

SEGA SAMMY Management Meeting 2023

Major Questions (Summary)

January 23, 2023

SEGA SAMMY HOLDINGS INC.

IR/SR Department, Corporate Planning Division

■ Date and time: December 12 (Tue.), 13 (Wed.), 2023, 16:00~

■ Respondents:

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*This document is an excerpt and summary of the Q&A session at the Management Meeting, and some edits and modifications have been made to improve comprehensibility.

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Entertainment Contents Business

Q: While I believe that Sonic and other mainstay IPs are expanding steadily and becoming much more profitable, why does the growth in profitability in the Consumer area as a whole appear to be not as high as expected?

A: Losses in the European business were the main factor in the previous and current fiscal years. Since our mainstay IPs, which are developed in Japan, is growing steadily, we believe that the profitability of the Consumer area as a whole will improve if we can realize an improvement in European business.

Q: Other companies are narrowing down their titles and moving toward to achieve home-run-level unit sales. SEGA, on the other hand, is increasing its pipelines, and it seems that it will be more challenging to increase the unit sales for each title. What is the reason for adopting this strategy?

A: This is due to SEGA's uniqueness. SEGA has a diverse range of IPs, and as the variety of gaming platforms and users increase, more various business opportunities are generated. In particular, most of

the time, SEGA is approached by platform owners at the launch of new platform. In other words, there are abundant opportunities to aim for a medium hit as well. Since aiming for a home run requires a large amount of cost and also have high risk, we will invest in a low, medium, and high scale while building a portfolio of titles to maximize sales growth and ROI.

Q: Will the overall profit of the Consumer area, which has been on a downtrend, turn around to increase as a consequence of structural reform in Europe?

A: The European business has had a significant impact on the decline in profits, and we expect profits to increase if the structural reform goes smoothly.

Q: I recognize that the recent decline in profitability in the Consumer area is due to the failure of new IPs such as *HYENAS*. Why do you continue to launch new IPs and work on Super Game? What will be the difference in new titles to be launched in the future compared to titles until now?

A: The cancellation of the development of *HYENAS* was caused by a combination of multiple factors, including the fact that it was not only a new IP, but also a high-level challenge to newly acquire expertise of managing online game. On the other hand, both new titles utilizing legacy IP and *Metaphor: ReFantazio* are new attempts, but the former are titles utilizing popular IPs from the past, and the latter is produced by the creators of *Persona 3 to 5*, so both of the challenges are based on a certain foundation. Furthermore, we are making steady progress in creating an environment which can control risks, based on efforts such as improving the development process, expanding sales territories, and strengthening relationships with platform owners.

Q: Is there any concern that review of pipeline through the structural reform could lead to a decline in sales?

A: The profitability of mainstay IP titles from Japanese studios has been expanding through the multi-platform and global-scale simultaneous release initiatives, and sales of some of them have increased several-fold. This approach has remained to be fully adopted in many titles from European studios so far, but some success cases are emerging. We believe that said concern can be covered by aiming to increase the number of units sold per title, regardless of the development studio.

Q: What is the outlook for repeat title sales for Full Game? Is it possible for the unit sales to be back to the level of FY2021/3, which was at its peak level due to stay-at-home demand?

A: It is difficult to say whether or not the market environment is likely to return to the level of the special demand at that time, but we recognize that it is a level that we should exceed. There are steps we can take such as full-fledged response to emerging markets, including pricing strategies, and also sales enhancement through promotion of new titles. In addition, together with efforts to expand IPs through the Transmedia strategy, we will strengthen our ability to sell our products.

Q: Why is there no flexibility in pricing for repeat sales in Full Game in emerging markets currently?

A: Our efforts for sales in emerging markets have just begun, and we have not yet accumulated sufficient expertise. On the other hand, the importance of tackling emerging markets is increasing, and in-house awareness towards this is also changing. We will continue to conduct research on market in each country and region, but at the moment, the foundation is now in place to promote the optimization in each region, including pricing.

Q: What are the KPIs for the initiative of "Strengthening engagement with fans"? When you offer a number of touchpoints, do you have a system that consistently captures the behavior of customers who have been exposed to multiple touchpoints by a single person?

A: For mobile games, we can recognize the status of engagement through data related to gameplay. For Full Game and movies, not only the number of purchasers and viewers, but the number of SNS followers and reactions to our news releases, etc., also could be KPIs. At present, we do not have a mechanism to list user activities within the framework of IPs, but we would like to consider it while looking at the cost and effectiveness.

Q: In the Consumer area, I think you should focus on developing existing mainstay IPs and legacy IPs on console and PC. Why are you promoting the mobile business in China?

A: We are not thinking in terms of a choice between console (CS) and PC or mobile. In expanding the touchpoints of our mainstay and legacy IPs, we will promote worldwide mobile gaming business in parallel with CS and PC business. Rather than doing all of them in-house, for example, we will collaborate with Chinese partner that has high development and operation capabilities in mobile, as in the case of the mobile title *Persona 5: The Phantom X*. In terms of global mobile development, collaboration with Rovio, which recently became our group company, could also be considered.

Q: Perhaps because the nature of the market makes it difficult for Japanese companies to control their own business in China, I see that Japanese companies have not been very active in this area. What is your strategy towards the success of *Persona5: The Phantom X*?

A: In Chinese market, we will maximize business opportunities and control risks by relying on our Chinese partners who have a wealth of expertise. Many Chinese companies are increasingly aiming for global success. The way we collaborate is changing from simply licensing out our IP for the Chinese market, as in the past, to working together to create titles for the global market.

Q: Regarding the monetization of mobile games, isn't the "Gacha" model that prevails in Japan difficult to be accepted in the West? What kind of billing model do you plan to adopt for *Persona 5: The Phantom X*?

A: At this point, there is nothing we can say, but we are aware that monetization methods differ by region, and we would like to select the most appropriate one. We will consider whether to focus on Asia or Europe and the United States, taking into account the compatibility with IPs.

Q: As you increase your pipeline and resources, there are concerns about your ability to manage risks such as quality, delays, and impairment. What are your thoughts on future hiring plans for domestic studios, etc.?

A: In Japan, our policy is to strengthen recruitment, but from the perspective of risk management, we are aiming for growth while maintaining a balance between in-house development and outsourced development. In terms of strengthening recruitment, we are making changes to our group-wide personnel system and strengthening our investment in human resources. According to a survey by a domestic recruitment agency, we are ranked high in the ranking of companies that students want to join, and we have taken the necessary steps to actively recruit talented personnel. In addition, we would like to strengthen the hiring of people who have diverse cultural background for domestic studios to further promote our global-scale initiatives.

Q: Regarding the development structure, do you mean that Full Game will be developed in-house and mobile games will be outsourced?

A: We will flexibly decide per project. We have the capability to develop everything in-house, including CS, PC, mobile, Full Game, and operating-type games, but we will consider the appropriate allocation of resources for each project on a case-by-case basis. For example, we will need to ask local companies for their support to expand our title into the Chinese market, as this requires unique expertise. In this way, the partnership approach differs depending on how we want to expand the business. We will look for the best partners to maximize business on a title-by-title basis.

Q: Is a global marketing structure and a cooperation structure between global studios being established?

A: New titles are usually released simultaneously around the world, and it has become routine for marketing personnel in Japan and overseas to communicate and work together. For example, the development team of *Like a Dragon* frequently holds conference calls with the U.S. marketing staff. Since our U.S. subsidiary covers the U.S. and European markets, which are the main markets for Full Game, we emphasize the close exchange of ideas from the development stage. Development team of *Sonic* has been working on this same approach for some while as well, and *Persona*'s team has also been taking steps.

Q: Could you tell us how you see the online game market? SEGA has online game technology through *PHANSASY STAR ONLINE 2* and other titles. Do you intend to further strengthen this area?

A: We recognize that online game will be one of the medium-term pillars of our future business and the investment in this area is necessary. Our domestic studio has already been operating *PHANSASY STAR ONLINE 2* for many years and has obtained the technology to run online games on PCs and consoles. It is the same for mobile games. We will further enhance our technology and expand the development of existing titles on a global scale. We believe that these knowledge will lead to the creation of Super Game.

Q: I would like to ask again what Super Game is. I would like to hear additional information such as target audience, genre, launch timing and etc.

A: At this point, we can say that it is an online game service that allows users to enjoy various ways of playing, not limited to just play the game, although the focus is on game. We are steadily advancing development.

Pachislot and Pachinko Machines Business

Q: What is your perspective on the Company's performance for the next fiscal year and beyond?

A: Although we refrain from going into details since we are still in the planning stage, we hope to generate at least a stable profit of 20.0 billion yen or more each fiscal year. As a background, although it will not be easy to continuously launch a blockbuster title on the level of *Smart Pachislot Hokuto No Ken* in this fiscal year, we believe that there is still room for replacement for smart pachislot machines from the point of view of penetration rate, and that stable demand will continue, thus enabling us to realize continuous profit generation.

Q: How far of spread of smart machine is required for full-fledged cost reductions in pachinko halls? What do you consider to be the bottlenecks that have not yet reached that level?

A: We do not operate pachinko halls, so we cannot give a detailed answer, but if the ratio of smart machines installed in pachinko halls were to reach 100%, labor costs, etc. related to operation would be reduced, sales efficiency per floor space would be improved because facilities needed for each pachislot and pachinko's row would be simplified, and also the noise problem, which is one of the factors that keep people away from pachinko halls, would be reduced. The lack of smart machine lineup in the industry as a whole may be a bottleneck, but there are already three smart halls in the market with ratio of smart machines installed 100%, and we expect this to continue in the future.

Q: *Smart Pachislot Hokuto No Ken* did very well in terms of both sales and utilization, but its follow-up, *Smart Pachislot Biohazard: Vendetta*, did not do well in terms of utilization. What is the background behind this?

A: This is a difficult question to answer, but *Smart Pachislot Biohazard: Vendetta* did not receive a bad in-house evaluation in advance. On the other hand, after its launch, there were noticeable elements of dissatisfaction from users in terms of gameplay and visual effects, and as a result, it did not contribute to utilization in pachinko halls. We will reflect on this in our future product development.

Q: What is the background behind the weakness in spread of smart pachinko, and what are the characteristics of recent hit titles from other companies in in the market?

A: We recognize that smart pachinko was not well received when it was first introduced, mainly because most of the titles released at that time were specification changed titles from the past. In addition, since actual balls are no longer used, it has been difficult to express the volume of the balls paid out, however we think that the latest hit titles have solved these problems through trial and error. We will continue to work on the development in order to catch up with this hit trend. .

Q: Is it correct to assume that the introduction of pachinko machines with "Lucky Trigger", which reflects the revised regulation, will stimulate demand for pachinko machines?

A: With the introduction of machines with "Lucky Trigger", demand is expected to increase for wider variety of machines in various specification ranges compared to the current situation. Currently, demand from pachinko halls is concentrated in the middle specification range (jackpot probability: around 1/320), but from March 2024, mainly machines with relatively high jackpot probability such as 1/99 and 1/199 will be able to feature "Lucky Trigger". We think this will increase the attractiveness of machines outside the middle-specification range.

Q: You mentioned *Pachislot Kabaneri of the Iron Fortress* as an example of utilizing a new IP. What is your future investment policy for anime IPs?

A: In order to further expand the user population, we intend to continue acquiring new anime IPs through investments in production committees, etc., and aggressively launch titles that utilize those IPs.

Q: Please tell us about the progress and economic benefits of the EC system for product sales, as well as how pachinko halls are evaluating it. Also, will EC sales become the mainstream in the long term?

A: We are already accepting orders from pachinko halls on our EC site. In addition, although business negotiations are basically conducted in person, for some titles, sales activities can be completed on the EC site. We believe that this system has been well accepted by pachinko halls too because it contributes to the reduction of labor costs, etc. for both pachinko halls and manufacturers by promoting DX related to the ordering of products. Some other manufacturers are also participating in our EC site, and we intend to further increase the number of participating manufacturers in order to make it a platform.

Q: "Communication between pachislot and pachinko machines" was mentioned as a possibility for improvement in efficiency and convenience over the long term but how should we image it?

A: As an example, if pachislot and pachinko machines can be connected to each other via Bluetooth, it may be possible to share visual effects that a person is seeing on the screen and jackpot information, etc. with friends who are playing with different machines in the pachinko hall. One of the most common reasons for acquiring new users is to be invited by their friends, and we hope that this will help things like that.

Investment in Growth, Financial Strategy

Q: I would like to know the background of the GAN acquisition and why you decided to make this acquisition from the perspective of increasing the corporate value of the Group.

A: In the past, we were working on the realization of an IR (Integrated Resort) business in Japan, but now we are working on the commercialization of an online-based gaming business which has high investment capital efficiency, rather than a land-based business that is heavily dependent on CAPEX. The North American market has extremely strict regulations, including compliance, making it very difficult to enter the market, but from another perspective, it is also a safe market to enter because compliance issues are less likely to occur. In addition, it has been growing into a booming industry centered on sports betting in

recent years.

GAN is currently developing the next generation of tech stacks, and its performance is in the red due to the burden of investment in development. However, in terms of customers, for example, it has one of the "Big 3" players in online sports betting as its customer. It is also providing solutions for managing customer accounts called PAM (Player Account Management system) for mega land-based operators while they are shifting their business into the online market, so as such it has a strong customer base. GAN also provides solution for the operation of RGS (Remote Gaming Server), which is used to distribute gaming content to online gaming operators. Since there are only a few companies in North America that can offer both RGS and PAM solutions at once, we believe that this is very attractive from the standpoint of technological capabilities as well.

Q: From the perspective of capital efficiency, how do you view the situation where the share price declines and corporate value decreases despite the debt financing from the Rovio acquisition?

A: We have recently announced structural reform of our European business, and since our overseas business has been the driving force of growth in the Consumer area to date, we believe that this is a major reason for concern about future growth. While we will continue to work on improving capital efficiency with respect to shareholder returns and business investment, we believe that the most important thing is to provide an explanation that can dispel concerns about the European business.

Q: I would like to know quantitatively and qualitatively of your future M&A execution policy. Is there no more in CS since you have used up your budget limit, or do you have flexibility to reconfigure parts of other areas?

A: In order to improve capital efficiency, we have set a growth investment quota of 250.0 billion yen as the capital structure of our balance sheet, which is the amount of business investment we would like to make while also utilizing debt. Although the figures are divided into approximately 100.0 billion yen for the Consumer area, 100.0 billion yen for the Gaming area and 50.0 billion yen for the Others area as a matter of convenience, the basic premise is that each investment must be economically rational, so it does not mean that all of the funds will be used. In the Consumer area, we used approximately 100.0 billion yen for the Rovio acquisition, and our first priority is to maximize synergies within the group through solid PMI. However, if there are further reasonable investments in the future, there is a possibility that we will additionally allocate the budget in the Gaming area to the Consumer area. In the Gaming area, the acquisition of GAN currently amounts to approximately 16.0 billion yen, and since there is still room in terms of the overall growth investment quota, we would like to consider additional investments if there are any reasonable options.

Q: What is your concept to the valuation of the 105.0 billion yen invested in the Rovio acquisition and what is your outlook for future earnings?

A: We have introduced ROIC management within the Group, and have set a hurdle rate for business investments, which is not to fall below 13% in terms of IRR. Not only the department in charge of M&A but

different departments such as corporate planning and finance also review the projection to ensure achieving IRR 13%. As a result, the IRR is not like Equity IRR, but rather we assume an adjusted IRR that take synergy into account, for example, not only the performance of Rovio, the investee itself, but also the return within the area relevant to the investment, including the benefits to be gained on the SEGA side after the acquisition. We have determined this valuation based on this Adjusted IRR assumption of well over 13% for Rovio.

While there is a hurdle rate of 13%, I personally believe that the minimum hurdle rate for investment in the Gaming area is 15%. Unlike the Consumer area, it is difficult to come up with an Adjusted IRR that takes into account synergies, so we assumed this investment performs 15% as Project IRR, resulting in the agreement upon rate of 1.97 US dollars per share.

So regarding our basic approach to investment, we operate under the rule that it must exceed the hurdle rate firmly, and that we include reviews from different departments within the company regarding the projection.

Q: Can we expect the implementation of structural reform in Europe have a positive effect on the future, including a reduction in invested capital? Or will it only have a short-term effect on cost containment and not on invested capital?

A: With regard to the European business, there is a possibility that ROIC will decrease momentary due to the decrease in profit level from impact of write-downs, etc., but we intend to increase ROIC by carefully observing the appropriate level of invested capital and revitalizing the business. In addition, Rovio has not yet made a significant contribution to our profits due to the amortization of goodwill, but in our future strategy for the Consumer area, we will focus on how much we can increase the return portion in these areas, including by globally expanding SEGA IPs using Rovio's mobile solutions, etc. We believe these will be a contributing factors to ROIC.

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