

Q2 results for Fiscal Year ending March 2022

Major Questions in Results Briefing for Analysts and Institutional Investors

November 11, 2021

SEGA SAMMY HOLDINGS INC.

IR/SR Department, Corporate Planning Division

(All contents here are the translation of Japanese materials)

■ Date: Monday, November 8, 2021, 13:00-

■ 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.)

Company-wide

Q: A share buyback of 30.0 billion yen was announced, but will you make decisions on share buybacks each fiscal year? Should we consider that the review of surplus funds has been completed once?

A: Regarding domestic IR, the timing of capital call is expected to be slipped for at least two years. In order to control the two-year surplus of Equity, from the perspective of balancing debt and equity, we announced this time that we will acquire treasury stocks of 30.0 billion yen, which is about 10% of our net assets. Regarding our approach in the future, the top priority we consider is to grow our business, and if the business investment of about 200.0 billion yen goes well, we think that we can make a return through the growth of the business, not only returning directly as a shareholder return. On the other hand, if this situation of business investment becomes unfavourable, there is a possibility that the time will come when we have to think about the same thing as this time. Also, we are considering whether we can make our dividends payment more flexible. We are thinking of increasing our dividends payment considering factors such as DOE 3% and total return ratio of 50% or more, rather than the 20 yen fixed dividend per half year, which we think is the minimum requirement.

Q: In what area will the business investment of 100.0 billion yen each be used as? How has your consideration proceeded compared to the full year results announcement in May?

A: As a controllable point, we will invest in strengthening development resources. For example, establishment of new studios, aggressive recruitment, and improvement of in-house development environment, etc. We are already making progress on this issue, but we think that the amount to be spent on them will be in the range of 10.0 to 15.0 billion yen at most. In addition, we are considering M&A and investment in new fields such as NFT. Opportunities for the domestic IR business may emerge in the next one to three years, but in the meantime, if there are opportunities to invest heavily in other areas, such as online betting which is gaining force overseas, there is the chance we prioritize them. Conversely, if an acquisition of a company can be realised without using more funds than expected such as through LBO, and if the cash will flow well, we may have additional investment capacity.

Entertainment Contents Business

Q: For “HUMANKIND™”, although the reviews at Steam, etc. are good, has it contributed to the Q2 results? Also do you think you can make this IP a series in the future?

A: It was good start so that we can expect to make this a series in the future. We find potential in this title, and it has become an IP we want to nurture for a long time. Although we cannot disclose specific figures as the revenue from the business deal are also included, it is undoubtedly a title that contributed to the Q2 results.

Q: Will the business alliance with Microsoft lead to differences in the relationship with other platformers? Also, will this collaboration lead to medium- to long-term financial support, etc.? When can we expect to see new titles?

A: We will collaborate with Microsoft to develop the titles we call “Super Game”, but we do not think this will lead to differences in relationship between other platformers as we are planning to release such titles to other platforms as well. Microsoft's cloud service, Azure, is spreading throughout the world, including Africa, South America, and other areas where we are still not able to reach, and we hope we could receive the support from them for those areas as well. We are already collaborating in Azure field for “PSO2”, and we would like to further develop this relationship. We are also conducting technical verification of whether the vision we want to achieve for new titles that will be developed in the future is feasible. Originally, we proceeded the development on our own, but in terms of delivering innovative titles globally in the future, we judged that it would improve feasibility by receiving technical support from Microsoft, and we reached to the alliance we announced recently.

Q: For the forecast for the second half of the Entertainment Contents business, especially in the Consumer area, it seems to be very conservative. While it tends to be conservative every year, what are your thoughts on the variable elements in the second half amidst there are number of relatively solid titles that are easy to forecast the sales such as "Shin Megami Tensei V" and "Total War: WARHAMMER III"? Please tell us about the assumptions for the second half forecast.

A: In the second half of the fiscal year, incentives at the end of the fiscal year, earn-outs in past M&A and other costs are expensed within fixed costs every year. The volume of these expenses are around 5.0 billion yen and incurred as unique expenses of the second half. As revenue from a number of licensing out deals were recorded in the first half of this fiscal year, the impact is around minus 3.0 billion yen as comparison between the first half and the second half. In addition, with the launch of the new titles such as “Total War: WARHAMMER III” (released in February) in the second half, margins will be lower from the periodic profit -and-loss perspective as the proportion of initial development costs to be recorded in this fiscal year is large. Therefore, in total, there will be a difference of about 8.0 billion yen compared to the first half.

Q: Please tell us about the sense of schedule for the major update of “PHANTASY STAR ONLINE 2 NEW GENESIS” in the future.

A: As many users pointed out the lack of game volume, we focused our development resources on improving this area in the major update in December. As a result, large-scale update has been realized at relatively early timing. Given this situation, we believe it will be difficult to continue to make major updates on a short span, such as every three months, but we are aiming for making updates in every six months or so. In addition, with the events and other activities, we are thinking of increasing the volume that players can play. While it is ideal if users play the game every day, the good thing about online games is that the users who play other games can come back if there are updates. Since this game has been running for 9 years and has a lot of fixed fans, we believe that if we can make updates properly, the fans will come back.

Q: For Sonic IP, a sequel to the movie and the distribution of a new animation on Netflix, etc. are already scheduled for next year. How do you look at the next fiscal year about this IP?

A: Sonic is a long-loved IP, celebrating its 30th anniversary this year, and a major new game is scheduled for release in next fiscal year. In addition, the release of the sequel of the movie "Sonic the Hedgehog", which predecessor had been a major hit globally, is scheduled next spring. The responses to the information that has already revealed are also good, and we expect it to be a bigger hit than the last one. We also plan to distribute a new full-CG animation in Netflix next fiscal year, and from this perspective, we hope that Sonic will be able to get significant exposure and deployment in the next fiscal year. As a survey indicate that Sonic has come within 50th place in the popularity ranking of characters worldwide, it can be said that the popularity of Sonic IP is increasing globally.

Q: Regarding future investment strategies, what are your thoughts on using outsourcing when increasing your pipeline for titles?

A: From the perspective of reinforcing development resources, we are also considering the use of outsourcing. As for outsourcing, we are considering various options, including not only domestic but also overseas studios. Although this was licensing out deal, "Streets of Rage 4", which is our IP, was remaked by a French venture studio based on our past arcade game and became a smash hit. We'd like to consider the use of outsourcing from the perspective of strengthening its resources both domestically and overseas, like outsourcing the development of another remake product to such studios, for example. We plan to actively use outsourcing as a complement to our resources.

Q: Regarding the explanation of approx. 100.0 billion yen investment in the Consumer area in the results presentation, there is no mention of Super Game, but is investment to Super Game included here?

A: Investment to Super Game is included in this 100.0 billion yen (The part where we plan to reinforce in the future, as an additional number to the existing development resources).

Q: It was explained that the upward revision of the full-year consolidated results forecast was due to the strong performance of Entertainment Contents Business, but I would like to know more specific background.

A: Repeat sales jumped significantly in Q1 of the previous fiscal year due to the impact of global lockdowns and other factors, but we initially considered this to be one-off. In fact, Q4, etc. in the previous fiscal year were weaker than expected, so we have not strongly expected in this fiscal year, but this went higher than expected. We think that the level of game habit itself may have raised higher through the stay-at-home period, and we feel that it will not go down to the level before COVID-19 and will be raised in the future. In addition to this strong performance of repeat sales, recording of many business development deals in the first half is the factor to the strong performance of the first half.

Pachislot and Pachinko Machines Business

Q: It was explained that the replacement of pachislot machines is not progressing well, but how do you think about the demand in the next fiscal year?

A: Although this is only a personal view, we think that the demand for pachislot machines will increase in the next fiscal year. The launch of Type 6.2 regulation machines, which is benefitted from the relaxation of regulation, has begun, and additional relaxation has been realized for the Smart Pachislot in the future. As a result of these relaxation, if titles that pachinko halls really want to purchase and users want to play comes out, we think that the demand can be expected to be higher than this fiscal year.

Q: The operating profit forecast for the Pachislot and Pachinko Machines Business is below that of the Medium-term plan. Should further structural reforms and associated expenses, etc. be considered in the future?

A: We will continue to implement measures to reduce costs, but we do not plan an additional implement of structural reforms, etc. In fact, orders themselves are increasing, but due to the shortage of components, we conservatively revised our plan. If the necessary amount of components can be obtained, we think we can catch up to the level of medium-term management plan.

Q: I would like to know when the problem of components shortage in the Pachislot and Pachinko Machines Business will be resolved.

A: Regarding the shortage of components, the circumstances differ depending on the component. Not only us, there is a shortage of semiconductors and a variety of other components in all industries, and some components are said that it might be short constantly until around 2023. Currently, we are responding not only by expanding procurement route and using alternative components, but also by reusing the parts from trade-in of machines in market. This is a measure that will lead to reductions in environmental impact and also costs, so we will continue to actively implement it.

Also, among our business, this concern has also emerged not only in the Pachislot and Pachinko Machines, but also in our Amusement Machine and Toys business, such as the shortage of semiconductors, IC, etc.

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