We would now like to begin the Financial Results Briefing Session of SQUARE ENIX HOLDINGS (the “Company”) for the fiscal year ended March 31, 2020 (“FY2020/3”).

Today’s presenters are:
Yosuke Matsuda, President and Representative Director
and
Kazuharu Watanabe, Chief Financial Officer.

First, Mr. Watanabe will give an overview of the Company’s financial results for FY2020/3, and then Mr. Matsuda will discuss the progress made by each of the Company’s business segments.

Good afternoon. I’m Kazuharu Watanabe. I will be presenting an overview of the Company’s financial results for FY2020/3.

In FY2020/3, the Company booked net sales of ¥260.5 billion (-¥10.7 billion YoY), operating income of ¥32.7 billion (+¥8.1 billion), ordinary income of ¥32.0 billion (+¥3.6 billion), and net income attributable to parent company shareholders of ¥21.3 billion (+¥2.0 billion).

The plans, forecasts, strategies and ideas described in this material are descriptions of forecasts of future results. These descriptions rely on information available as of the date of production of this material and are based on assumptions and judgment made by the Company’s management. Readers are advised not to rely solely on these forecasts. Readers should also not assume that these forecasts are accurate or valid information, even after the date of public release. There are many factors that may cause actual results to vary considerably from the forecasts, and in some cases actual results may be inferior to forecasts. The information on the future forecasts described in this material is current as of May 13, 2020. The company is not obliged to update or correct forecasts concerning the Company’s future results, including forecasts or outlook, if new information becomes available and/or events occur after May 13, 2020.
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I will next break down our results by segment. The Digital Entertainment segment posted net sales of ¥188.6 billion (-¥15.9 billion YoY) and operating income of ¥32.7 billion (+¥8.1 billion).

The HD Game sub-segment benefitted from the launch of “DRAGON QUEST XI S: Echoes of an Elusive Age – Definitive Edition” and the booking of advanced shipments of “FINAL FANTASY VII REMAKE,” which was launched in April 2020. However, sub-segment sales fell YoY due to the high bar set in the previous year by the release of multiple major new AAA titles. Furthermore, additional sales of titles released in the previous year were weak, and we booked write-downs on the content production account, resulting in an operating loss for the HD Game sub-segment.

The MMO sub-segment saw both net sales and operating income rise YoY due to the release of expansion packs for “FINAL FANTASY XIV” and “DRAGON QUEST X” and the resulting rise in monthly paying subscriber numbers.

Net sales and operating income rose YoY in the Games for Smart Devices/PC Browsers sub-segment thanks to strong performances by “Romancing SaGA Re:univerSe” and “DRAGON QUEST WALK,” the latter being launched in September 2019.

The Amusement segment posted net sales of ¥45.6 billion (-¥600 million YoY) and operating income of ¥1.4 billion (-¥500 million). Arcade operations were solid, but a decline in amusement machine sales resulted in YoY declines in net sales and operating income.

The Publication segment booked net sales of ¥19.4 billion (+¥5.2 billion YoY) and operating income of ¥7.2 billion (+¥3.1 billion). Sales in digital formats, such as from the “MANGA UP!” manga application and e-books, rose sharply. Sales in printed formats were also brisk, resulting in YoY growth in net sales and operating income.
The Merchandising segment posted net sales of ¥8.7 billion (+¥1.4 billion YoY) and operating income of ¥1.0 billion (+¥100 million). The YoY rise in net sales and operating income was due to the release of new character goods based on our owned IP.

This concludes my overview of our financial results.

I am Yosuke Matsuda. I will be discussing conditions in 4Q FY2020/3 and thereafter.

In the Games for Smart Devices/PC Browsers sub-segment, “WAR OF THE VISIONS: FINAL FANTASY BRAVE EXVIUS,” which we launched in November 2019, continued to deliver a strong performance in 4Q as it had in 3Q. In addition, digital sales, such as those from our “MANGA UP!” manga application were strong in the Publication segment.

By contrast, conditions were challenging at the Amusement segment. In particular, the coronavirus outbreak reduced March sales at existing arcades to 70% of the previous year’s level, and we expect conditions to remain challenging in FY2021/3 as we comply with municipalities’ requests for closures of arcade facilities.

At the HD Game sub-segment, we decided to produce and ship fewer packaged products of “FINAL FANTASY VII REMAKE,” which was launched on April 10, because of the impact on distribution channels we anticipated from the coronavirus. As a result, sales of disks were lower than we had initially expected, but digital sales have gotten off to a good start, and we are hopeful about how sales will continue to
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We refrain from setting consolidated forecasts for FY2021/3, as of yet, because of the impact the coronavirus may have on our business as a whole, which limits our ability to estimate earnings for the following primary reasons.

In order to estimate the impact on Amusement segment earnings, we need to know when our arcade facilities will re-open and what operations will look like thereafter, which is difficult to predict at present.

In terms of game development as well, we have made good progress on enabling our internal resources to work from home, but we are beginning to face some issues in terms of the work we outsource, including voiceover audio recording and motion capture. As such, there is risk of impact to our development schedule going forward.

We will disclose earnings forecasts as soon as we are able to make forecasts appropriately and reasonably.

Our objective under the mid-term plan that concludes in FY2021/3 has been to create a business structure capable of consistently generating net sales of ¥300-400 billion and operating income of ¥40-50 billion.

We have successfully created a structure whereby we are able to maintain net sales in excess of ¥300 billion, but we have yet to reach the point that we can consistently deliver operating income in this range, so we will work to take our efforts to the next level.
I will next discuss our strategy for the way ahead.

Over the short term, we will work to further increase the percentage of sales we generate digitally and to develop content and services from which we can expect recurring earnings contributions, such as microtransactions and GAAS (Games as a Service).

Over the medium-term, we will develop titles and offer services for cloud streaming, which we believe is poised to take off going forward.
Q: If you were to release your major HD game titles on schedule and exclude any downside factors to earnings from the coronavirus, would you still find it difficult to achieve operating income of ¥40 billion or more in FY2021/3?
A: While we will strive for operating income of ¥40 billion or more in FY2021/3, it is difficult at present to arrive at a quantitative estimate of the impact the coronavirus is likely to have on our business. As such, we intend to release earnings guidance when such assessments become feasible.

Q: Other than increasing the percentage of digital sales, do you have any initiatives in mind for improving the profitability of the HD Game sub-segment?
A: Everything comes down to the quality of our games. We are going to work hard to ensure we develop high-quality games that our customers can enjoy over a long period of time.

Q: How satisfied are you with initially having sold 3.5 million units of “FINAL FANTASY VII REMAKE”? Do you have any plans to offer it on additional platforms?
A: We are pleased that we were able to top 3.5 million units given that we chose to produce and ship fewer physical disks due to the impact that we foresaw from the coronavirus outbreak. Disk sales were lower than we had initially anticipated, but growth in digital sales increased their percentage of the whole, which we expect to lead to a better gross margin. We will refrain from commenting on the possibility of offering the title on additional platforms for now.

Q: Could you share the breakdown of the ¥7.9 billion write-downs on inventory assets?
A: Of the ¥7.9 billion, ¥7.5 billion were write-downs on the content production account. Of those, ¥5.7 billion were on the HD Game sub-segment and the remainder on Games for Smart Devices/PC Browsers sub-segment and others.

Q: E3 was cancelled for 2020, but do you have any plans to host events of your own around the same time to unveil new titles?
A: Our Group will not be live streaming its own event because the coronavirus pandemic will prevent us from assembling all the visual assets from the various studios and titles. We intend to unveil new titles going forward on an individual basis at the appropriate timing.
Q: Do you have any initiatives planned to grow additional sales of “FINAL FANTASY VII REMAKE?”

A: Capturing new players is key. I will refrain from going into the details, but we have plans for initiatives to capture players throughout the year, so please keep an eye on our progress. I also note that we will not engage in any marketing strategy that relies solely on pricing.