

# THE FACTS

For those less familiar with the SEGA SAMMY Group, beginning by reading this section is advisable. It includes basic information on the business lines of the Group and the business conditions it faces.

## THE FACTS

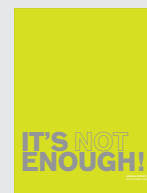
# Our Communication Tools

To enhance communication with shareholders, investors, and a wide range of stakeholders, the SEGA SAMMY Group continually expands and improves its communication tools.

### Investors

#### The SEGA SAMMY Group's Annual Report 2012

In *Annual Report 2012*, as well as reporting on the Group's business results for fiscal 2012, we have sought to further understanding of our growth strategies going forward. To this end, compared with the insights offered through disclosure pursuant to laws and listing regulations, we provide additional information that presents the Group in a different light. Furthermore, to assist the understanding of as many readers as possible, we have prepared "THE FACTS," which mainly comprises basic information.



#### Online Annual Report 2012

An HTML version of *Annual Report 2012* is available on the investor relations page of the SEGA SAMMY HOLDINGS web site. ➔ <http://www.segasammy.co.jp/english/ir/ar2012/>



#### IR Web Site Page

On the IR page of the SEGA SAMMY HOLDINGS web site, we post comprehensive, reliable information for shareholders and investors promptly. This includes timely disclosures as well as financial settlement figures in Excel format.

IR page of the SEGA SAMMY HOLDINGS web site ➔ <http://www.segasammy.co.jp/english/ir/>



### Individual Investors

#### Web Site Page for Individual Investors

A dedicated web site page, "For Individual Investors," and other pages provide an easy-to-follow introduction to the Group's business lines. Meanwhile, *SEGA SAMMY Monthly Report* features the latest information on the Group's products and services.

"For Individual Investors" web site page ➔ <http://www.segasammy.co.jp/english/ir/individual/>



#### Business Reports

Every six months, *SEGA SAMMY REPORT* updates our shareholders on business results and topics.



### General Stakeholders

#### SEGA SAMMY Group CSR Report 2012

*SEGA SAMMY Group CSR Report 2012* details the Group's wide-ranging corporate social responsibility (CSR) activities. *Annual Report 2012* includes an overview of issues from among these activities that could affect the Group's medium-to-long-term strategies or business results. Also, our CSR-related web site page, "Social Responsibility," carries the latest reports on our CSR activities.

"Social Responsibility" web site page ➔ <http://www.segasammy.co.jp/english/pr/commu/>



# History



<b>1950</b>	1951 Founded
<b>1960</b>	1960 Incorporated (Company name: Nihon Goraku Bussan Co., Ltd.) 1964 Started production of amusement arcade machines. 1965 Started operation of amusement centers. Changed company name to SEGA ENTERPRISES LTD.
<b>1970</b>	
<b>1980</b>	1983 Launched SG-1000 8-bit home video game platform. 1985 Launched <i>Hang On</i> , the world's first force feedback game. Launched <i>UFO Catcher</i> .  1986 Registered stock on over-the-counter (OTC) market. 1988 Listed stock on the second section of Tokyo Stock Exchange. Launched <i>Mega Drive</i> 16-bit home video game platform.
<b>1990</b>	1990 Listed stock on the first section of Tokyo Stock Exchange. Launched <i>R-360</i> , the world's first amusement arcade machine that could rotate 360 degrees in all directions. 1991 Launched first title in the <i>Sonic the Hedgehog</i> series. 1993 Launched <i>Virtua Fighter</i> , the world's first amusement arcade 3D computer graphics fighting game. 1994 Launched <i>SEGA Saturn</i> 32-bit home video game platform. 1995 Launched <i>Print Club</i> with ATLUS Co., Ltd. 1996 Opened <i>TOKYO JOYPOLIS</i> rooftop theme park in Tokyo's Odaiba area. 1998 Launched <i>Dreamcast</i> home video game platform.
<b>2000</b>	2000 Changed company name to SEGA CORPORATION.  2003 Launched <i>The King of Beetles "MUSHIKING,"</i> kids' card game.
	2004 Established SEGA SAMMY HOLDINGS INC. 2005 Acquired all outstanding shares of The Creative Assembly Ltd. (SEGA). 2006 Made SPORTS INTERACTIVE Ltd. a wholly owned subsidiary (SEGA). Entered strategic business alliance with Sanrio Company, Ltd. (SEGA SAMMY HOLDINGS). 2007 Made TAIYO ELEC Co., Ltd., a subsidiary (Sammy). 2008 Reached agreement with Sanrio Company, Ltd., to jointly develop new characters (SEGA SAMMY HOLDINGS). 2009 Made GINZA CORPORATION a subsidiary (Sammy). Established SEGA SAMMY VISUAL ENTERTAINMENT INC.* (SEGA SAMMY HOLDINGS). Established Bakugan Limited Liability Partnership (Bakugan LLP) (SEGA SAMMY HOLDINGS and Group companies).
<b>2010</b>	2010 Made Sammy NetWorks Co., Ltd., SEGA TOYS CO., LTD., and TMS ENTERTAINMENT, LTD., wholly owned subsidiaries (SEGA SAMMY HOLDINGS). Cancelled 17 million shares of treasury stock (SEGA SAMMY HOLDINGS). 2011 Made TAIYO ELEC Co., Ltd., a wholly owned subsidiary (SEGA SAMMY HOLDINGS). 2012 (As of August) Made Phoenix Resort Co., Ltd. a wholly owned subsidiary (SEGA SAMMY HOLDINGS). Concluded agreement on establishment of joint venture with Paradise Group of South Korea (SEGA SAMMY HOLDINGS). Established SEGA Networks, Ltd., through divestiture from SEGA (SEGA).

	1975 Established Sammy Industry Co., Ltd. 1978 Began game machine development. 1982 Began sales and marketing of pachislot machines.
	1989 Began sales of <i>Aladdin</i> single-bonus hitter pachislot machine.
	1991 Moved head office to Toshima-ku, Tokyo.
	1995 Began sales of pachinko machines. 1997 Changed company name to Sammy Corporation.
	1999 Registered stock on OTC market. Launched <i>GeGeGe No Kitaro</i> , the first pachislot machine equipped with an LCD.
	2000 Made RODEO Co., Ltd. (formerly Barcrest Co., Ltd.), a subsidiary. 2001 Listed stock on the first section of Tokyo Stock Exchange. Completed Kawagoe Factory. 2003 Launched <i>Hokuto No Ken</i> pachislot machine, which set a new record for unit sales.



*UFO Catcher*  
© SEGA



*Aladdin* pachislot machine  
© Sammy



*Sonic the Hedgehog*  
© SEGA



*Hokuto No Ken*  
*pachislot machine*  
© Buronson & Tetsuo Hara  
© Sammy

\* Currently MARZA ANIMATION PLANET INC.

THE FACTS

# Summary of the SEGA SAMMY Group

The SEGA SAMMY Group is a comprehensive entertainment company with business activities spanning a broad array of areas from pachislot and pachinko machines through to amusement arcade machines, amusement center operations, home video game software, digital content for social networking services (SNS) and smartphones, toys, and animation. By creating synergies among Group companies and taking on new challenges that exploit its expertise in entertainment, the Group aims to grow corporate value continually.

**SEGA SAMMY HOLDINGS INC.**

Date of Establishment  
October 1, 2004

Capital  
¥29.9 billion

Total Shares Issued and Outstanding  
266,229,476 shares

Number of Shareholders  
88,239

Number of Employees  
6,700 (consolidated)

As of March 31, 2012



SEGA SAMMY's dramatic progress worldwide



SEGA SAMMY blue  
success and growth

SEGA SAMMY green  
stability and  
permanence

**The Group Logo**

The logo symbolizes the creation of synergies by intertwining two renderings of the initial letter of both company names, the letter S, in the blue and green corporate colors of SEGA and Sammy. The curving lines linking SEGA and Sammy represent the Earth, simultaneously expressing the companies' solidarity and the Group's determination to develop globally.

**Pachislot and Pachinko  
Machine Business**

This business segment comprises the pachislot machine business, which has maintained its position as the industry leader, and the pachinko machine business, which has been building its presence each year thanks to strengthened development capabilities. A feature of the business segment is an operational structure that is highly resistant to changes in market conditions, which we built by reforming cost structure and establishing a balanced product portfolio. Going forward, we aim to maintain the No. 1 market share of the pachislot machine business and to acquire a leading market share for the pachinko machine business in the medium term. To this end, we are further bolstering our development system while ramping up manufacturing and supply capabilities.

**Net Sales**

Billions of yen

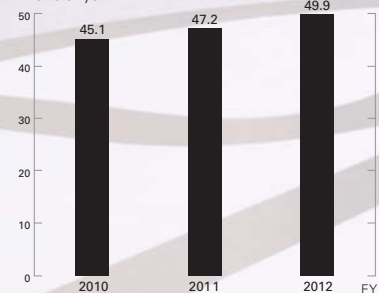


**Amusement Machine  
Sales Business**

As SEGA's founding business, this business segment has remained in the vanguard of the very latest market trends by creating numerous world-first and industry-first products. It caters to diverse needs through an extensive product lineup that covers network-compatible games through to products for families. Also, the business segment is promoting the supply of products and services designed to revitalize the market, including products provided through a revenue-sharing business model.

**Net Sales**

Billions of yen

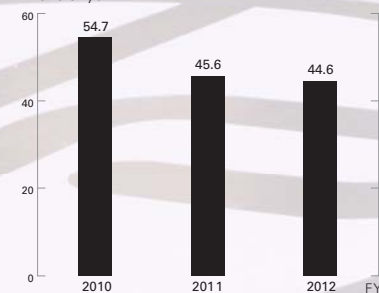


**Amusement Center  
Operations**

By collaborating with the Amusement Machine Sales Business segment and deploying diverse amusement center formats, this business segment is developing a network of amusement centers ideally suited to particular locations. While steadily strengthening earning power through unceasing structural reform efforts, the business segment is launching such ventures as new-concept theme park-type amusement centers.

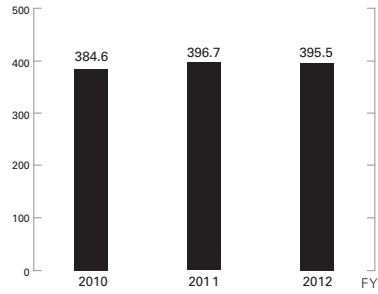
**Net Sales**

Billions of yen



### Net Sales

Billions of yen



*Pachislot Hokuto No Ken*  
©Buronson & Tetsuo Hara /  
NSP1983  
© NSP2007.  
Approved No.YRI-125  
© Sammy



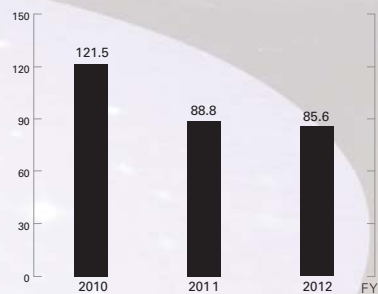
### Consumer Business

This business segment comprises the game content business, the toy sales business, and the animation business.

The game content business is restructuring businesses in the packaged game software area while urgently shifting the allocation of management resources toward content for SNS and smartphones. Meanwhile, in the toy sales business, fabless company SEGA TOYS CO., LTD., is building a unique position through the development of edutainment toys and products for adults. In the animation business, TMS ENTERTAINMENT, LTD., is generating steady earnings by taking advantage of rich animation assets, which include *Go! ANPANMAN*, *Detective Conan*, and *Lupin the 3rd*. Furthermore, MARZA ANIMATION PLANET INC. is producing computer-graphics (CG) animation.

### Net Sales

Billions of yen



*StarHorse3 Season I*  
A NEW LEGEND BEGINS.  
© SEGA



TOKYO JOYPOLIS



*Kingdom Conquest*  
© SEGA



**THE FACTS**

# Pachinko and Pachislot—The Basics

## What Are Pachinko and Pachislot?

Pachinko machines trace their origins to bagatelle boards, imported to Japan almost a century ago, in the 1920s. In the 1930s, the first pachinko hall opened for business. The prototype of modern pachinko machines, the “Masamura Gauge” machine, appeared in 1949. Subsequently, pachinko machines evolved to reflect the preferences of Japanese players. Pachinko is a game in which players manipulate a handle in order to mechanically shoot steel pachinko balls with diameters of about 11mm onto a vertically positioned board studded with numerous pins. When the balls fall into certain devices or the jackpot mouth, additional pachinko balls are won. The gameplay is similar to pinball. The main difference is that in a pachinko machine the board is nearly vertical.

Meanwhile, the roots of pachislot are said to be slot machines brought from the United States after the end of the Second World War. The 1960s saw the emergence of modified slot machines requiring a certain level of playing skill because they incorporated buttons that allowed players to stop the reels spinning. Subsequently, these machines were upgraded to the current box-cabinets and spread to pachinko halls throughout Japan. The functions and gameplay of pachinko and pachislot machines have continued to evolve, creating a uniquely Japanese form of entertainment.

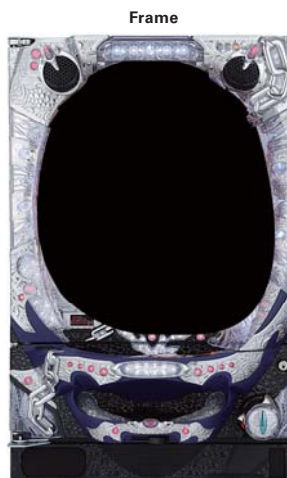
Today, machines continue to entertain fans through varied, dynamic staging based on LCDs and a range of other electronic components.

### The History of Pachinko and Pachislot

	Pachinko	Pachislot
<b>1920s</b>	Bagatelle boards arrive in Japan from overseas	
<b>1930s</b>	First pachinko hall opens for business in Nagoya	
<b>1940s</b>	Prototype of modern machines, “Masamura Gauge” appears Entertainment Establishments Control Law enforced, pachinko halls begin operating under license	
<b>1950s</b>	Pachinko machine manufacturers’ industry association, Nikkoso, established First pachinko machines with “Yakumono” appear	
<b>1960s</b>	Machines with tulip-shaped devices appear	Large slot machines imported to Japan
<b>1970s</b>	Electric pachinko machines appear	
<b>1980s</b>	Pachinko machines with digital displays, “digipachi,” appear	Pachislot machine manufacturers’ industry association, Nichidenkyo, established Box-cabinets appear and spread rapidly
<b>1990s</b>	1991 Pachinko machines with LCDs appear 1992 “CR machines” compatible with prepaid cards appear First tie-up pachinko machine appears	No. 2 through No. 4 pachislot machines appear
<b>2000s</b>	2004 Revised Entertainment Establishments Control Law enforced New-format machines appear	Games diversify with appearance of modified slot machines, CT machines, multi-line, and large-jackpot machines 2004 Revised Entertainment Establishments Control Law enforced No. 5 pachislot machines appear

## Pachinko Machine Boards and Frames

The frame is the cabinet part of a pachinko machine and has attached to it a handle, a glass frame unit, and speakers. Also, the frame physically controls the shooting and paying out of pachinko balls. Meanwhile, the board comprises liquid crystal displays (LCDs), tulip-shaped devices, and numerous pins. The board incorporates electronic components, such as boards and sensors that control gameplay, including images and win chances presented by LCDs, and payouts. Because frames can be used continuously for certain periods, pachinko hall operators can introduce new pachinko machines by purchasing boards and simply attaching them to frames already installed at pachinko halls. Also, because the price of a pachinko board is less than that of an entire machine (a frame and a board), this arrangement enables pachinko hall operators to lighten their capital investment burden. For manufacturers, sales of pachinko boards provide higher margins than sales of entire machines and help maintain market share. Therefore, board sales benefit manufacturers and pachinko hall operators.



**Frame**



**Boards**

*Pachinko*  
*SOUTEN-NO-KEN*  
© Tetsuo Hara  
& Buronson /  
NSP2001,  
Approved  
No.YDG-102  
© Sammy

**New pachinko machines can be introduced by simply attaching boards to frames**



*Dejiten CR*  
*Hokuto No Ken Toki*  
© Buronson  
& Tetsuo Hara /  
NSP1983  
© NSP2007,  
Approved  
No.YKN-101  
© Sammy

## How to Play Pachinko

### Step 1 Rent balls

After deciding which machine to play, the player rents special balls and puts them into the machine's upper tray.

### Step 2 Shoot balls

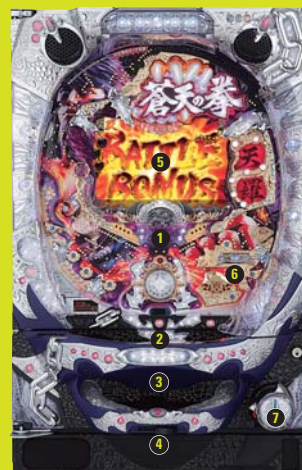
Turning the handle on the bottom right shoots the balls.

For most machines, when a ball enters the start hole underneath the LCD, the machine gives the player a chance to win a jackpot. Therefore, the player uses the handle to adjust the impetus of the balls so that as many as possible enter the start hole.

### Step 3 If the player hits the jackpot...

If the LCD screen shows the same three figures (numbers) in a line, the player wins the jackpot. When the player wins the jackpot, the jackpot mouth in the lower part of the machine opens, and the player continues shooting balls. If a large number of balls fill the lower tray, the player can use the ball remover to transfer the balls to a box.

- 1 Start hole
- 2 Upper tray
- 3 Lower tray
- 4 Ball remover
- 5 LCD
- 6 Jackpot mouth
- 7 Handle



Pachinko SOUTEN-NO-KEN  
© Tetsuo Hara & Buronson / NSP2001,  
Approved No.YDG-102  
© Sammy

## How to Play Pachislot

### Step 1 Rent medals

After deciding which machine to play, the player rents special medals.

### Step 2 Enter medals, spin the reels

The player puts three or more medals into the machine's medal slot and pushes the lever to spin the reels.

### Step 3 Halt the reels

The player halts the reels by using the stop buttons on the front of the machine cabinet.

### Step 4 Depending on the figures the halted reels show...

If the reels show the same three figures in a line, depending on the figures, the player can either spin the reels again, receive a small payout of a set number of medals, or begin a jackpot bonus game.

- 1 Main reels
- 2 Credit display
- 3 Bet button
- 4 Lever
- 5 Stop buttons
- 6 Payout display
- 7 Medal slot
- 8 Panel
- 9 Tray for receiving medals
- 10 Medal discharge



Pachislot CODE GEASS Lelouch of the Rebellion  
© SUNRISE / PROJECT GEASS-MBS  
Character Design © 2006 CLAMP  
© NAMCO BANDAI Games Inc.  
© Sammy

## THE FACTS

# Size and Competitive Conditions of Pachinko and Pachislot Machine Markets

This section focuses on the structures of the highly distinctive markets for pachinko and pachislot machines—which are unique to Japan—and the regulatory environments of these markets.

## Market Scale

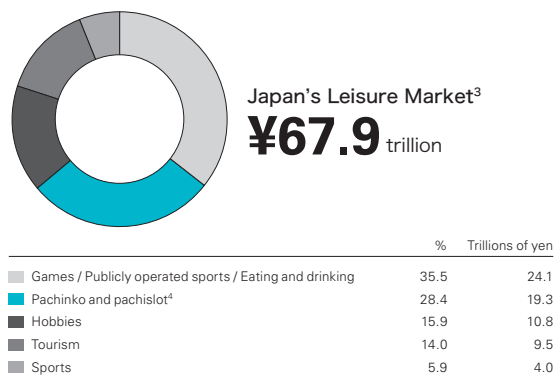
As one of Japan's flagship leisure industries, pachinko and pachislot claims a major share of the country's leisure market, and the influence of the industry is extending into various different areas. Comprising the ball and token rental fees that the pachinko halls charge, this market accounts for roughly 28.4% of the leisure market, revenues of ¥19.3 trillion<sup>1</sup>, and 16.7 million players<sup>1</sup>. Of the approximately ¥1.2 trillion<sup>2</sup> in revenues generated, the pachinko machine market represents 68.8%, or ¥825.7 billion<sup>2</sup>, and the pachislot machine market 31.2%, or ¥375.0 billion<sup>2</sup>. As well as affecting pachinko and pachislot machine manufacturers, trends in the pachinko and pachislot machine markets affect other industries. These include manufacturers of such components as LCDs, light-emitting diodes (LEDs), and sensors, who play a key role in the increasing use of advanced technologies for pachinko and pachislot machines, and manufacturers of peripheral equipment for the machines, who have developed in step with the growing automation of pachinko halls.

<sup>1</sup> 2010. Data for 2011 unavailable from research organization as of August 31, 2012.

Source: *White Paper on Leisure Industry 2011*, Japan Productivity Center

<sup>2</sup> 2011. Source: Yano Research Institute Ltd.

## Shares of Pachinko and Pachislot in Japan's Leisure Market



Source: *White Paper on Leisure Industry 2011*, Japan Productivity Center

<sup>3</sup> 2010. Data for 2011 unavailable from research organization as of August 31, 2012.

<sup>4</sup> Total amounts of hall ball and token rentals

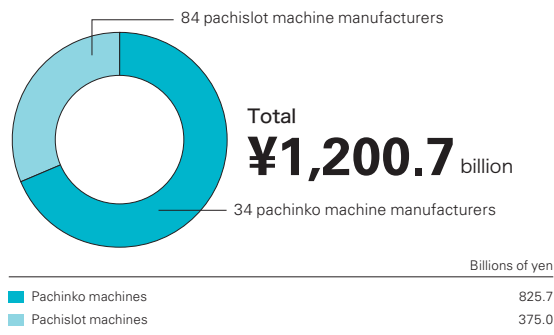
## Competitive Conditions of the Pachinko and Pachislot Machine Markets

The pachinko and pachislot machine markets comprise 34<sup>5</sup> pachinko machine manufacturers and 84<sup>6</sup> pachislot machine manufacturers. Manufacturers' shares of the market fluctuate significantly depending on whether or not they have hit titles. In recent years, orders have concentrated on a particular group of manufacturers, consolidating the standing of the leading manufacturers and making the market increasingly oligopolistic. This reflects the strengthening of a tendency among pachinko hall operators—who face tough market conditions—to choose machines and brands that have proven high utilization rates and are therefore likely to give a reliable return on investment. Consequently, companies with robust development capabilities and abundant funds for investment are advancing their positions further. At the same time, there is a growing trend toward tie-ups and mergers centered on such companies.

<sup>5</sup> As of July 31, 2012. Member companies of Nikkoso, the pachinko machine manufacturers' industry association

<sup>6</sup> As of February 28, 2011. Member companies of Pachislot Manufacturing Network

## Pachinko and Pachislot Machine Market Scale<sup>7</sup>



Source: Yano Research Institute Ltd.

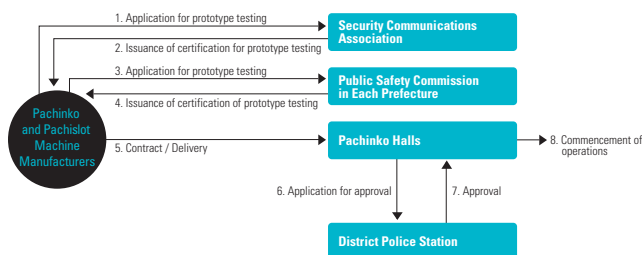
<sup>7</sup> Fiscal 2011 (settlement dates from July to June)

## Overview of the Regulatory Environment and Its Effect

Before launching a machine, manufacturers are required to navigate an approval process in accordance with the Entertainment Establishments Control Law. First, they must file an application for prototype testing with the Security Communications Association and acquire certification that elements like materials, functions, and gameplay are in conformance with the law.

Next, the machines are verified by the Public Safety Commission in each prefecture. Only then can they be supplied to pachinko halls. Before commencing operations, the pachinko hall operators must acquire approval from district police stations.

## Approval Process for Pachinko and Pachislot Machines





The Entertainment Establishments Control Law and the internal regulations of industry bodies have been revised frequently with a view to the sound development of the industry. These revisions have driven changes

in market conditions. Most recently, in July 2004, regulations pertaining to the Entertainment Establishments Control Law were revised. These revisions initiated major changes that continue to affect the market.

## Key Indicators for Analysis of Conditions in the Pachinko and Pachislot Machine Markets

Revision of regulations pertaining to the Entertainment Establishments Control Law affects the development of pachinko and pachislot machines and changes gameplay, which leads to structural change in the market as a whole. The accompanying changes in the business results of pachinko hall operators affect sales of pachinko and pachislot machines. When pachinko hall operators are in a favorable financial position and have extra capital investment capacity, they actively replace existing machines

with new ones to attract customers. Annual turnover, which shows how many times pachinko hall operators replace machines during one year, is a reliable indicator of pachinko hall operators' investment appetite and financial position. Furthermore, utilization rates—the utilization time of pachinko and pachislot machines as a percentage of business hours—clearly show the appeal of pachinko and pachislot machines, which has a direct bearing on pachinko hall operators' financial position.

### Annual Turnover

**Annual pachinko and pachislot machine unit sales ÷ Pachinko and pachislot machine installations**

Shows the number of times pachinko hall operators replace machines during one year and their capital investment appetite

### Utilization Rate

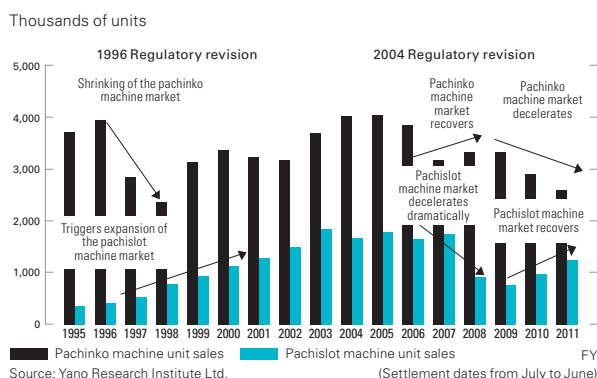
**Utilization time of pachinko or pachislot machine ÷ Pachinko hall operators' business hours**

An indication of user endorsement of pachinko or pachislot machines

## Cyclically Changing Market Conditions

In the pachinko and pachislot machine market, changes in market conditions due to revisions of regulations pertaining to the Entertainment Establishments Control Law and pachinko and pachislot machine manufacturers' innovations in response to these changes have generated cyclical trends. In the 1990s, changes in regulations and internal regulations caused a slump in the pachinko market while triggering rapid expansion of the pachislot market. The July 2004 revision of regulations pertaining to the Entertainment Establishments Control Law revitalized the pachinko machine market from 2008 to approximately 2010 but led to a downturn in the pachislot machine market. Since 2011, this trend has reversed again, with the pachislot machine market picking up as the pachinko machine market softens. For pachinko and pachislot machine manufacturers, the key to securing stable earnings lies in establishing brand appeal and product appeal for pachinko machines and pachislot machines.

## Cyclically Changing Market Conditions



**THE FACTS**

# Market Conditions for Respective Businesses

## Pachinko and Pachislot Machine Business

### Long-Term Trends—From the 1990s to 2005

After peaking in 1995, the number of players began trending downward due to casual players leaving the market because an increasing number of machines featured more complicated gameplay or strong gambling elements. As a result, the pachinko and pachislot market<sup>1</sup> entered a period of long-term decline. Fiercer competition among pachinko hall operators to attract a declining number of players and major operators' rapid advances led to a shakeout of small pachinko hall operators with less financial muscle. Consequently, the number of pachinko halls continued to decrease.

Meanwhile, unit sales of pachinko and pachislot machines remained solid, thanks to heavy demand from pachinko hall operators as they sought to secure players by replacing existing machines with new models. Also, the market generated higher revenue levels as the prices of machines continued to rise due to the incorporation of such features as LCDs. From the mid-1990s onward, however, regulatory reform caused pachinko machine installations to trend downward, while installations of pachislot machines grew because they offered a wider scope of gameplay. These pachislot machines required more playing skill and incorporated such new functions as "assist time."

### Following the July 2004 Regulatory Revision

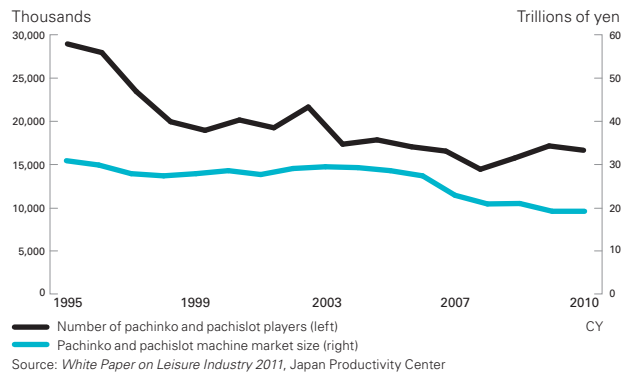
#### 1. Pachislot Machine Sales Slump, Pachinko Machine Sales Rise (from 2006 to mid-2009)

Focused on controlling excessive gambling elements, the regulatory revision of July 2004 narrowed the scope of pachislot machines' gameplay. The effect of the revision became clear from fall 2007, after the interim measures period<sup>2</sup> ended. As pachinko hall operators proceeded to replace old-format pachislot machines with those compliant with the new regulations, players' departure from the market accelerated due to the difference in gameplay. In response, pachinko hall operators actively replaced pachislot machines with pachinko machines, which were recording comparatively steady utilization rates<sup>3</sup>. This resulted in an upturn in installations of pachinko machines.

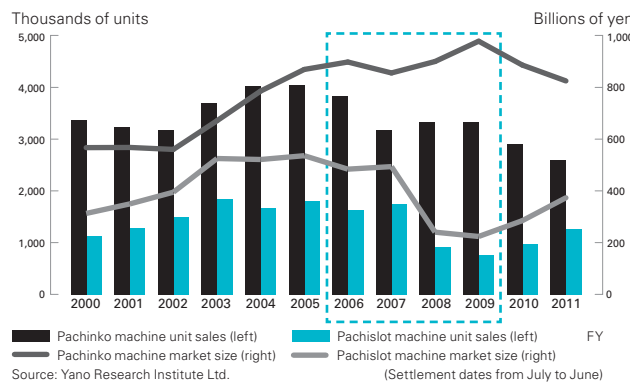
Also, although annual pachinko machine unit sales plateaued as business conditions for pachinko hall operators became tougher, the pachinko machine market continued to expand on a revenue basis. This growth was attributable to a rise in prices for machines, stemming from the increased use of advanced technologies and a hike in copyright fees that reflected fiercer competition over the acquisition of intellectual property. Faced with deteriorating profitability as the investment burden of machine replacement grew while player numbers declined, pachinko hall operators sought reliable returns by introducing machines that promised high utilization rates. This caused the market to polarize further into two groups: leading manufacturers and other manufacturers.

1 The total of pachinko hall operators' ball rental fees and token rental fees  
 2 Aiming to mitigate sudden change of conditions and investment burden of pachinko hall operators, the regulatory revision of July 2004 included a three-year interim measures period for replacing old machines with new-format machines.  
 3 The utilization time of pachinko and pachislot machines as a percentage of business hours

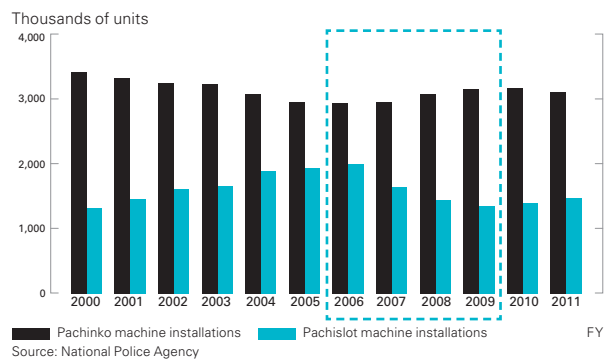
**Pachinko and Pachislot—Player Numbers and Market Size**



**Pachinko and Pachislot Machines—Unit Sales and Market Size**



**Pachinko and Pachislot Installations**



## 2. Pachinko Machine Sales Decelerate, Pachislot Machine Sales Recover (since mid-2009)

From 2008, casual players began leaving the pachinko market due to the increasing installation of pachinko machines with a strong gambling element, known as “Max-type” machines, which promised a comparatively early return on investment. In response, pachinko hall operators adopted a strategy of lowering ball rental fees called “one yen pachinko,” while manufacturers introduced pachinko machines with a weaker gambling element, called “amadigi” with a view to broadening the base of players.

Although lowering ball rental fees increased utilization rates, in the short-term it led to a decline in sales per machine for hall operations, which worsened their business results. As the sudden drop in annual turnover<sup>4</sup> shows, the softening of replacement demand for new pachinko machines—which had underpinned the market—became more conspicuous from the second half of 2009.

Meanwhile, demand from pachinko hall operators for pachislot machines began to rise thanks to manufacturers’ continued development efforts, which created pachislot machines with gameplay that earned player support while remaining within the bounds of regulatory reforms. The recovery of pachislot machines since bottoming in fall 2007 is clear from such indicators as annual turnover, utilization rates, and average gross profit per machine per day<sup>5</sup>. Sluggishness in the pachinko machine market, accompanied by favorable conditions in the pachislot machine market, continues in the current fiscal year.

<sup>4</sup> Annual turnover = Annual unit sales ÷ Machine installations

<sup>5</sup> Average gross profit per machine per day for pachinko hall operators

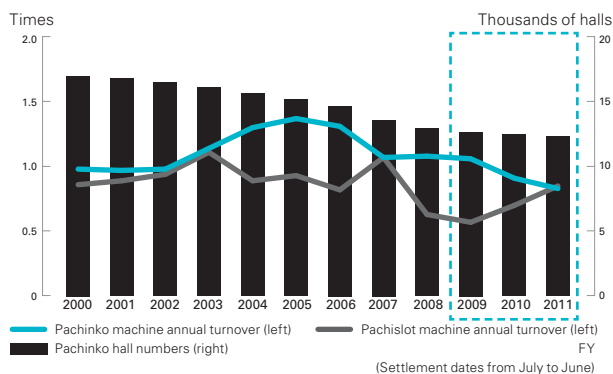
### Summary of Market Conditions

- The long-term decline in the number of players has not changed significantly. Pachinko hall operators continue to face challenging business conditions.
- Aiming to enhance capital investment efficiency, pachinko hall operators are increasingly favoring particular manufacturers and machine models with brand appeal likely to realize high utilization rates.
- While demand is growing for pachislot machines, which offer comparatively high utilization rates, demand for pachinko machines is weakening.
- An oligopoly comprising manufacturers with abundant development funds and advanced development capabilities is becoming more entrenched.

### Keys to Prevailing in Competition with Other Manufacturers

- Develop machine models with gameplay that helps increase the number of players
- Establish a balanced product portfolio able to use cyclical changes in market conditions as a tailwind
- Acquire market share efficiently by exploiting collaboration among Group companies to realize economies of scale
- Build production and supply capabilities able to cater to short-term intensive demand

## Annual Turnover\* and Pachinko Hall Numbers

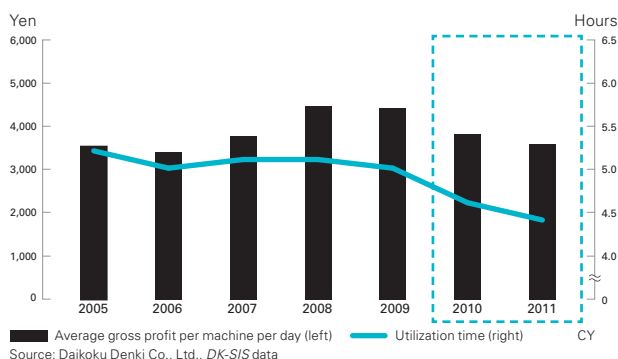


\* Annual turnover = Annual unit sales ÷ Machine installations

Sources: The Company has calculated annual turnover based on data from the National Police Agency and Yano Research Institute Ltd. Pachinko hall numbers are from the National Police Agency.

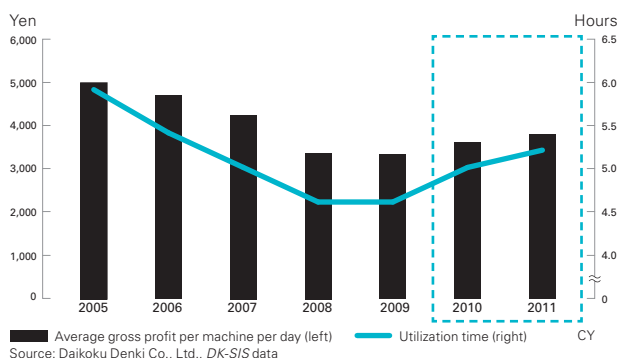
## Utilization of Pachinko and Pachislot Machines

### Pachinko Machines



Source: Daikoku Denki Co., Ltd., DK-SIS data

### Pachislot Machines



Source: Daikoku Denki Co., Ltd., DK-SIS data

**THE FACTS**

Market Conditions for Respective Businesses

**Amusement Market** (amusement arcade machines / amusement center operations)

**Bottoming Out of the Amusement Center Operations Market Becomes Clearer**

The amusement center operations market has been contracting since fiscal 2007. However, the trend is gradually turning around. In recent years, amusement centers operators have responded to the shrinking market by closing unprofitable amusement centers and increasing operational efficiency. As a result, the year-on-year rate of decline in net sales from amusement center operations is slowing: while for fiscal 2009 it was above 10%, it was only 1.7% for fiscal 2010. Although conditions remain tough, there are signs that the market is bottoming out. Year-on-year net sales of existing amusement centers have been declining since fiscal 2004. However, although this figure was down 11.8% for fiscal 2009, it decreased only 2.7% for fiscal 2010, indicating a gradual bottoming out. This was attributable to a 4.5% year-on-year rise in revenues from crane games, which supported the market, and the contribution of new players. Furthermore, amusement center operators gained attention in a new role as facilitators of community-building efforts focused on senior citizens.

The financial position of amusement center operators, which had remained tough, is improving steadily due to the bottoming out of net sales and the revamping of earnings structures. With major amusement center operators taking the lead, capital investment appetite is beginning to return. This is putting a brake on a vicious circle whereby delay in revitalizing amusement centers was driving players out of the market.

**Amusement Arcade Machine Sales Up for First Time in Three Years**

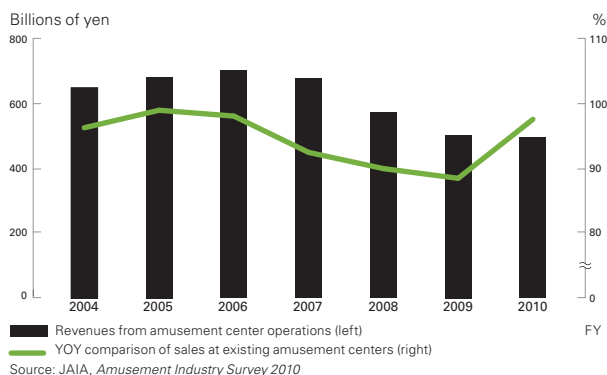
Because the capital investment of amusement center operators affects it directly, the market for amusement arcade machines saw year-on-year declines in sales for three consecutive years from fiscal 2007. However, in fiscal 2010 sales were up 2.1% year on year. Partly due to a rebound from the significant 13.5% year-on-year drop in fiscal 2009, sales of almost all product categories rose from the previous fiscal year. Higher product sales indicate that amusement center operators, centered on major companies, are regaining an appetite for capital investment.

In recent years, amusement arcade machine manufacturers have taken a variety of steps to alleviate amusement center operators' investment burden. Examples of these initiatives include standardizing machine cabinets, adopting systems that enable amusement center operators to upgrade content by simply replacing computer graphics boards or by downloading new content, and introducing multipurpose computer graphics boards that reduce cost. In addition, revenues from revenue-sharing business models, in which manufacturers sell amusement arcade machines at low prices and share revenues from machine utilization with amusement center operators, have grown rapidly—rising 2.3 times compared with fiscal 2007. This business model is likely to become even more popular because, at the same time as mitigating amusement center operators' capital investment burden, it promises to secure long-term earnings for amusement arcade machine manufacturers.

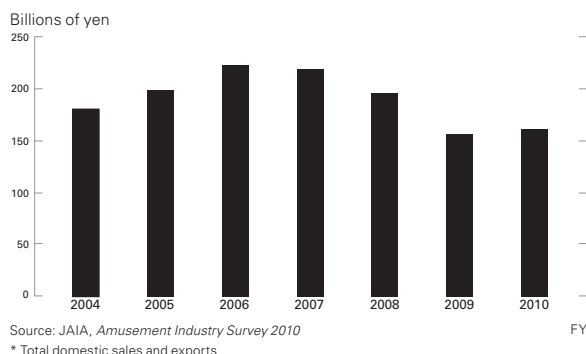
Amusement center operators and amusement arcade machine manufacturers are collaborating to reinvigorate the industry as a whole by establishing new usage fees and rates that diversify earnings sources and by developing products that attract new players.

All market data in the text is from JAIA, Amusement Industry Survey 2010.

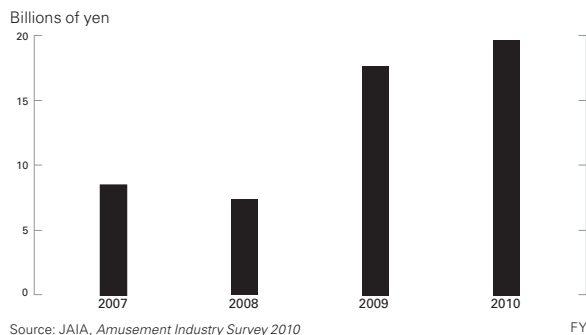
Revenues from Amusement Center Operations / YOY Comparison of Sales at Existing Amusement Centers



Amusement Arcade Machine Sales\*



Revenues from Content Fees / Revenue-Sharing Business Models



## Home Video Game Software Market

### Game Content for New Platforms Leading the Market

In 2011, the global video game market, including video game software and game consoles, is estimated to have accounted for revenues of ¥3.63 trillion<sup>1</sup>, down 8.3% from the previous year. Partly reflecting a transition among home video game consoles and handheld game terminals to a new generation of platforms, the video game software and game console market saw steep year-on-year decreases in all regions: 5.9%<sup>1</sup> in Japan, 8.4%<sup>1</sup> in the United States, and 8.8%<sup>1</sup> in Europe. In the packaged game software market, popularity concentrated on particular titles, further reinforcing the oligopoly among software publishers. Also, video game content for such new platforms as SNS, smartphones, and online games became the new driver of the global game content market, accounting for ¥3 trillion of the ¥5.13 trillion<sup>1</sup> in revenues this market generated.

### The Popularity of Smart Devices Spurs Growth of the Social Game Market

Japan's online game content market grew 8.0% year on year, to ¥239.9 billion<sup>2</sup>. In this market, social games are growing at a phenomenal pace. The social game market has been expanding rapidly since 2008 in Japan. This fast growth in a short period is the result of the explosive proliferation of such smart devices as smartphones and tablet PCs combined with the upgrading of telecommunications infrastructure. Domestic shipments of smartphones rose 2.7 times year on year, to 23.4 million units<sup>3</sup>—accounting for the majority of mobile phone shipments for the first time. Numerous companies are competing fiercely in this market because it allows them to supply content worldwide easily through a common operating system, while an open environment for basic development lowers the barrier to market entry.

### Video Game Industry Hurries to Convert Business Model

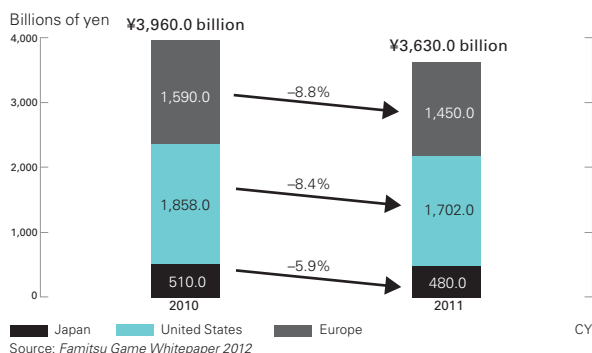
Software publishers are very quickly shifting the main focus of their businesses from existing markets, which are contracting, to the content market for new platforms. The structure of this market differs greatly from that of the packaged game software market, where companies' involvement ends after selling products. In the content market for new platforms, however, success depends upon a company's ability to detect changes in the market sensitively after distributing content and to flexibly adjust to it accordingly. Aiming to shorten development lead times and cater to a diverse range of players, software publishers are building business models suited to the new market's structure by establishing subsidiaries or dedicated divisions and pursuing mergers and acquisitions (M&As). Moreover, to replace games with excessive gambling elements, which have become a social issue, companies are searching for content that will drive market growth. In Asia, the online game market promises significant growth. Therefore, companies are advancing measures to open up this market.

1 Source: Famitsu Game White Paper 2012

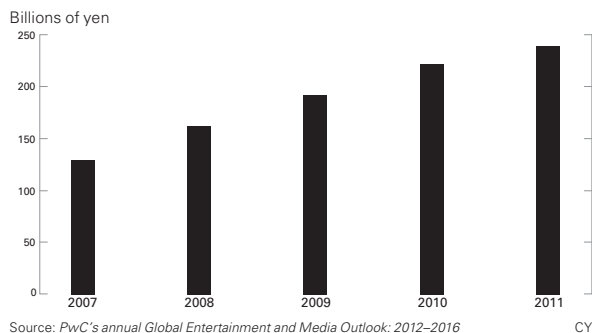
2 Source: PwC's annual Global Entertainment and Media Outlook: 2012–2016

3 Source: MM Research Institute, Ltd.

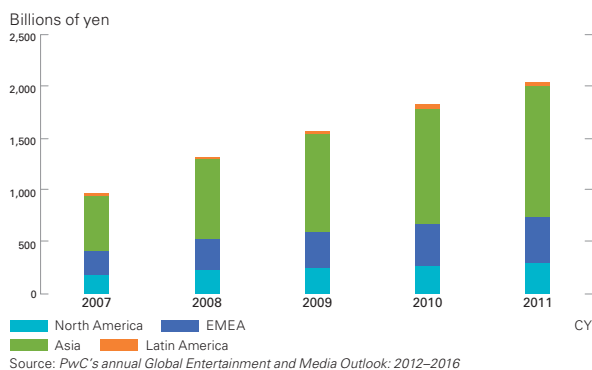
### Global Video Game Market (consoles + software)



### Online Game Market in Japan



### Global Online Game Market



**THE FACTS**

Market Conditions for Respective Businesses

**Toy and Animation Markets**

**Japan's Toy Shipment Market**

**Challenging Conditions Set to Continue over the Medium-to-Long Term**

In fiscal 2010, Japan's toy shipment market, comprising eight main product categories and excluding home video game consoles and software, grew 2.3% year on year, to ¥331.2 billion, thanks to brisk sales of toys for boys. For fiscal 2011, although toys for boys are likely to continue performing solidly, Japan's toy shipment market is expected to edge down 0.5% year on year, to ¥329.6 billion. Due to the Great East Japan Earthquake and an increasing emphasis on saving power, sales of analog games, which had been contracting, have grown dramatically.

Although the industry is pursuing initiatives to develop demand for products targeting adults, the majority of products target children. Therefore, given society's aging over the medium-to-long term, the market is unlikely to expand significantly. In response, the industry is expected to step up rollouts in markets overseas and accelerate efforts toward tie-ups and mergers.

**Animation Market**

**Hit Movies Drive the Market**

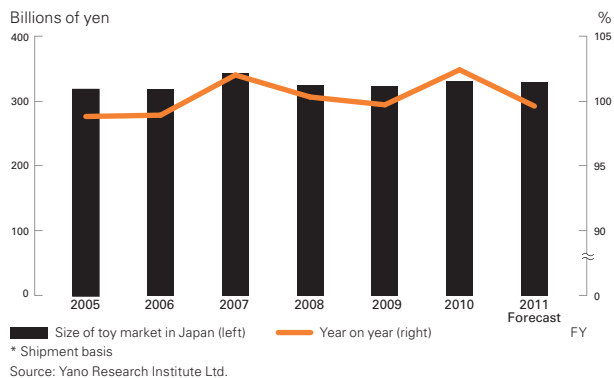
In 2010, the animation market grew 5.8% year on year, to ¥229.0 billion. Animation hits at movie theaters have dominated the market in recent years. This trend continued in 2010, with such hits playing a central role in the animation market. As well as popular Japanese animation, in 2009 and 2010 Western animation hits helped grow the overall animation market by expanding the markets for movie theater and video animation.

As for terrestrial broadcasting, the market is contracting. Since peaking in 2006, the number of animation series broadcast on television has been declining. On the other hand, the pay-TV market is continuing to expand as the animation channels of satellite and cable TV services attract more viewers. In 2011, viewer numbers are expected to increase because a new satellite TV service has begun broadcasting.

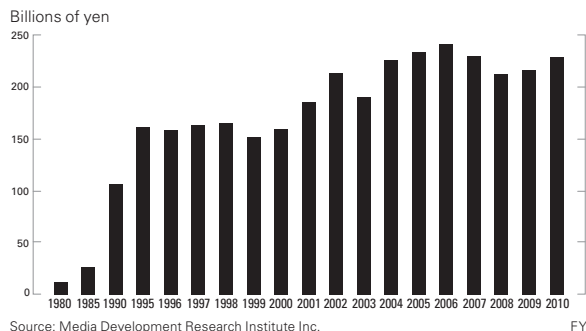
In video sales, animation is heightening its presence by growing as the overall video market declines.

While the market for distribution services for PCs is flat, the market for distribution services for mobile terminals is growing. Furthermore, with the rapid spread of smartphones, the viewing of videos through mobile terminals is likely to expand even further.

**Toy Market in Japan\***  
(excluding home video game consoles and software)



**Animation Market in Japan**  
(for movie theaters, television, DVDs, and network distribution)



# Market Data

<b>Number of Pachinko Halls</b>					Number of halls
CY	2007	2008	2009	2010	2011
Number of pachinko halls with pachinko machines installed	12,039	11,800	11,722	11,576	11,392
Number of pachinko halls with only pachislot machines installed	1,546	1,137	930	903	931
Total	13,585	12,937	12,652	12,479	12,323

Source: National Police Agency. Number of pachinko halls with pachinko machines installed includes halls that combine installations of pachinko machines, pachislot machines, arrange-ball machines, and other machines.

<b>Pachislot Machine and Pachinko Machine Sales, Installed, and Market Scale</b>						
CY / FY*		2007	2008	2009	2010	2011
Pachislot machines	Machine sales (units)	1,744,308	913,094	766,094	979,794	1,259,924
	Machines installed (units)	1,635,860	1,448,773	1,347,176	1,390,492	1,474,838
	Market scale (millions of yen)	502,501	247,860	225,869	286,700	375,054
Pachinko machines	Machine sales (units)	3,173,725	3,339,146	3,332,984	2,900,286	2,602,760
	Machines installed (units)	2,954,386	3,076,421	3,158,799	3,163,650	3,107,688
	Market scale (millions of yen)	868,623	921,338	985,227	886,914	825,714

Sources: National Police Agency (machines installed) and Yano Research Institute Ltd. (machine sales and market scale)

\* Number of machines installed is on a calendar year basis. Number of machine sales and market scale information is on a fiscal year basis (settlement dates from July to June).

<b>Amusement Machine and Amusement Center Operations Markets</b>					
FY	2006	2007	2008	2009	2010
Net sales of amusement machines (millions of yen)	223,357	219,061	196,164	169,632	173,167
Net sales from amusement center operations (millions of yen)	702,857	678,099	573,104	504,271	495,767
Number of amusement centers	23,613	22,723	21,688	19,213	18,638
Year-on-year comparison of sales at existing amusement centers (%)	97.8	92.2	89.7	88.2	97.3

Source: JAIA, *Amusement Industry Survey 2010*

\* The number of amusement centers is the total of category 8 centers and non-category 8 centers classified by the Entertainment Control Law.

<b>Global Shipment of Home Game Software</b>					Billions of yen
FY	2007	2008	2009	2010	2011
Software	848.6	1,024.3	758.6	670.5	530.9
Hardware	2,087.7	1,908.3	1,490.8	1,126.9	926.4

Source: CESA GAME White Paper 2012

<b>Global Online Game Market</b>					Billions of yen
CY	2007	2008	2009	2010	2011
North America	176.7	228.3	245.8	267.4	293.9
EMEA	233.9	296.5	349.0	402.8	449.2
Asia	533.5	771.4	945.3	1,117.7	1,259.2
Latin America	21.6	28.3	33.2	38.6	44.4
Total	965.7	1,324.5	1,573.3	1,826.5	2,046.7

Source: PwC's annual *Global Entertainment and Media Outlook: 2012-2016*

Calculated using exchange rate of US\$1 = ¥80