that we're focused on are Epic of the Kingdoms 3D. This is a massively multiplayer online role playing game. It's built on the Unity 3D platform. That means it'll be available both on PC and on tablet and mobile.

So we're very excited about that game. It's created by the same team that created Atlantica. It's a very high quality studio, and it's going to be very unique in the fact that it'll launched on multiple platforms.

The second big one is Counter-Strike Online 2, which we co-developed with Valve, a very high quality developer based in the United States. And it's a sequel to our hit first person shooter Counter-Strike Online, and we're launching into closed beta in Q3 in Korea and then, elsewhere after that.

The third major one is what's currently being called Mabinogi 2, and this is a game that's based off of the Mabinogi back story in fiction, but is in a very different game world and with a very different game play characteristic. So that's the third big one.

After that -- so those are the remaining major titles for 2012, and then, when we start to go forward and think about 2013, we have several additional ones in 2013, which include FIFA Online 3, which we just announced. We'll be launching that in Korea. We'll be launching a game at the very end of Q4 called Warface with Crytek, but the bulk of that start will happen in the beginning of 2013. This is a first person shooter game that is developed by a very high quality developer, again, in Germany, called Crytek.

And then, the next one coming up is -- we'll be launching the 2K Baseball Online franchise that we've -- that we're working on with Take-Two. So we think that that leads to a robust new product pipeline that we're very excited about.

The second part of the question, I think, was about performance. Yes. So, we haven't provided guidance on what the impact on MAU and ARPPU is, but when you think briefly about how MAUs and ARPPUs work, our games work, as we've said before -- they work sort of differently. They launch differently than the traditional video games business. In the traditional video games business, you make, typically, 90% of your revenue in the first one to two quarters after launch, and our business works differently.

What happens is, as a game gets launched into the market, a community develops around it, and that starts to drive up -- and as that community develops, of course, you see that -- those numbers in MAUs. And then, people start buying items within the games, and typically, they buy fewer items early on than they buy over time, and that ultimately is why you see growth in games.

If you're properly supporting a game over a period of time -- an immersive game, then it will generate revenues that increase over time, and we said before that our games have a really solid track record of going -- growing year after year after year. That's happened with all of our top eight titles. If we're doing our job well, as we introduce these games, that same thing will happen.

Now, when we do our forecasting, we factor in not heavy launch of new games. It doesn't make a huge impact on our P&L in the first few quarters after launch, but if we're successful, those games resonate with customers, and you see the impact in the revenue; over time, it goes up.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

How much revenue are you expecting from FIFA Online 3? Can you give us details on the contents of the contract? Are you expecting to launch in countries beside Korea?

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Okay, I'll take this one. FIFA Online 3 will be launched, I believe, in 2013, and we have not given guidance on 2013. But I can say we're very happy to work with EA -- with one of the greatest sports franchises. And for now, the announcement is only for Korea, and we cannot disclose the contract details, but our intention is to take FIFA Online franchise to an entirely new height, at least, in Korea. Next question, please.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

On your financing made at the end of July, you've made a loan from SMBC with collateral. Can you let us know what securities you have put up as collateral?



Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. This is Owen. We haven't disclosed the details of that relationship, but what I can tell you is we were able to complete in very favorable terms. So we're very, very happy with that relationship, and we will be disclosing additional information, as required, in due course.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Can you discuss progress on your mobile strategy? Can you provide revenue trends of game titles provided through your mobile platform?

Owen Mahoney - NEXON Co., Ltd. - CFO

So, first of all, we've been -- there's a couple different components about our mobile strategy. We've introduced several new titles during the course of the quarter; actually, 13 on mobile. We're happy with our progress so far. Those titles have been both launched in Korea, to start with, and in Japan. I'd say it's early days. A lot of those launched towards the tail end of the quarter. During Q3, we plan to launch ten more titles.

But one that's a standout within the titles that we recently launched is KartRider Rush Plus, which is a sequel to the KartRider Rush game that we launched previously -- or, last year on mobile. Kart -- the original KartRider Rush generated 10.5 million downloads, and KartRider Rush was introduced on June 29, and so far, it's generated 10.5 million downloads. So we think we're off to a pretty good start there, so we're happy with how that started, and we hope to see additional success from other mobile titles that we launch.

We're moving aggressively in mobile, particularly in Japan. We think Japan is a market where mobile is very important. We have acquired a very high quality developer in inBlue in Japan. It's a small developer, but they're very -- they're known for very high quality games. We think it's a good start, and we plan to continue to be aggressive about development on the mobile platforms.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

What tangible synergies can we expect to see from your strategic initiatives you made this quarter?

Owen Mahoney - NEXON Co., Ltd. - CFO

Sure. So, we've -- to recap, we've made three major announcements. One was the acquisition of inBlue, which I just mentioned. Second is the investment in NCsoft. We purchased 14.7%. And then, we announced, with FIFA Online, agreement that we did with Electronic Arts. We're very happy with all three of those. FIFA Online you'll see in the impact in our FY '13 numbers, which we have not announced yet, but we think it really helps our portfolio in Korea. We're very excited about that.

In NCsoft, we've talked about it before. We have not announced any specific plans on that, but we're in active dialogs with that team. And so -- and then, on inBlue, it's a small developer, but they've got an outstanding pipeline, and so, we're very excited about how that works -- or how that agreement enhances our development capabilities for mobile, and particularly, in Japanese mobile. So we factored that into our internal forecast for FY'12, and we're building that into how we think about 2013, but we haven't split that out.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Explain in more detail the commercial strategy you plan to have with NCsoft post the stake ownership.

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Okay. Owen has already mentioned very briefly about this. Well, as the majority shareholder of NCsoft, I think this transaction brings together NCsoft's strong pipeline of compelling IPs and Nexon's leading international publishing platform and free-to-play expertise.

We hope this investment forms a basis for a long-term partnership, especially future commercial opportunities, allowing both NCsoft and Nexon to leverage our respective strengths. We do have active discussions going on, but we do not have any details to announce yet. We will certainly update you as soon as we have the details ready.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Do you have any interest to invest in minority stake in any Western game companies?

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Of course. We are open to any kind of opportunities, as long as they meet our objectives. I would say our objectives are to secure good content or good development teams or to deploy our games in new territories or to have access to new platforms. So, if the Western company can provide us with good IPs or allow us to access the territories or new platforms, we'll certainly be interested. And, as I said, not just to Western game companies; we'll be open to any kind of opportunities that are out there.

Hanako Muto - NEXON Co., Ltd. - Head of Corporate Communications

Any change in your view and strategy in North America and Europe?

Owen Mahoney - NEXON Co., Ltd. - CFO

I think no on both. So, a couple things, just on North America. First of all, we talked last quarter about coming out a challenging period in North America, where we had, in Q4, and then, into Q1, the results of a pretty significant hacking challenge. We feel pretty strongly that we've seen our -- a lot more stability in our servers and in our position in North America, so we're very happy about the progress we've made there. It's -- we have to continue to be very vigilant, but we feel like we've really turned the corner there. We've got a very strong technical team in place. They've done a great job, and we continue to believe that North America is an extraordinarily important place to be investing.

New markets take time; we expect it to, and therefore, we think it's well worth our time and effort to invest, in part, because North America is a market that is starting to, frankly, catch up to the rest of the world, in terms of broadband speeds -- or, at least, catch up to Asia. We've -- I think we've mentioned this before, but broadband speeds around Asia are just very, very much faster than they are in North America and at cheaper rates. So that helps our business, because we're benefited by broadband speeds.

And then, clearly, free-to-play is something that the North American gamers are starting to see a lot more of, and that means that they're more amenable and open to playing free-to-play games. They understand it better. The consumptions of -- or, the consumption patterns are well understood. So, now that we've got our back end in much better position than it was a quarter or two ago, we've trimmed back the marketing funnel, and we feel like we're in better shape there.

As for Europe, Europe's a bucket that -- or, is in a bucket that we report as -- that includes Southeast Asia and South America and several others. Europe itself, within that, grew 6% on an as reported basis and 20% on a constant currency basis. That's slower growth than we've had in previous quarters, but there again, we think that broadband is really speeding up in Europe and is available -- and therefore, really supports our business model.



The same sort of general trends that we see in North America, we see in Europe, and therefore, it's well worth our time and effort. We plan to continue investing in those markets, and so, there's no change in our strategy. So we plan to keep working there.

I think that's the end of our questions. And with that, we'd like to open it up to questions and answer -- the question and answer session. So we would invite -- operator, if you could invite the folks to join the call and ask any additional questions they might have, that would be great.

Operator

Certainly, sir. (Operator Instructions).

Atul Bagga, Lazard Capital.

Atul Bagga - Lazard Capital - Analyst

Hey, you guys, thanks for taking my question. Just quick question on high level -- is there any shift or any change in your views about free-to-play business model versus subscription based business models, especially as it relates to your change of outlook for the year and your investment in NCsoft? Thank you.

Owen Mahoney - NEXON Co., Ltd. - CFO

Hey, Atul, this is Owen. I'll take that question. No, we don't have any view -- change of view whatsoever, relative to free-to-play. We think free-to-play -- again, we think that there's two shifts going on in the world for games, overall. One is the shift from offline to online is exorable, and it's clearly happening. We've seen it happen in Korea and China and elsewhere around Asia, and it's clearly coming to North America.

The second thing is -- and within that, we think free-to-play is the business model that fundamentally unlocks the economic value of online, and our business -- again, we're running a business that's growing at 22%, organically alone. That's exactly within line with our history. That's in line with our long-term plan, and it's running at a 45% operating income margin level, which is the high end of our internal plans. So we think that's pretty definitionally a great business.

And so, we like it a lot, and it's built entirely on free-to-play. We -- all of our games are based off of free-to-play, and we think there's opportunities to make more games -- more high quality games free-to-play and that they benefit from that, if it's done well -- if it's executed well.

So, when we think about NC, we think there's opportunity there, and that was one of the impetuses for our investment in NC. One of the other major impetuses in our investment in NC is that we think that NC is led by one of the top creative teams in the entire business, with an IP bench that that team has created that is among the very best in our industry.

We just have enormous respect for their development teams in the creative leadership there, so we think that combination is really exciting for us. And so, it doesn't -- but it doesn't change a bit about how we think about where free-to-play fits in the world.

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

It will not change, because this is the best model to users as well. Why? Because the game is free, and you can play the game for free, and we believe this will be the dominant model in the global games market in the future.

Atul Bagga - Lazard Capital - Analyst

Very helpful. Thank you, guys.



Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Thanks, Atul.

Owen Mahoney - NEXON Co., Ltd. - CFO

Thank you. Operator, next question, please.

Operator

Yes, sir. Mark Moore, Brookside Capital.

Mark Moore - Brookside Capital - Analyst

Hey, guys. How's it going? Just, I guess, two quick questions. The first one is regarding Japan, specifically, which I know is a -- has a bit of a smaller market. But is there -- we're kind of wondering about the year on year growth rate that happened in Q2 in Japan and, sort of, what is cooking in that market. And if you've mentioned something, I apologize. I was about five minutes late getting on the line. And then, I want to ask you a second question about guidance, but let me first ask you about Japan here.

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Okay, I'll take the first question about Japan. Japan has been a traditionally huge game market, but mainly on console. Japan never had a good PC game market. We see a lot of growth coming from the mobile platform these days. I think this has something to do with the life of Japanese; also, the game playing habits. But what we see is that the market -- the PC online game market is not growing as fast as we have expected, so a little bit of disappointment there, to be frank.

But we do see a lot of growth coming from the mobile platform, so we will focus more on the new platform in the future. I think one of the announcements we made was the acquisition of inBlue, and I think that's a very good starting point for us, and we hope to have greater opportunities in the future in Japan, on mobile platform, but we will continue to focus on expanding the PC online game market as well.

Mark Moore - Brookside Capital - Analyst

Yes, Seungwoo -- well, on that issue, just really quickly, the places where you see the most accentuated slowdowns here in Korea and in Japan happen to also be the places with the highest growth rate of -- sort of, of Smartphone going on. Is the underlying platform of PC starting to come under stress in these most developed markets, as the Smartphone proliferates, and folks have other -- are just spending less time in front of the PC?

Seungwoo Choi - NEXON Co., Ltd. - CEO, President

Well, I believe that mobile platform and PC are very different -- different usage, different purpose, and different type of content, different type of information. So, although a lot of growth is coming on mobile platform, I don't think that will weaken our position on the PC platform.



Owen Mahoney - NEXON Co., Ltd. - CFO

Yes, one of the things that I'd say, Mark, just on that, is, as Seungwoo said, the mobile platform works very differently. Lifestyles are different in Korea and Japan. You really have to separate out. Japan is a very different place for games. The lifestyle and how people access the internet is very, very different.

Relative to Korea, which you mentioned, I want to be clear on Korea. We don't give guidance by regions, but Korea was definitely within the range of what we expected during the quarter. And so --

Mark Moore - Brookside Capital - Analyst

Yes. No, my only thought was if you said you grew 9% constant currency, and you were beating the market, then, that means the market was growing somewhat slower, if you can actually discern the difference. You're probably talking about lower mid single digits. That's not very fast growth, frankly, in terms of revenue for that business. (inaudible) That's what sort of scares me.

Owen Mahoney - NEXON Co., Ltd. - CFO

Yes, I understand, Mark. We're not seeing it that way. Actually, we see Korea continues to be a strong market for us. We're growing in it, and the -- we don't see -- a lot of it depends on the schedule for content updates and the schedule for new game introductions.

Mark Moore - Brookside Capital - Analyst

Yes.

Owen Mahoney - NEXON Co., Ltd. - CFO

And that's just the way that the market works. So these are not constant forces. They operate in flux, and different markets are going to have different content update schedules -- or regions are going to have different content update schedules, and so, it was right in the range of what we expected to see this quarter.

Mark Moore - Brookside Capital - Analyst

I'm sure that's... Thanks Owen. Just one quick other question, just in terms of the -- what it is that you're seeing in terms of trends right now, and I don't want to pick this apart too much, but -- that makes you want to take the guidance down just a little bit. In terms of metrics, where is it happening? You actually have -- seem to have quite a good hold, in terms of paying penetration.

And so, is this -- is what's going on is that ARPPU is slipping, or is it that there is an accelerated sort of slowdown in terms of MAUs? Or what is it that's going on right now in the marketplace that you're seeing?

Owen Mahoney - NEXON Co., Ltd. - CFO

Yes. So, what we're just -- we're looking at just early numbers, in terms of revenue overall, and I'm not sure that we can discern a -- break out the trends by MAUs' conversion rate or ARPPU at this point. We just saw the overall aggregate number just a little lighter than we expected. And I want to emphasize again.

This is a tweak, and it's certainly within the range, and if we were giving ranges, we wouldn't change the range. But we're required to provide a number, and so, we are providing a number, and we want to -- and we've made the commitment again that we want to tell you what we're seeing.



I -- but I don't think that we can pull it apart and say we're seeing a trend in any one of these items that we can pull apart and say that what's affecting things, at this stage. And again, as I mentioned before, it's very early days. We thought about whether we should update or tweak the guidance at all. We thought that, on balance, it was the right thing to do, but it is too early to tell if there's a longer term trend there, Mark.

Mark Moore - *Brookside Capital - Analyst*

Is it -- was Q3 last year a particularly good quarter? I was just looking on sort of Q on Q numbers -- Q2 to Q3 of last year versus Q2 to Q3 of this year. Is there any reason to think that last year the guys did a lot of content updates or something was happening in Q3 of last year that made it a tougher comp for you?

Owen Mahoney - *NEXON Co., Ltd. - CFO*

No, I -- look -- one thing that didn't happen is we didn't have the Q over Q comp that we do this year, but I think you see the -- how Q1 is stronger, and Q3 tends to be stronger. So we didn't have that at work last year. But, really, what you've got is there's sort of three factors that create the wave in any given quarter.

Again, it's seasonality, it's content updates, and it's new product introduction, and I'd like to emphasize again. We made our numbers that we had for our plan, and we communicated those numbers as clearly as we possibly could. So we're happy with Q2. We think we're right on track to do exactly what we've been doing for years and what we intend to continue to do for years.

Mark Moore - *Brookside Capital - Analyst*

Okay, thanks, Owen.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Thank you. Next question, please.

Operator

Yes, sir. Mia Nagasaka, Morgan Stanley.

Mia Nagasaka - *Morgan Stanley - Analyst*

Oh, hi. This is Mia from Morgan Stanley. Thank you for your presentation.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Thank you, Mia.

Mia Nagasaka - *Morgan Stanley - Analyst*

I have three -- hi there. I have three questions. So, my first question is on the US market. Looking at all the social media earnings coming out for the last month, I realize that mobile shift is happening in the US. I understand that Nexon's business model is in the middle of the high core and the very casual on the social side. I was just wondering -- does the mobile shift really affect your business? What's your strategy?



And my second question is the European market. So, I understand that the European and others market was down by 28%, year on year, in the second quarter. I understand that the breakdown -- there's more than like ten countries in this section. Can you give us a little bit more color on major areas, which is categorized in the others?

And let me ask you the last question. I just wanted to confirm that your --

Owen Mahoney - NEXON Co., Ltd. - CFO

Mia? Hey, Mia?

Mia Nagasaka - Morgan Stanley - Analyst

Third quarter -- yes?

Owen Mahoney - NEXON Co., Ltd. - CFO

Can I interrupt you for one second? Can you hold off the last question for once, just so we can --

Mia Nagasaka - Morgan Stanley - Analyst

Okay. Sure.

Owen Mahoney - NEXON Co., Ltd. - CFO

Make sure to keep your questions straight.

Mia Nagasaka - Morgan Stanley - Analyst

Okay. Sure.

Owen Mahoney - NEXON Co., Ltd. - CFO

Okay. So, first of all, let's talk about the mobile shift in -- or the expanding mobile business in North America. Let me emphasize -- we -- the PC free-to-play games business, which is predicated on immersive games, that's the business that we've built our business on. It's a great business. We like it around the world.

Now, we're -- just going to mention that in some places, it's stronger than others. Japan -- there's never been, really, much of a PC market at all, because Japanese either tend not to play games on their PCs or even really use PCs as entertainment devices at all.

In places like North America, it's much stronger, where a third of the -- roughly, a third of the business, a little bit more, has been -- the games -- traditional games business has been on PC. If you add social in there, it's actually a little bit bigger than that now. We -- and one other just correction. We don't make casual games. We make immersive games that are divided -- designed to be played by a very broad audience for months or years on end.

And so, when we think about mobile, we think about it as an adjunct to our business -- something that expands the business, because what you find with mobile players is our core market that plays on PC tends -- with the exception of a couple reasons, but certainly, in the United States,

certainly, in Korea and China -- they have mobile devices, but mobile devices tend to be short form, short play, more casual experiences, at least, till now.

So, just as we didn't see a shift from immersive or console games to Facebook games, for example, we don't see a shift from immersive games or other forms of, call it, heavier gaming into mobile. We don't see that shift. Now we are experimenting with things like what we're doing on tablets with some of our larger titles, such Three Kingdoms 3D, and we think that there is an opportunity to make immersive games on mobile platforms, and we think that that ultimately expands our audience. So that's how we're thinking about North America.

The second question you asked about was the breakout of Europe, if I've got that correct.

Mia Nagasaka - *Morgan Stanley - Analyst*

Yes, that's right.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Breakup of Europe, relative to other countries. We were -- in the category of Europe and others, we -- that's a bucket that includes South America, Southeast Asia, and other areas. And Europe was up 6% on an as reported basis, but it was up 20% on a constant currency basis. Actually, where we were down in that category was in Southeast Asia and, in particular, Taiwan. We feel that we're going to get that on a better track, going forward.

So -- but we do expect higher growth from the European market over time, as we ramp up our business there, and, as I mentioned before, it's certainly well worth our while, because of what we're seeing there.

Seungwoo Choi - *NEXON Co., Ltd. - CEO, President*

Also, if I can add a little to that, Europe is a very interesting market. It definitely has a lot of countries -- different countries. You mentioned about color in major areas. We cannot really divide into countries, based on performance, but I can give you a couple of examples, such as, first person shooting games -- they tend to do much better in the UK, Germany; Poland is one of the most important emerging markets. Another example, with Turkey, whereas, games like MapleStory tend to do better in The Netherlands or Israel, a new -- another new market.

So it really depends on which genre and which country we're talking about, but overall, Europe is a very exciting market for us, and we expect to see continuous growth there. And I think I mentioned in our previous call, we set up our Luxembourg office at the end of last year, and we are shifting our business from Korea to Luxembourg, and I think will -- that will provide us with a better infrastructure to stabilize and expand our business in the future.

Mia Nagasaka - *Morgan Stanley - Analyst*

Thank you, Seungwoo.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

I think, Mia, you said you had another question?



Mia Nagasaka - *Morgan Stanley - Analyst*

Oh, yes. Very quickly, I just wanted to confirm that -- I understand that your revision is tweaking the numbers, but your third quarter operating profit is JPY9.2 billion. And I'm still a little bit trying to wrestle the numbers, because I understand that the third quarter should be the strongest quarter, due to seasonality, but can you add a little more explanation? Is there any factors that you found out the Asian market was weaker -- that is, slightly weaker than you had expected? Or are there any other reasons, like changes in the pay rate or something? (inaudible).

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Sorry I interrupted you. Yes. So, I'll talk about Q3. Our guidance is for just under JPY25 billion, which is up from the JPY22.8 billion that we reported in Q2. Relative to operating margins, again, we're targeting, for the year, 45%. We've said it's actually going to -- by our forecast, it's going to come in just a little bit ahead of that, but that's what we're targeting for.

And as we ramp up towards the end of the year, we have several new product launches. As those products get ready to launch, we will be investing more in marketing and getting ready for those launches, so that's why we've got higher marketing costs there. We've also been investing in new game developments. So that's been our expectation on those topics. On -- so, obviously, those are the main factors as we think about the balance of the year.

Mia Nagasaka - *Morgan Stanley - Analyst*

Okay, thank you. Great.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Thank you.

Seungwoo Choi - *NEXON Co., Ltd. - CEO, President*

Thank you.

Operator

Thank you very much, sir. There are no further question at this time. Sir, please continue.

Owen Mahoney - *NEXON Co., Ltd. - CFO*

Okay. Well, it sounds like there's no additional questions. We thank you very much for your time. As Seungwoo and I had mentioned, we're very excited about the quarter. We're also very excited about the remainder of the year. We feel we're right on track for our organic growth rate that we have achieved very consistently, and so, we look forward to talking with you again next quarter.

Seungwoo Choi - *NEXON Co., Ltd. - CEO, President*

Yes. Thank you very much indeed.

Operator

Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may now all disconnect.

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