

## SEGA SAMMY Management Meeting 2021

### Major Questions

December 24, 2021

SEGA SAMMY HOLDINGS INC.

IR/SR Department, Corporate Planning Division

(All contents here are the translation of Japanese materials)

■ Date: Tuesday, December 14, 2021, 16:00-17:30

■ Respondents:

Haruki Satomi (President and Group CEO, Representative Director of SEGA SAMMY HOLDINGS INC.)

Koichi Fukazawa (Senior Executive Vice President and Group CFO, Director of the Board of SEGA SAMMY HOLDINGS INC.)

Yukio Sugino (President and COO (Representative Director) of SEGA CORPORATION)

#### **Session 1: Growth strategy of Consumer business**

Q : Looking at the video, "SONIC FRONTIERS" looks like an open world kind of concept. Is that correct? Also, if you have any target number of sales, can you please share?

A : As for target number, because this is a completely new title for the first time in many years, and we are planning for a global multi-platform roll-out, we would like to go beyond the first year sales number of "SONIC FORCES", which is the previous title. For lifetime sales, we look forward to further increase. We'd like for you to wait future announcement for the details, but this is the title with no compromise in terms of quality and that has taken on many new challenges.

Originally it was planned to be released on this year, the 30<sup>th</sup> anniversary of Sonic, but we have postponed the release for a year in order to further brush up the quality. Not only for this title, but during the development phase, we have been steadily conducting analysis to improve the quality of the title before release, such as introducing game testing based on external evaluations, and I have a feeling that it will become a good game and have high expectations for it.

Q : For the initiatives with NetEase for Total War, what kind of scheme do you plan for this, including the publisher choices, especially for inside and outside of China? Also, can you share your views regarding its impact on revenue?

A : For the publisher of this business, we are planning for NetEase at this point. However, because of the current uncertain environment in China, we would like to discuss and decide the best option for each other including the intentions of our licensor, Games Workshop in mind. We would like to refrain from disclosing the impact on revenue.

Q : You have mentioned about P2E\* type model within the explanation of external environment. Can you please share the view you have for P2E at the moment?

A : In terms of NFT, we would like to try out various experiments and we have already started many different studies and considerations but nothing is decided at this point regarding P2E. There have been many announcement about this already including at overseas but there are users who shows negative reactions at this point. We need to carefully assess many things such as how we can mitigate the negative elements, how much we can introduce this within the Japanese regulation, what will be accepted and what will not be by the users. Then, we will consider this further if this leads to our mission “Constantly Creating, Forever Captivating”, but if it is perceived as simple money-making, I would like to make a decision not to proceed.

(\*Play-to-Earn: Mean to earn while playing)

Q : As for the concept about the additional growth investment of 100.0 billion yen, it seems this is an additional investment in addition to the base, but in the first place, how much is your base annual investments? Can you also share the area you are planning to invest (e.g. expansion of existing IPs, creation of new IPs, creation of Super Game, etc.) and the scale of investment in each area?

A : The image of base R&D expenses is about 50.0 billion yen per year at the moment. In future phase, R&D expenses are expected to increase as we are proceeding aggressive recruitment in domestic and overseas for the further enhancement of R&D resources. We are also expecting the reinforce of R&D resource by M&A, etc. within this additional investment of 100.0 billion yen. We'd also like to invest in maintenance of office environment in addition to aggressive recruitment, as the working environment, especially for overseas studios, is highly regarded and partially this leads to the creation of hit titles.

Other expected area for investment are acquisition of IPs and supplementation of value chains. We think our value chains are still weak in order to compete in global and online game market. As the expertise is being acquired through the roll-out of “PHANTASY STAR ONLINE 2”, we'd like to invest to enhance this. Also, about acquisition of IPs, we would like to consider if there are good studios, regardless of whether it is domestic or overseas. Although we would like to consider various possibilities, since M&A is subject to the circumstances of the other party, and at the same time, it is important that the acquisition price is reasonable, we will proceed with careful consideration. I also think that it would be better to work with partners on new technologies and domains, including NFT, rather than dealing with them in-house, and I would like to consider investing in such fields.

Q : Can you share the possibility of strengthening the monetization of Sonic IP further in order to increase profits, such as merchandising, movies and etc?

A : In terms of contribution to the profits, we think the games will be the main. We'd like to proceed the major new title for global and multi-platform in game area. Referring to the recent environment, the number of movie viewers we reached has increased significantly due to the global hit of the movie and the following subscription roll-out of it, and if you include mobile and other businesses, the IP has been able to reach the scale like hundreds of millions of people. As the effect of hit of the movie, the situations in which parents and children of two generations can enjoy Sonic IP together is increasing, so we think it is important to release high-quality games at this timing. For the expansion other than the game, we believe that it is principle to work with partners who are reliable and can provide high quality products and services.

As for animation we are working on with Netflix, we can roll out this with very low risk as the Sonic IP is strong. Towards the release of sequel movie, which is scheduled to be released in April, we expect the increase of view of the previous movie via subscription, etc. and will boost revenue again. The licensing business including merchandising has already become a scale of tens of billions of yen on a retail sales price basis, and its roll-out in EU and NA is expanding considerably. On the other hand, we still have lot of challenges in Asia market including Japan, so we want to focus our efforts over the next year when we release the new game.

Q : Is there any other SEGA owned IP that could take strategic IP roll-out similar to Sonic?

As for the potential other than Sonic IP, in terms of licensing and merchandising, IPs which we are receiving a lot of offers at the moment, are Persona and Project Sekai. I think we can continue to further roll-out aggressively for these IPs in the future. However, we don't expect they will grow to the IP that can reach to hundreds of millions of people, at the similar scale with Sonic, at this moment.

In addition, Super Monkey Ball, which we released the remake this year, has a history of recorded millions of downloads once when it was released as a launch title in App Store, and is very popular especially in the U.S., so we may see the possibility of the roll-out in video and merchandising. The offer for making video and remake of past IP is increasing significantly following the success of Sonic movie. We are considering revitalizing the revival of dormant IPs in the future, including the possibility of working with other partners.

Q : Can you share about your strategy for the repeat sales, especially how you think about the strategy to pile up the revenue continuously every year? It seems you can earn revenue from repeat sales following the year when you have numbers of new titles. However, there is an example of the other company which is combining pricing and regional strategies to build up profits. I'd like to hear your thought on such approach.

A : As for Consumer games, the culture of buying a package game on the day of release is no longer on the trend, and the penetration of digital sales has made it to a business that contributes to revenue for a long-term. In fact, the year after a new title is released, that title is counted as a repeat. Especially if the new title is released at the end of the fiscal year, it will contribute to the increase in volume of repeat sales the following year. For the pricing strategy, we feel that we are at a point where we need to rethink. For example, for the new Sonic game, as we are focusing on quality and spending certain amount of money on development, we think it is important to maintain the price by maintaining the value of the IP at high level, rather than simply lowering the price at early stage to increase the number of unit sales.

Other point is area roll-out. With the advance of digital transformation (DX), it became possible to reach areas such as South America, Africa, India, etc., where were previously beyond the reach of our marketing. We are constantly searching and examining how much opportunities each area has, and from the next fiscal year, we would like to increase our revenue base by steadily developing such areas.

Q : I guess this is related to NFT and P2E, but “Metaverse” is becoming a buzz word in recent year. Please tell us how SEGA defines this word and how you see the business opportunities, etc., with this.

A : As for the definition of Metaverse, I perceive it as a place where the people gather and communities are generated. For example, I think the reason why “Fortnite” and “Animal Crossing” is called Metaverse, is that many people gather there, and the community is generated there. Therefore, I think it is important that the IP itself is well established and welcomed by many users. For example, I don’t think a Metaverse can be established in a game with only 10,000 players. Conversely, the presence of Metaverse-like elements does not always gather people to a game. We are often said that “PHANTASY STAR ONLINE 2” has already embodied the Metaverse as it held the event like music live, etc. in the game and I think it is the strength of SEGA that we have been developing the sandbox type scalable game. If we don’t incorporate such new elements in the future, I think the games of today will be outdated in three to five years' time, so we are very conscious of creating games towards the world of five years or so from now. However, I believe that the goal is not to create a Metaverse, but the most important thing is to create a high-quality game.

We want to make Super Game as a game that support global and multi-platform with having a network and a community. If such game has a competitive element called PvP, it could turn into an e-sport. Furthermore, it could become a Metaverse if it has tens of millions of downloads worldwide and a certain number of active users. We are holding live performances within the game in Project Sekai, and they have been very well received. Although it is not a virtual world, we are challenging on the things to generate Metaverse. Although we don't call it a Metaverse as we think it is quite possible that the definition of the Metaverse will be changed from the current concept in five years, we think that a game with similar concept will be our Super Game.

Q : Please tell us how you manage the project management in overseas studio and any difficulties you are facing if you have.

A : As for the project management of overseas studios, the current head of SEGA Europe has experience in managing development companies, and is very good at communicating with studios. For example, when he shows us an organization chart, he always has the image that the studio is at the top and he is at the bottom. He has instilled in the studios under SEGA Europe his spirit that the management supports the studio, and is building a trusted relationship between the two. We have been able to build a relationship where we can frankly say anything within the group including the headquarters, even in the current environment where it is difficult to have face-to-face meetings. In particular, we believe that our stance of protecting and respecting the identity of the studios that joined the group through M&A is a major reason why they are functioning well.

As for the difficulty we are facing recently, I think it all comes down to the management under the impact of COVID-19. In addition, the game market is currently in a battle for how to acquire the developers, so we are struggling with the same issues with other companies for how to acquire human resources and their retention.

Q : The FPS game being developed by Creative Assembly is expected to be released in the next fiscal year, but there is no information at all, so please update the information.

A : There are several obstacles that we need to overcome for the FPS developed in Europe studio and we would like to launch the product after properly overcoming these obstacles and achieving a satisfactory quality level. We'd like you to wait for the update of information.

## **Session 2: Pachislot and Pachinko Machines Business, Financial Strategies**

### **Pachislot and Pachinko Machines Business**

Q : About the deregulation of pachislot and pachinko machines, will it be a enough incentive for pachinko halls to install smart pachislot and pachinko? I think there also was an incentive from deregulation when installation of CR machines occurred, but I think this time's deregulation is not as much as that time. In addition, from the perspective of capital investment, there may be a risk of smart pachislot and pachinko not spreading, but how do you think about it?

A : I think this time's deregulation will be a large change since the replacement to CR machines. Purchasing a dedicated unit is basically needed for smart pachislot and pachinko like CR machines, but when replacement to CR machines occurred, from the point of view that deregulation contributes to the sales, there was a fight over the units at that time. Also, by how the pachinko halls install smart pachislot and pachinko, the degree of benefit will differ for the pachinko halls. I think pachinko halls that place only smart pachislot and pachinko will gain more benefit from operation efficiency, compared to pachinko halls that place both existing pachislot and pachinko, and smart pachislot and pachinko. In consideration of approval status of prototype testing and continuing sales of existing machines, I think the full-scale spread will be around 2024.

### **Financial Strategies**

Q : About the measures to improve ROIC, I would like to know if you have confidence while working on it right now, and the degree of certainty including the schedule point of view. Will you be able to achieve the target by FY2026/3?

A : On the premise that we have set a goal of achieving ROE 10% within 3 years as our medium-term plan target, we will also achieve the ROIC hurdle rate within this period. Regarding Sammy, the possibility of achieving is high because they have already considered specifically about the measurers to improve ROIC. Also, regarding Sega, the investment amount will be larger from here, but we set their hurdle rate at the level that can be exceeded by achieving their ordinary income of the medium-term plan period.

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