

Full Year Results for Fiscal Year Ended March 2021

Major Questions in Conference Briefing about Results for Analysts and Institutional Investors

May 21, 2021

SEGA SAMMY HOLDINGS INC.

IR/SR Department, Corporate Planning Division

(All contents here are the translation of Japanese materials)

■ Date: Thursday, May 13, 2021, 12:00-

■ Respondents:

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Pachislot and Pachinko Machines Business

Q: Regarding the FY2022/3 forecast, you mentioned that the forecast is based on expectation that pachinko halls' purchasing motivation won't go up in Pachislot and Pachinko machines market, etc. Are you just conservative, or do you already see such a trend at the beginning of FY22/3?

A: Most of the halls are removing their old regulation machines on schedule, and if this continues, old regulation machines that are installed in the market will be removed by the end of January 2022. Therefore, we aim to obtain approval for new regulation machines in order to supply our machines at this timing when there is the replacement demand in the market. The market will return to normal after the removal of old regulation machines, so we are going to make an effort to increase the hall's purchasing motivation.

Q: Regarding the figures in the Mid-Term Plan, what will happen to the income if sales are not sufficient. Especially in the Pachislot and Pachinko Machines Business, it is very hard to imagine the market 3 years from now, so about the final year of the Mid-Term Plan, will you tell me how do you think about your income when sales are not achieved?

A: A decline in sales doesn't mean that income will decrease in conjunction. We will take care of it by adjustment depending on the demand of machines and conducting cost controls.

Entertainment Contents Business

Q: Regarding the figures in the Mid-Term Plan, in Entertainment Contents Business, income will jump significantly in the final year and I would like to know how the income will increase over the next 3 years. You mentioned the development of FPS title in European studio, so will such new titles contribute and result to the final year's growth? When I think back to the previous Mid-Term Plan, I honestly feel

uneasy if the plan is dependent on some specific new products.

A: The income forecast is built by mix of title portfolios. For operation-type games, there is a trend that the sales will be highest in the second year, and in the third year, amortization of early phase of development ends and contribution to revenue is high. From this perspective, we think that the developing FPS title in the European studio will contribute in the final year of the Mid-Term Plan. Regarding "Phantasy Star Online 2", reboot title NEW GENESIS will be released in the first half of FY2022/3, but along with this, while we are working on global simultaneous expansion, areas such as Southeast Asia and South America are not included yet. Therefore, if we would expand our service to these areas sequentially, we are able to raise earnings with small additional cost. If new titles from Atlus, which are being able to sell for a long time recently, comes out from the first year of the Mid-Term Plan, it will contribute to the earnings as a repeat title from the next fiscal year and beyond. As a result of these factors, we have an image of the earnings jumping up in the final year of the Mid-Term Plan. Therefore, our plan is not like a plan that is extremely dependent on some specific new products, as you have mentioned.

Q: Forecast for income of the Consumer area is 21.0 billion yen in FY2022/3 and 25.0 billion yen in FY2023/3. Regarding the advertising expenses, etc. in this forecast, how will these expenses, etc. be in FY2023/3 compared to the forecast for FY2022/3?

A: As new titles will increase, the budget for advertising expenses is large in FY2022/3. In terms of historical trends, there are few cases where the entire budget has been used up, but in some circumstances, there are titles that spend more advertising expenses than the budget. For example, we are currently allocating certain extent of budgets for FY2022/3, but because we hold official Olympic titles in our product line-up, the amount of advertising expenses we would spend will change depending on whether or not it is held. Basically, FY2023/3 will be the cycle when the titles released in FY2022/3 becoming the repeat sales and new titles will also appear, so we think that we can aim for earnings of more than FY2022/3.

Q: In 2020, "Persona 5 Royal" took the top in the ranking website for games overseas (Metacritic) and SEGA as a whole also took the top in the publisher rankings. While the reputation for its products is extremely high, there is an image that its reputation is not leading to much earnings, possibly because of some shortage in the way you sell them. What are your views on the divergence between these high ratings of users and the sales results, and how will this change within the Mid-Term Plan?

A: Regarding the evaluation of metacritic, there was a problem with product quality in the game of Sonic in the past, which is our representative IP, and a major reflection was that it recorded an extremely low score and largely betrayed user expectations. Since then, we set a policy of prioritizing the creation of high-quality games that people who purchase our games will enjoy, and not acknowledge to release the products when quality is insufficient just to achieve the plan in the short-term. Of course, it is the best if QCD (quality, cost, delivery) is well balanced, but we believe that the accumulation of such quality-oriented policies has been reflected in such ratings.

Therefore, as you pointed out, the next step for us is an improvement in selling methods. As

explained in the briefing session, the potential for significant expansion of sales of the same game is still left through the simultaneous global release and the multiple languages support, and we think the earnings will naturally follow. Until now, for example, when we launch Ryu ga Gotoku (Yakuza in overseas) title, we have released the Japanese version first and subsequently released in succession for each region, so there were dispersion in the level of localization, such as whether or not to support voice localization and the corresponding languages. By changing this to the simultaneous roll-out in multi-platform and multiple languages, the dispersed marketing costs can be spent within certain period of time in focus and can be restrained as a result. In terms of the PC market, Steam has been the strongest platform up to now, but it becomes the environment where we can expand to other platforms, including Epic Games. By pursuing such multi-faced roll-out, we think we can establish the structure that will enable to sell the titles 2 million to 3 million units in lifetime, which had previously been sold around 1 million units globally.

Q: Regarding the term Super Game explained in the briefing session, I personally think that "LOST JUDGMENT" could be a title considered to be a Super Game title, but why did you set it as a target for a little further ahead in the explanation? I would also like to hear about the targets set for this, such as the number of title to be developed as a Super Game.

A: We don't see "LOST JUDGMENT" as a Super Game, and it is positioned as a pillar strategy title, including series like Ryu ga Gotoku (YAKUZA in overseas). Sonic, etc. are also one of the pillar strategy titles, and we are aiming to grow these as the pillars that aim to achieve sales scale of around 20 billion per year, including revenues from non-game channel, such as animation, merchandise, and licensing, etc. In other words, I want you to understand that we will work on making existing IPs into a global brand.

As I mentioned earlier, Super Game Strategy has a separate concept from them, and aims to provide new and innovative games that can be "online" and "communitized" globally, within five years as the target.

"PHANTASY STAR ONLINE 2" is expected to achieve accumulated sales of 100.0 billion yen by the end of FY2022/3 and in the following NEW GENESIS, we will continue to operate with a firm view to how further we can grow this. In addition, game currently under development at European studio is proceeding under the R&D expenses at the level of our highest-ever and we believe will be similar to Super Game, although it will not be fully fit for the definition, as this has been in development before we raised Super Game concept.

In addition, our domestic studio has already begun working on the concept of 2 titles aimed at Super Game. At the same time, it is possible that we will take the option of acquiring development studios for implementing these strategies.

Q: I would like you to explain specifically about the creation of Super Game in Consumer area. I think it will take about three to four years to create one game. Therefore, even if development starts from now, I think the game won't be able to be released until around 2026.

A: We are already in the phase of planning about the Super Game, and we aim to launch it around CY2024 to CY2025.

Resort Business

Q: Your policy on IR (Integrated Resort) has changed dramatically from participating in majority to minority, so I would like to ask about the background that triggered this change such as regulations, etc.

A: Considering the situation that we would also like to invest heavily in other business as well, we considered options including participating in minorities. As a result, there is a strong possibility that we will be able to secure adequate profitability when we participate as a minority, and we view this business can become viable even if we curtail our investment.

At the same time, even when considering partnerships with other companies, we have seen an image that bringing in the strengths of each other would be better than tackling this business by us alone. For example, in order to attract Chinese customers, it would be better to form a partnership with a foreign company, and in deepening of the analysis of Japanese customers, there is benefit for our partner to work with us as we have been accumulating the expertise through the operation of PARADISE CITY. In this way, from the perspective that we would be able to form a good partnership, we have shifted our stance to aim the participation as a minority.

At present, we consider the law related to the development of IR as the big concern. Since the guarantee of business duration term is not stable under this law, financing may become tough condition so we judged that it would be better to control risks to some extent and aim at appropriate returns.

Other

Q: Regarding the Mid-Term Plan announced, how do you think about the probability of achieving the goals for the final year? In the previous Mid-Term Plan, although there were the considerable changes in the market environment, some parts fell short.

A: Regarding the shortfall in the previous Mid-Term plan, we have set the goal high, and immediately after the announcement, the rules of Pachislot and Pachinko machines changed, so the preconditions were broken. For this time, for Pachislot and Pachinko Machines Business, we have set a realistic goal rather than a high goal. For Entertainment Contents Business, we think that the life cycle of each title is extending more than ever and can be sold longer. For example, the games that will be released in FY2022/3 and FY2023/3 will contribute as a repeat title in and after the next fiscal year. Also, by proactively expanding our titles to new platforms, we believe it's an achievable goal.

The biggest difference between the previous Mid-Term Plan and the new Mid-Term Plan is that we now have a better idea of the amount of funds that will be needed for IR business. We have been conducting our business activities while our net assets being at a high level due to the IR business, so ROE did not rise easily. However, from this fiscal year onward, we would like to take such risks and leverage firmly, including proactive investments to the Consumer area.

Q: Regarding ROE, you may withdraw from IR business depending on the conditions, and if this happens, the current cash will become redundant. In this case, are there possibilities of implementation of buybacks or raising dividend, etc. to lower the equity and raise ROE?

As you pointed out, if the investment doesn't go smooth as expected, we need to control the equity to

some extent. In the situation of cash piling up, discount will happen, so we need to take balance. If by any chance we don't obtain a license for IR business, we have to think of returning to shareholders and investing to different businesses about the surplus, because we won't be able to achieve our ROE goal, and won't be able to earn in the future.

Q: Until the Yokohama IR project becomes a little more concrete, should I think of your shareholders return policy to be the same as current?

A: We now have a rough idea of the exposure we can take and how much funds are needed. For shareholders return policy of the total return ratio to at least 50% and the DOE to 3% or more we proposed this time, we'd like to implement them regardless of the Yokohama IR. Funds for Yokohama IR are not needed immediately and will be needed sequentially. We will keep it in place, but as cash accumulates in existing businesses, we will invest it to other businesses and return it to shareholders.

Q: I assume that ROIC in businesses other than Sammy and SEGA is low. Please share your thoughts on ROIC management and business portfolio management, including the sale of assets and businesses.

A: For example, when we set the company-wide ROIC target at 10%, the standard values for ROIC of business companies vary from company to company due to differences in business characteristics of each group company. However, we set ROIC to be achieved by each business company on the assumption that will exceed WACC target when viewed from a consolidated perspective as a whole, and this ROIC target is not a KPI such that business that have not been achieved are immediately considered as the business to withdraw from.

When considering the media mix of contents, we consider being able to provide the contents it offers to customers through various channels and products to be a major business objective and value. In addition, there is the merit such as being able to acquire the license of other companies' IP for other business as a consequence of holding certain business, so there are some business that we continue to hold from the perspective of business portfolio.

We may consider the withdrawal of business when we face strategic distortions, such as it is better to sell rather than continue to be held by our group, not only from the P/L aspect but also from the strategic aspect, like the sales of Amusement Center Operations business in FY2021/3. However, we think we have been able to organize our business portfolio once with the structural reform this time. We have set hurdle rates for ROIC of each business company in a way they contribute to the targeted ROEs, and we would like to work on under the present organization for the time being.

Q: Regarding operating income for this fiscal year, it was 9.0 billion yen at the revised forecast announced on February 12, 2021, but the landing announced today was 6.5 billion yen. What are the reasons?

A: Operating income was lower than expected, mainly due to impairment of some titles, increase in advertising expenses, and sales of parts of new and repeat titles fell short in 4Q than expected in the Consumer area.

Q: In addition to reduced fixed expenses due to the structural reform implemented in FY2021/3, FY2022/3 expects an increase of 35.0 billion yen in sales compared to FY2021/3. However, the operating income increases only 6.5 billion yen to 20.0 billion yen. Isn't your expectation too weak?

A: We have postponed various investments in FY2021/3, and there are business areas that we are going to proactively invest from FY2022/3. In the Pachislot and Pachinko Machines business, we have reduced our fixed expenses due to the structural reform, but we have a conservative look towards the pachinko hall's purchasing motivation, and in addition, we included investment fees for our new business and advertising expenses, such as TV commercial fees for our new titles in the budget. Also, in the Entertainment Contents Business, there will be many titles to be released in FY2022/3, so we included many advertising expenses in the budget. In addition, we expect our repeat sales to temporarily decrease because the number of new titles sold in FY2021/3 was low, and the settling of stay-at-home spending. These are the reasons. However, from here on, there will be a lot of new products from FY2022/3, so we think the volume of repeat sales will pick up again in FY2023/3.