

08-Feb-2018

# NEXON Co., Ltd. (3659.JP)

Q4 2017 Earnings Call

## CORPORATE PARTICIPANTS

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

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## OTHER PARTICIPANTS

Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Han-Joon Kim

*Analyst, Deutsche Bank AG (Hong Kong)*

Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Thomas Kwon

*Analyst, Daiwa Securities Capital Markets Korea Co., Ltd.*

Keiichi Yoneshima

*Analyst, Credit Suisse Securities Japan Ltd.*

Haruka Mori

*Analyst, JPMorgan Securities Japan Co. Ltd.*

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## MANAGEMENT DISCUSSION SECTION

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Thank you for taking the time out of your busy schedules to attend Nexon's earnings presentation. This presentation will be streamed live on the Internet including the Q&A session.

I am Yuki Hayakawa, the Head of Public Relations, and I will be your moderator today. First, let me introduce the attendees. From your right, Owen Mahoney, our Representative Director, President and CEO; Shiro Uemura, our Representative Director and CFO; last but not least, Maiko Ara, the Head of Corporate Development and IR.

Now, let me explain today's program. First, President Mahoney will give you an overview of the full-year 2017 and introduce highly anticipated new titles in English. Next, CFO Uemura will give you some highlights for the full year and Q4 of 2017 as well as Q1 outlook of 2018 in Japanese. We would then have Q&A session. The presentation will take about 30 minutes, and we have about 25 minutes for Q&A. Today's presentation will be available on our IR website within a few days. Lastly, please make sure that you have all the handouts: first, today's investor presentation material, consolidated financial results and three press releases, five documents in total. Let us know if you are missing any documents.

Do you have all the documents? Now, let us begin our presentation. President Mahoney, please.

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Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

Thank you all for joining Nexon's 2017 fourth quarter earnings presentation today. Thank you also for those of you who are joining us remotely through the live broadcast. Today, we're extremely happy to report record-breaking

annual results for the full-year 2017 in which our revenues were up over 25% year-over-year. Our operating income more than doubled, and our net income nearly tripled from 2016. This excellent performance was driven by our key titles across the regions as well as new games we launched during 2017.

We also recorded our highest Q4 revenues and operating income ever. Uemura-san will be reviewing our results in more detail shortly. Dungeon&Fighter had an outstanding year and continues to be a powerful driver of our business. The China service for D&F will be celebrating its 10th anniversary in 2018. The sustained robust growth of this franchise has continued to surprise many industry observers, showing annuity-like performance year after year that much more closely resembles a Software-as-a-Service model than a typical entertainment industry pattern. From very early on, our focus has been on the long-term growth of this franchise rather than harvesting short-term returns. This is an approach that has served our financial performance by, first and foremost, serving our customers.

As a result, D&F has achieved double-digit percentage year-over-year growth worldwide in 2017, which is particularly noteworthy given its strong double-digit percentage growth in 2016. And to give you a sense of size, the largest movie franchise of all time is Star Wars, going back to 1977, and industry estimates for its life-to-date box office are \$9 billion. Today, D&F's life-to-date revenues are bigger than life-to-date box office of Star Wars franchise, and it's just one quarter as old. On February 1, we introduced the Lunar New Year update to Dungeon&Fighter in China, and it's off to a very strong start. We look forward to giving you the full report on the performance to this update next quarter.

MapleStory also had a great year in 2017 with its global revenues recording double-digit percentage growth year-over-year. Like Dungeon&Fighter, MapleStory's sustained growth illustrates an important point about Nexon's approach. The game has continued to perform well fundamentally because our live game teams have taken the long view, focusing on bringing its millions of customers back over a period of many years rather than driving near-term revenues. Our focus on long-term value for customers over short-term revenue has enabled us to deliver robust annuity-like returns for our shareholders over many years. It is a key example of how Nexon thinks differently about games and about product life cycles.

So, the great Q4 in 2017 is a result not of decisions we made in the last few months or few quarters but about hard decisions we made a year or more ago. So, now, let's talk about some decisions we have been making more recently as they will fuel our growth in the coming years. As you recall, we purchased Pixelberry, the California developer of Choices, in the fourth quarter. The early integration between Nexon and Pixelberry has been going very well, and we've been integrating our advanced data analytics platform with Pixelberry's game operation servers.

Choices delivered great results in the fourth quarter and is off to an excellent start in 2018. We think Choices represents a whole new form of mass media, a merging of games and storytelling targeted at an embarrassingly underserved market. Both the game and the company exemplify the kind of innovative thinking that is the hallmark of all great advances in games in broader media.

And while most of the rest of the games industry seems intent on copying either the specific gameplay or the business model of even the most basic innovation, we believe that sustainable growth can only come from relentlessly reinventing our business including the definition of what a game is. Nexon can do this because of our massive consistent franchises are able to fund the [indiscernible] (00:07:52) development risk-taking required to make tomorrow's hits. Like many of Nexon's and the industry's biggest hits, the game's surface level simplicity you see on the video masks great depth underneath the surface.

Okay. The next game to highlight is OVERHIT. We launched the game on November 28 in Korea. OVERHIT was developed by our Korean partner, NAT Games, which is also the developer of the previous game and the series HIT. We're very happy with the early results in Korea, and we'll be launching in other regions soon, starting with Japan.

And finally, I'd like to show you some gameplay video of Durango, which we launched two weeks ago in Korea. It is off to an excellent start. 2.5 million people pre-registered for the game in Korea, the highest number of pre-registrations for any Nexon game in Korea and fully 5% of the entire Korean population. It immediately took the number four ranking on Apple and Google app stores prior to any featuring and despite relatively low monetization.

Durango is a pioneering game, a fully open-world MMORPG on mobile. The game is set in a primitive universe inhabited by dinosaurs. Players explore, hunt, collaborate, and fight in an effort to survive and build societies both with and against other players. Durango expands the definition of what a mobile game can be. There's nothing like it on mobile anywhere in the world.

Durango reflects our development team's relentless focus on thinking differently about games and about reaching beyond the typical conventions and genres in our industry, and you'll see many more of our exciting products launching around the world in 2018.

Supporting all these launches and our ongoing growth, we have made some changes in our management team. We named Jiwon Park, formerly CEO of NEXON Korea, as Global Chief Operating Officer, a newly created role in Nexon Group. He will oversee the global business and operations with primary focus outside of Korea. Jung-hun Lee, formerly Vice President of Business of NEXON Korea, has now been nominated for the role of CEO of NEXON Korea. These are two of our best executives who have made enormous contributions to building Nexon. Jiwon has expanded NEXON Korea's game lineup and rebuilt its live operations capability. Jung-hun has held various leadership positions in NEXON Korea and led the launch and success of the FIFA Online 3 franchise as well as the successful launch of various mobile games including HIT, Dark Avenger 3, AxE, and OVERHIT. These changes are designed to grow our organization's capabilities as we grow our product lineup.

Lastly, I'd like to touch on our business in the West. We have recently made several changes to our Western organization by centralizing and integrating some of our operations there to better serve our Western player base. Previously, we had three entities responsible for operations in the West: Nexon America for PC publishing in North America, NEXON Europe for PC publishing in Europe, and NEXON M for mobile publishing in the U.S. and the EU. We've now consolidated Nexon America and NEXON Europe, and all of our future PC and console publishing operations in the West will be managed out of Nexon America.

Additionally, last year, we set up OC Studio in Irvine, California to enable us to better develop games that will resonate well with players in the West. So, going forward, our operations will be serviced out of two locations, NEXON M and Nexon America, and games will be developed at OC Studio in addition to Big Huge Games and Pixelberry.

Our industry is rapidly changing with technology advances that could alter our business massively over the next few years. We need to quickly adapt, and these operational changes will put us on a strong footing to do so.

With that, I'll turn it over to Uemura-san to discuss the fourth quarter and full-year results and the Q1 2018 outlook.

## Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Thank you. CFO Uemura, please continue.

## Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

Now, let's move on to FY 2017 results. FY 2017 revenues were ¥234.9 billion, up 28% year-over-year on an as-reported basis. On a constant currency basis, full-year revenues were up by 25% year-over-year. FY 2017 operating income was ¥90.5 billion, up 123% year-over-year on an as-reported basis and up 123% year-over-year on a constant currency basis. FY 2017 net income was ¥56.8 billion, up 182% year-over-year on an as-reported basis and up 191% year-over-year on a constant currency basis.

Continuing on to the Q4 results. For additional details, please see the Q4 2017 investor presentation included in the handouts. We were pleased that revenues were at the high end of our outlook for the quarter. For Q4, revenues were ¥52.7 billion, up 22% year-over-year on an as-reported basis and up 14% year-over-year on a constant currency basis. Operating income was ¥11.8 billion, and net loss was ¥2.2 billion, both of which were below our outlook.

Revenues were at the high end of our guidance primarily driven by Dungeon&Fighter in China, which performed well throughout the quarter. Operating income was below our outlook. It was positively impacted by the revenue outperformance of high-margin China Dungeon&Fighter as well as lower-than-planned HR costs and CSR donations. But those factors were offset by the impairment loss on items including goodwill on subsidiaries, prepaid royalties for publishing titles, and game IP.

We had a net loss of ¥2.2 billion, which was below our outlook primarily due to the FX loss of ¥15.5 billion on our U.S.-dollar denominated cash deposits and account receivables related to the appreciation of the Korean won against the U.S. dollar during the fourth quarter.

Revenues from our China business in the fourth quarter exceeded our expectations. Again, this was mainly driven by Dungeon&Fighter, which showed strong performance throughout the quarter. While we did not conduct any large-scale updates in the fourth quarter, we introduced multiple in-game events that were well-received by users. In the fourth quarter, revenues typically decrease quarter-over-quarter from the third quarter, which is seasonally strong driven by summer vacation and the National Day holiday. This was true again this year with revenues, ARPPUs, MAUs and paying users for Dungeon&Fighter in China decreasing quarter-over-quarter. Revenues, ARPPUs, and paying users for Dungeon&Fighter in China in the fourth quarter grew year-over-year, while MAUs slightly decreased year-over-year. In addition to Dungeon Fighter, MapleStory2, which began its open beta pre-test in September also contributed to the year-over-year growth in China.

Revenues from Korea in the fourth quarter were at the low end of our outlook. PC revenues decreased year-over-year primarily due to a year-over-year decrease in revenues from Dungeon&Fighter, which saw particularly strong performance in Q4 last year driven by successful update in the second half of 2016.

On the other hand, mobile game revenues grew significantly year-over-year driven by contributions from OVERHIT, which was launched on November 28 as well as AxE and Dark Avenger 3. The year-over-year increase in revenues from mobile games more than offset the revenue decrease from PC online games. As a result, revenues for the Korea business as a whole grew year-over-year.

Our North America business grew year-over-year in the fourth quarter primarily due to contribution from Pixelberry Studios, our new subsidiary in the region. We completed our acquisition of Pixelberry in late November, and we consolidated about a month of its [ph] PL (00:17:21) in the fourth quarter.

Now, turning to our Q1 2018 outlook. For the first quarter of 2018, we expect revenues in the range of ¥81.9 billion to ¥89.8 billion, representing a 10% to 20% increase year-over-year on an as-reported basis and a 5% to 15% increase year-over-year on a constant currency basis. We expect Nexon Group revenues to increase year-on-year primarily driven by a strong performance in China and an increase in revenues from North America, driven by contributions from Pixelberry Studios, which we expect to partially be offset by revenue decreases in Japan, Europe, and other regions. We expect operating income to be in the range of ¥45.1 billion to ¥52.3 billion. We expect net income to be in the range of ¥40.4 billion to ¥46.3 billion.

In China, we conducted a large-scale content update of our key PC online game, Dungeon&Fighter, on February 1 in time for the Lunar New Year, and the game is off to an extremely strong start. We expect revenues to grow year-on-year, driven by the extremely strong start of the Lunar New Year update, accompanied by the strong sales of [ph] Avatar (00:18:42) package. In addition, we expect MapleStory2 to contribute as a driver for year-on-year growth in China.

As for large-scale update scheduled for Dungeon&Fighter in 2018, there are no big changes from 2017, and we expect to conduct them at a pace of about one to two updates per quarter. Please refer to the investor presentations for the information on scheduled updates.

In Korea, we expect PC online game revenues to decrease year-on-year mainly due to the revenues from key titles including the FIFA Online 3 and Dungeon&Fighter decreasing year-on-year, partially offset by the new PC online title, Moonlight Blade, which started its open beta test in January and full launch in February, [ph] merely (00:19:32) contributing to revenues.

In contrast, we expect mobile revenues to increase year-on-year with contributions from OVERHIT and AxE, which launched in the second half of 2017 as well as Yulhyulgangho M and Durango, which launched in January 2018. Overall, we expect Korea revenues to be flattish year-on-year due to the decrease in PC online game revenues offsetting the increase in mobile revenues.

In Japan, we expect revenues to decrease year-on-year, mainly due to the deceleration of mobile games including HIT and browser games. We have multiple mobile games slated for launch in 2018 in Japan, and preparations are currently under way.

In North America, we expect revenues to increase year-on-year driven by the contributions from Pixelberry Studios, which became our consolidated subsidiary in November last year. In Europe and other regions, we expect revenues to decrease year-on-year mainly due to the deceleration of the mobile game HIT in Europe and Asia.

In the Q1 of 2018, we expect the operating income to be in the range of ¥45.1 billion to ¥52.3 billion, which is an increase of 14% to 32% year-on-year. Favorable factors compared to 2017 Q1 on operating income are, first, an increase in revenues primarily driven by our high-margin China business. Second, in Q1 2017, we recognized impairment loss of ¥2.7 billion, which will not be repeated.

These factors will be partially offset by, first of all, an increase in HR cost due to higher head count, mainly in Korea and North America, annual salary hike, and higher stock option expense; second, an increase in marketing

costs associated with Pixelberry Studios, key title Choices, and the launch of the new title including Durango. The high end of the range reflects the fact that we expect the impact of positive drivers to be larger than the negative drivers, resulting in operating income growth year-on-year.

[indiscernible] (00:22:09) to inform you that today at the board of directors, we passed two resolutions. First is the resolution on stock split. This is aimed at increasing the liquidity and expanding the investor base. Each share of common stock as of March 31, 2018 will be split into two shares.

The second is a resolution on the policy to transit to a company with an audit and supervisory committee. After the transition, the committee members will become a part of the BOD. This will enable us to further strengthen the supervisory function of BOD and enhance the corporate governance as well as execute business and make judgment with speed by delegating decision-making authority for business execution to the executive directors.

We disclosed the details including the appointment of directors and amendments to the Article of Incorporation related to the transition as soon as they are determined. Details of those resolutions are available on our IR website.

Now, we are happy to take your questions.

## QUESTION AND ANSWER SECTION

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Thank you. We will now begin the Q&A session. In addition to the people in attendance here, we will also take questions through the teleconference. First, we will take questions from those in attendance here. Please raise your hand if you have any questions. Our people will bring you a microphone. Also, we would like you to say your name and company name when you ask us a question. Are there any questions? Person sitting at the front.

Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Q

Thank you very much for your presentation. I am Nomura's Yamamura. I have three questions.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Excuse me. Can you ask one question at a time, okay?

Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Q

Then first question about Dungeon&Fighter in China. On February 1, you have updated it, and I want to know what kind of events you have conducted. Last year, it trended very well. So, as compared to the previous year, how is it going, if there are any changes? Please answer what are the differences. That's question number one.

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A



Thank you very much for your question. China Dungeon&Fighter's Q1 situation-wise as compared to last year, Lunar New Year started later last year, thus, update happened on February 1, which is two weeks later than the previous year. So, regarding different KPIs, we have to look at the situation after the Lunar New Year. But when you look at 2017 full year, user base is very stable, and it grew dramatically last year. And also, we were able to conduct a content update, thus, we can say that it is trending well.

Last year, we had level cap update, therefore, that further boosted our growth. But this year, we do not have any level cap update but conducted only the update of the content, and we have new character with a different profession, and that is the content of the update that we have conducted. So, as far as the most recent situation is concerned, I believe that we can expect some growth.

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Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Q

Thank you very much. Now about Korean mobile business, you have AxE and OVERHIT and you have Durango, and I understand that the launch of these games were successful. How do you plan to nurture these titles? Each game is quite different in nature. So, if you have any particular strategy as to how to grow these titles, can you comment on it?

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Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Regarding the mobile business in Korea, Nexon as a group, once we launch a major title, it can be ranked at the top list. So, having said that, we are doing well, and the challenges are retention and how we can grow the titles so that many people will continue playing the games, OVERHIT and also AxE. We will be updating our content and also cater to the speed that is being sought for by the users. And I believe that if we can be successful in those areas, we can retain the players. Of course, there are [ph] detailed (00:27:50) strategic points that we will be pursuing. But all in all, we will try to make sure that daily operation will go smoothly [ph] and conduct (00:28:00) content update, say, OVERHIT as an example, not only in Korea, but it will be very popular in other parts of the world especially in Japan, at least that is our take. So, we launched new titles in Korea, and we try to launch in other parts of the world once we deem it is a fit for other parts of the world as well.

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Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Q

Thank you very much. Last question, Owen, you mentioned about the investment for technology, so mid- to long-term perspective-wise, you mentioned about investment in the past, and I am quite interested in it. And do you have any particular technology that you are interested in? And if there is any priority in terms of investment, can you update me on the status?

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Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

It's a great question, and we were just talking about it before our presentation today, and noting how sometimes when we talk publicly about technologies that we're particularly interested in, we find that some of our competitors very rapidly watch that and then copy what we do. So, I'm going to be a little careful about that. I hope you don't mind. Yes, we're actually very conscious as we have a lot of different areas that we're very interested in.

But let me just speak about one of them. Pixelberry's game, Choices, looks like a very simple game on the surface. But as I mentioned in my prepared remarks, it's actually quite deep underneath, and we think that that's



helped it already even without integrating much of our user acquisition in analytics technology into the game. It's helped it to perform very well since we purchased the company already.

But think about in the future a little bit what a game experience like that could be just with the advance of a little more AI and a little more with voice recognition. I personally have at home an Amazon Alexa device, and I ask it to tell me the news and the traffic in the morning when I make coffee. Some people here in this room might use Siri or an equivalent technology from Google. But the idea of you could talk to your game as a form of input/output when combined with a game like Choices could be pretty interesting when you think about a virtual friend or a virtual boyfriend or girlfriend. I think if you project out five years from now, 10 years from now, it's completely within the realm of possibility that we'll be talking to our games as if they were virtual – we'll be talking to virtual characters in the game because voice recognition is getting very, very good.

So, that's one example of where we think that the game industry is going to change radically in the next five years, and we're very excited about some of those opportunities, and we're working very actively inside the company to go explore them.

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Junko Yamamura

*Analyst, Nomura Securities Co., Ltd.*

Thank you very much.

Q

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Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Next question, the gentleman in the third row.

A

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Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Thank you for the presentations. Sugiyama from Goldman Sachs. I also have three questions, if I may.

Q

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Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Yes, so one question at a time please.

A

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Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Yes. At the beginning, during Owen's presentation, you talked about the Dungeon&Fighter in China. It's almost like the annuity business or a SaaS model. So, this time, I think that unlike the entertainment industry, you showed us the certain growth. So, could you talk about the background? And also in order to repeat this with other titles, what are the missing thing with other titles?

Q

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Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

Again, your first question? I'm not sure I understood the first question.

A

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Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Q

So, you mentioned Software-as-a-Service and annuity-like curves for Dungeon&Fighter in China, and we think that's quite different from how entertainment or games industry trend. We're wondering what signs you saw in the China business, which led you to explain D&F in China as that.

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Thank you for your question. Why I think that games like Dungeon&Fighter can look at times more like a Software-as-a-Service model or as an annuity-like business than they do like a typical entertainment platform is because Dungeon&Fighter and several of our other games have repeatedly just simply shown that pattern. And I gave a presentation most recently at a Nomura conference a couple months ago that is available for viewing on our IR website that you might have seen. But I think that the pattern that is in many people's heads when they look at a online game is that a game goes up and then it goes down within the first couple quarters and then it goes to maybe a long tail but that 90% of your revenues will be made within the first one or two quarters in a game.

Now that's commonly held mental model, and it's a commonly held mental model because it's oftentimes true. It's true for most games. It's been traditionally true in the packaged goods games industry. It was certainly true in the early days of Facebook games around the 2009 to 2012 period. And it's been very true in the mobile business.

But the problem with the model and that mental model is that it's not always true, and the exceptions to that model are massive. So, Dungeon&Fighter is an excellent example, perhaps our industry's best example about the exception to that rule. It sometimes goes a little bit down. Sometimes, it goes up, but it is following this general trend that is either very, very stable over time or increasing over time.

And I find it to be a fascinating – frankly, it's a problem for people when they understand our stock about how this could happen. They're constantly looking for the day when Dungeon&Fighter goes away. And that was, in fact, our single biggest question that was asked of us during the IPO roadshow in 2011 when I was CFO. The number one question was when is Dungeon&Fighter going away. And today, Dungeon&Fighter is 2.5 times or more bigger than it was during the IPO roadshow in 2011. So, it is not an accurate mental model for the biggest hits in the games industry.

There are other examples by other companies. League of Legends has done continuously very well by Riot, which is now owned by Tencent. Several other Tencent games have done very well. Some games by Blizzard have continued to do extraordinarily well.

So, this mental model throws people off about Nexon's business, and that's why I mention it sometimes over and over. I hope that answers your question.

Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Q

Thank you very much. Another question, in one of your slides on page 17, you talked about the full-year forecast in 2G (sic) [2D] (00:36:06) Dungeon&Fighter. You continue to make the preparation. So, fiscal 2018, are you ready to distribute that by the end of 2018?

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

We have not made any announcements about that game yet. My apologies. We can't tell you more, but we have to tell our customers first.

Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Q

May I ask another question? LawBreakers, now you're going into that console business. The title is going to be terminated, but you're in the console business. So, any takeaways from that? Any perspective on the console business in coming years?

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

The LawBreakers or to the console business in general?

Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Q

To the console business in general.

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Well, let's see. There's let's call it the medium term of two years or so and then the longer term, call it five years or more. Over the longer term, five years or more, ultimately, we see probably a consolidation or integration between all the different platforms, the three major platforms. That would be mobile, PC and console. We think that that day will probably come at some point. And in fact, I have in my pocket an iPhone X, and I'm just surprised by what an incredible device that is. Well, let's see, five years ago, we would not have been able to deliver a game like Durango on a mobile device. The networking layer was just not strong enough nor was the graphics layer. But I think you're going to see more sophisticated games on mobile, and ultimately, the things are going to be more and more portable.

I also think that the console companies are thinking differently about their business than they were even a few years ago. And in fact, Nintendo is a leader when you look at the switch about the idea of bringing something that used to exist in a living room and bring that portably with you around. So, my guess, I don't have any particular insight, but I think that Sony and Microsoft are thinking about their console businesses in a different way than they did even a couple years ago. A couple years ago, they would talk about owning the living room, but as we all know, there really isn't a living room anymore or at least, that's not where we consume the bulk of our media consumption, in the living room. We consume it in the subway or out and about or in all different rooms in our house.

Getting back to your question on console, I think in the meantime, though, in the more immediate term, in the next few years, a console represents a huge opportunity particularly for online games. Console games used to be primarily a single player or a group player games, and more and more, there's an opportunity in the living room. And so, we see that as an opportunity, which is why we're going to be bringing more games to console coming up in 2018 and beyond.

Masaru Sugiyama

*Analyst, Goldman Sachs Japan Co., Ltd.*

Q

Thank you.

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

By the way, one other thing on that is we don't know the exact timing, so we're going to watch it closely. We're not in the business of forecasting far out into the future. If we were, we'd probably be like everybody else who forecasts things. It's a very hard business to be in, but we are watching it very closely, and in the near term, we think there's a big opportunity in console.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Any other question? Third row from the front, gentleman, please.

Keiichi Yoneshima

*Analyst, Credit Suisse Securities Japan Ltd.*

Q

Thank you. I am Yoneshima of Credit Suisse Securities. I have three questions, so I will go one at a time. Firstly, about impairment loss, I want to confirm in 2017, when you look back at it, say, every quarter, you have about ¥3 billion to ¥4 billion. And I know that game itself is trending well, but every quarter, you are recording impairment loss. So, I want to know what is the area in which you are recording impairment loss. And I know that in Q1 2018, you don't expect any impairment loss. But looking at the past history, it seems that you have a tendency to have impairment loss. And so, can you tell me in what area you are recording impairment loss?

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Thank you for your question. Regarding our thinking of impairment loss, firstly, let me tell you what is the content of impairment loss. We acquire the game IP and also we prepare royalty fees, and when we close that game or even after the launch of the game, there are cases in which we cannot recover the investment. And in those instances, we have to record impairment loss. We have multiple titles in our pipeline, and we are conducting our development. That being the situation, we encounter impairment loss even though each impairment loss amount is not that high. But cumulatively speaking, you see a ballpark figure.

We want to continue challenging so that we can have abundant pipeline. And it's a destiny or fate, so to speak, to have impairment loss. But as you know, it is quite difficult to forecast the impairment loss in a concrete manner. So, in our outlook, we do not factor in impairment loss. So, in a way, that is a downside. So, if we were to record impairment loss, that will be a negative driver.

Keiichi Yoneshima

*Analyst, Credit Suisse Securities Japan Ltd.*

Q

Thank you. Second question about China business, I know that Dungeon&Fighter is trending very favorably. And regarding MapleStory2, as you have commented, I know it is growing. Can you give me more tips, say, this quarter, you see that it might grow by 5% to 10%? And in terms of the impact of MapleStory2, what will be the magnitude? Do you think there is an impact of about 10% or is it still too small to talk about the contribution? It's becoming a hit, so you mentioned it or can you tell me about the contribution rate of MapleStory2 to the whole business?

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Regarding MapleStory2, we didn't have this title last year. So, year-on-year, it is contributing greatly. Having said that, Dungeon&Fighter is such a big hit and a big title. So, comparatively speaking, in the growth of China, MapleStory2 is not playing a major role. Regarding PC online business, whether it be Dungeon&Fighter or not, we need to nurture it slowly so that it can have longevity.

So, we do not expect a dramatic growth of sales, but rather, we want MapleStory2 to grow gradually as we designed it. I know that interest of China business, there will be some contribution by MapleStory2, but then the major one is still Dungeon&Fighter. Yes, when you talk about China, you cannot just ignore MapleStory2.

Keiichi Yoneshima

*Analyst, Credit Suisse Securities Japan Ltd.*

Q

Please turn to page 22. In Q1, you have different titles, and if you have any titles that you know that are coming in Q1, I will appreciate it. I know that Durango is already in the market. Are there any other titles that will be launched in Q1? And if you can tell me any country in which you will be launching these titles, please let me know.

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Let's start with PC. We've already announced the following. FIFA Online 4 will be launched before World Cup, and preparation is under way accordingly. Next about Astellia, it will be launched sometime in Q2, i.e. around June. Battlerite will be launched sometime in 2018, and that was already announced.

Now, moving on to mobile titles, we have Durango, and it was launched in Korea already. And we plan to launch it globally ex-China. Preparation is under way. OVERHIT is scheduled to be launched in Japan, but the timing is not determined yet. Elsword, we haven't decided on the schedule, and KAISER is scheduled to be launched in Korea, but timing-wise, it is not determined. DARKNESS RISES, this is a global version of Dark Avenger 3, and we will go global and preparation is under way. FINAL FANTASY and Dungeon&Fighter, these, we haven't decided on the schedule. Project D undecided and MapleStoryM, we will go global and preparation is under way. And Mabinogi Mobile is scheduled to be launched sometime in 2018, and preparation is under way. That will be the overall flow.

Keiichi Yoneshima

*Analyst, Credit Suisse Securities Japan Ltd.*

Q

Thank you.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Thank you very much. I think there will be more questions, but we would like to now take questions from those people who are connected via phone.

Operator The next question is Han-Joon Kim from Deutsche Bank. Please go ahead.

Han-Joon Kim

*Analyst, Deutsche Bank AG (Hong Kong)*

Q

Hi. Thanks for the opportunity to ask questions. I wanted to follow up on Durango. And I've been personally excited for this one and other ones as well in the past. But sometimes, we have a good start and then they fade for various reasons. And so, Durango is unique. It's gathered a lot of attention. The start is good. But like I would

like to see if there's any quantitative way to think about where we are in Durango and how it might differ in terms of life cycle, what kind of maybe KPIs we're seeing that gives us some thought that the trajectory for this game could be different from some of the other ones that we've seen recently. So, any kind of quantitative KPIs to kind of gauge Durango, I think that will be much appreciated.

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**Owen Mahoney**

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Han-Joon, thanks for your question. This is Owen. I think the short answer to your question is it's just way too early to tell. As you know, this is a deep, rich MMORPG, and the play style implies a much longer period of play for customers. What makes this very different from anything that's really been tried before and makes it difficult to answer your question is it's the first time that something like this has really been tried on mobile. And as a result, it's going to skew in sort of an interesting but hard to predict way from benchmarks that we usually look at because it is so different.

I would anticipate or we will get a whole lot of mobile users who would otherwise play much more simple games as an example. And some of those people will not stick with a much deeper experience like Durango over time because that's not what they really want. And so, especially when you get [ph] featuring (00:49:11) on Apple and Google, that will happen. So, some of those people will not stay.

On the other hand, it will open up a much deeper experience to people who otherwise wouldn't have been exposed to let's call it a PC-style MMORPG. And so, we don't know what the patterns are yet. I'd say qualitatively speaking, the early returns are terrific. But as you know, in a game like this, we're not paying too much attention to what happens over a period of a couple weeks. We're much more interested in trying to figure out what will happen in a couple of years or over the period of a couple of years. So, that's the source of your question I would anticipate – or I would imagine, and that's certainly where the real question is. But I think it's way, way too early for us to figure out the answer to that question.

---

**Han-Joon Kim**

*Analyst, Deutsche Bank AG (Hong Kong)*

Q

Okay. Well, I appreciate that, and I fully understand where you're coming from. But if I just try to maybe press that point a little bit further, have we seen anything that would make you kind of ponder, make a pause a little bit and think that this could be on a different trajectory or so far, we've been a little bit too busy trying to manage to get people into the game that we haven't been able to kind of do any diagnosis or again, is it too early to be able to make any kind of diagnosis?

---

**Owen Mahoney**

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Yeah, I think it's too early to tell. I mean, again, we've highlighted it. We're really happy with the start. That's what I definitely can tell you. And qualitatively, the feedback that we're getting from our customers, as you probably well know, the first couple days, the demand for the game and given that it is such a deep, rich game overwhelmed our capacity given how deep of a game it is. So, that was something that we really had to scramble to make sure that we could handle. Looks like we're in a much better shape than we were a few days ago, but that's a function of just having huge demand for the game. It was even bigger than what we anticipated.

But overall, the feedback we've been getting qualitatively from people is they're playing the game, they're really liking the game, they really are drawn into the world because it's such an immersive world. So, we're very gratified by that. But I'll tell you, when you do something that's completely different and you think completely differently, the



reality of that or definitionally, you can't look to comparisons to other experiences you've had, and that's just a function of being a pioneer, and that's what we are with this game.

Han-Joon Kim

*Analyst, Deutsche Bank AG (Hong Kong)*

Q

Okay. [ph] Got it (00:52:03). I appreciate that. My follow-up question is just on Dungeon&Fighter for the first quarter in China [ph] yes, (00:52:11) and I'm a little bit surprised with the first quarter guidance, and I suspect you guys have seen some data to support that. But I think we've always tried to stay away from pushing the envelope on the ARPPU side, so I noticed that our MAU and our paying ratio kind of declined in the fourth quarter. But for the first quarter, are we seeing signs that user bases, actually MAU is picking back up, and paying ratios picking back up and perhaps it's a less function of the ARPPU?

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Well, thank you. As I said, concerning Q1, the Lunar New Year was later than the previous year, so we haven't really had the full analysis. But what we are hoping for is a slight decline at the MAU and a slight increase of the paying user and a slight increase of ARPPU. So, slight decline of MAU. There are two reasons. First is that due to the publisher, there was a bot sanction; and second, as I mentioned, the Lunar New Year was later. And usually, toward the Lunar New Year, we have a warming-up event. But since it was later, during the time period, we didn't really have a lot of warming events, so that led to the lower MAU.

But up to Q3, the paying user increased significantly last year, as we mentioned. So, in that sense, from Q3 to Q4, paying user increased. It was a slight increase. So, revenue is driven by ARPPU. So, based on this trend, Q1, probably we can expect higher ARPPU, but Dungeon&Fighter [indiscernible] (00:54:10) Dungeon&Fighter PC titles, if you took at ARPPU and also mobile ARPPU. It doesn't mean that they are much higher. So, it is not going to be a big hike of the ARPPU, which might lead to the concern. So, those people who buy the small items, they enjoy, they pay, and they start to buy packages. So, that's how the ARPPU is increasing. So, we'd like to continue to see Dungeon&Fighter in China, and we consider that to be healthy.

Han-Joon Kim

*Analyst, Deutsche Bank AG (Hong Kong)*

Q

Okay. Great. Thank you very much. That's all my questions.

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Thank you.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

There is one more person asking question over the phone, please.

**Operator:** The next question is Thomas [indiscernible] (00:55:11) from Daiwa Securities. Please go ahead.

Thomas Kwon

*Analyst, Daiwa Securities Capital Markets Korea Co., Ltd.*

Q



Right. Thank you for taking my questions. I have always this question on Durango. As you mentioned, Durango [ph] has been viral (00:55:23) since its launch, but now, we see that your company is now selling in-game items for Durango so very aggressively, essentially in-game items for the game performance, and [ph] they even know or referenced the (00:55:39) monetization plan in the future as well [indiscernible] (00:55:45). Is it fair to expect this weak revenue [indiscernible] (00:55:52) from Durango even after its potential launch into the global market? [indiscernible] (00:55:58) company's monetization strategy for Durango game. Thank you.

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Just to be clear, I want to make sure I understand your question. Your question is about monetization strategy for Durango. Is that correct?

Thomas Kwon

*Analyst, Daiwa Securities Capital Markets Korea Co., Ltd.*

Q

Yes, that's my question.

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Regarding Durango, considering the genre of Durango, I do not think that this is a game for monetization per se, but rather, we want people to continue playing for a long time. So, more or less, it is closer to PC title. So far, retention is good, therefore, I believe that we can upgrade this game for a long time, and though with that as a backdrop, we want Durango to contribute in both revenues and operating profit. As we have mentioned, it is contributing to the profit, but this is not the game that we should be focusing on monetization per se.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Any other question?

Thomas Kwon

*Analyst, Daiwa Securities Capital Markets Korea Co., Ltd.*

Q

This is all my question. Thank you.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

Thank you very much. Now, we would like the people in the floor to ask questions. Person sitting third row from the front.

Haruka Mori

*Analyst, JPMorgan Securities Japan Co. Ltd.*

Q

Mori from JPMorgan. I think I understand that we are running out of time. Short question about the guidance for Q1, last year, I think, the Lunar Year guidance was included and the March also showed the effectiveness of that and was better than expectation. So, based on the initial feedback, to what extent do you think that the effectiveness of this Lunar New Year content update will continue, if you can give us your feeling on that.

Shiro Uemura

*Representative Director and Chief Financial Officer, NEXON Co., Ltd.*

A

Well, the later Lunar New Year update due to the time difference, the update was later. So, this will continue, we believe, until the end of March. As for Q2, we cannot give you any numbers. But in that sense, probably there will be some effect remaining in Q2. Thank you.

Haruka Mori

*Analyst, JPMorgan Securities Japan Co. Ltd.*

Q

Second question, it's a question about the eSports, impact from the eSports on Nexon or your efforts in the area of the eSports. I would like Owen to answer. PUBG is becoming popular. So, this is an opportunity, and this is also a competition. So, eSports business opportunity, how do you think about that? Any comments?

Owen Mahoney

*President and Chief Executive Officer, NEXON Co., Ltd.*

A

Well, boy, that's a long topic. Let me try to simplify it a little bit. First, I'll make a blanket statement that may seem a little silly. But I think our industry sometimes gets hung up on individual topics that over the long term don't actually have a major impact fundamentally on the totality of the whole industry. Certainly, people used to talk about Facebook games a few years ago, and we got asked a lot of questions about our Facebook strategy. Some of you remember those questions from the time of the IPO. And we said, respectfully, we have no Facebook strategy because we think Facebook is a terrible platform. That's what we thought at the time. It turned out to be true.

Now, I'm not saying the same thing about eSports. I think eSports is very interesting. I watch eSports games sometimes myself. But I think the point that people miss is it's primarily a PC environment, not a console or not a mobile environment, at least as of today and for the foreseeable future, and there's a lot of reasons for that. So, there seems to be a lot of discussion about eSports in Japan. But Japan is not particularly a PC-oriented market. So, I'm not quite sure why that is.

The second thing I'd say is that if you take one or two of the big games out of eSports, people would be a whole lot less enthusiastic. And those games are League of Legends would probably be the biggest one, and maybe Overwatch as well. But if you took one or two of those games out, I think it would be a lot harder for a lot of the companies, for example, in California that are raising venture capital around eSports. They'd have a much harder time to do it.

And I also think at least internationally and less so in Japan but certainly in North America one of the things that's driving all the discussion about eSports is, frankly, there's a lot of traditional sports franchise owners and other infrastructure that are very interested in this topic because frankly, those sports are going away or on the decline. If you look at the statistics for baseball, this has been happening for some time. It's more recently been happening in the NFL. The viewer numbers for the NFL has gone down, from what I understand, quite significantly. So, if you're a team owner or somehow if you're an agent or you're somehow involved in that, you look at the future and you say, well, I can see the future, this is going away, I need to think about something new, what's new, oh, well, some of the big game executives are really pushing eSports, oh gosh, I better start buying eSports because I've got no future otherwise. That literally is happening.

So, I think there's a whole lot of reason why people are interested eSports. Some of them are real, some of them are not. But let's really back out to what is going on underneath, and it's a much broader discussion. The broader discussion is about viewing games. And viewing games is actually a pretty fun activity. I do it a lot myself. I have two boys. They're 12 and 14. They both love to watch people who are good at playing games, view it. And sometimes that's eSports, but oftentimes, it's not eSports at all. It's sometimes two guys on a couch making jokes while they play some game, and they're broadcasting that over Twitch. It can make for some very good viewing.

And so, I think people who play a lot of games, people who watch a lot of games – I've had several discussions around the industry and I think we're all watching this pattern emerge that viewing games, other people who are good at playing games and commenting on them and the interaction between their viewers and themselves is actually really fun. It makes for a compelling viewing. And that, I'm very, very excited about.

And in some cases, that will come from eSports. I certainly watched a lot of great sports games, particularly watching StarCraft in Korea 10 years ago, but a lot of things have to be in place for that to be a real business, not just a lot of investment. So, I don't have a huge prediction about how that will be, but I am somewhat cautious about this.

Now, as far as Nexon is concerned, Nexon has Nexon Arena in Korea. It seats about 550 people. We have roughly 300 events a year, and I would encourage anybody in this room to come and see it. It's in the middle Gangnam. It's part of the nightlife in Gangnam. It's very, very fun to watch, great players, live, play games. But what we find in eSports is that players determine what will become an eSports game. The gamers themselves determine that. The company doesn't determine that. And there've been a lot of examples where a company has designed what they thought was an eSports game, and it just hasn't worked out.

So, when you look at a game, you have to watch what players are doing and are they playing it and broadcasting that online. So, those are a mishmash of different comments about the future of eSports. I'm not sure if that's helpful, but it's certainly worth watching and certainly a topic that's worth watching.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

A

So, did he answer your question? Thank you.

Yuki Hayakawa

*Head-Corporate PR, Corporate Branding, NEXON Co., Ltd.*

Unfortunately, time is up. We would like to conclude Nexon's 2017 fourth quarter earnings presentation. Please leave electronic interpreter device on the table when you leave. We appreciate your cooperation on the link feedback sheet to support our IR activities. Again, thank you very much for joining us today.

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