

Financial Results Briefing for Fiscal Year Ended March 2021 (Conference Call)

Nintendo Co., Ltd.

Q&A Summary

Date: Thursday, May 6, 2021

Attendees: Shuntaro Furukawa (Representative Director and President),
Hajime Murakami (Executive Officer)

- The following are the main questions and answers from the financial results conference call. Please note that portions of this content have been edited or revised to improve readability.
- If you quote from this Q&A, please include a citation or link to this file.

Q1 What are your assumptions behind the forecast of 25.50 million units of hardware shipments for the current fiscal year (ending March 2022)? Also, if demand continues to be stronger than expected, will you be able to ship out more units than indicated in the current forecast? Or, do you believe that additional supply would be difficult due to factors like the current shortage in semiconductor supply?

A1 Shuntaro Furukawa (Representative Director and President):
The financial forecast for the current fiscal year was created based on our results through the previous fiscal year (ended March 2021) and the sales projection for the current fiscal year, taking two main points into consideration. The first point is that during the previous fiscal year, *Animal Crossing: New Horizons*, released in March 2020, was a hit and greatly drove hardware sales, especially in the first half of the year. As a result, sales during the first half of the previous fiscal year were on a scale unprecedented in our company's history, and we believe that we need to take this temporary effect into consideration. The second point is that hardware and software sales remained quite strong during the fourth quarter (January through March) of the previous fiscal year, and that even recently we are still maintaining a high level of sales. In March of this year, Nintendo Switch entered its fifth year since launch. However, we recognize that, unlike the fifth year in the life cycles of our previous game systems, Nintendo Switch currently has very high momentum. Taking these two points into consideration, we have set our hardware sales forecast for this fiscal year at 25.50 million units.

As for production, we achieved steady hardware production through the end of last calendar year, and as a result, in the previous fiscal year we set a record for our highest fourth-quarter sales volume. Meanwhile, demand for hardware continues to exceed our expectations even after the beginning of this calendar year, and production has currently not caught up to this high demand due to the tight supply and demand situation for semiconductor materials worldwide. Although we are currently striving to produce as many units as possible, the fact is that our production plans are more uncertain than they were at the beginning of previous fiscal years. Our full-year sales plan is based on the premise that we can secure the materials necessary for production, but if we are able to produce more units, we will work hard to meet the strong demand, and to be able to ship and sell those units.

Q2 What is the current scale of active users on Nintendo Switch? Qualitative information would be fine as well. I'd like to hear more about your stance regarding active users as part of the premise for your software sales forecasts.

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A2	<p>Furukawa:</p> <p>After the release of <i>Animal Crossing: New Horizons</i>, there was a substantial increase in the number of consumers playing Nintendo Switch. There was a gradual decrease afterward, but there was another considerable increase during the year-end holiday season last year, which reached the highest number of active users since the release of Nintendo Switch. Although the number slightly decreased after the beginning of this calendar year, a lot of consumers are playing Nintendo Switch with the recent March release of Capcom's <i>Monster Hunter Rise</i>, so we don't think that the momentum is fading. Many new software titles will be released this fiscal year, starting in the first quarter, which we think will help continuously expand the range of consumers who play Nintendo Switch to include those who haven't played Nintendo Switch in a while or are completely new users.</p>
Q3	<p>Overall software sales, not just limited to big titles, were strong in the fourth quarter of the last fiscal year. Hardware sales were also good, and digital sales were flat compared to the previous quarter (the third quarter of the last fiscal year), staying at a very high level. Do you think this was affected by the resurgence of COVID-19? It looks like people's lives are getting back to normal in the United States and other countries. However, given these circumstances, what are the assumptions underlying the outlook for this fiscal year?</p>
A3	<p>Furukawa:</p> <p>In the previous fiscal year, the number of consumers interested in Nintendo Switch expanded significantly after the release of <i>Animal Crossing: New Horizons</i>, resulting in the strong demand for both hardware and software through the first nine months, and we think the effects of that were seen in the fourth quarter as well. In addition to the main drivers of <i>Animal Crossing: New Horizons</i> and <i>Ring Fit Adventure</i>, the fourth quarter also featured very strong sales of our evergreen titles. From January through March 2021, sell-through of Nintendo titles like <i>Mario Kart 8 Deluxe</i>, <i>Ring Fit Adventure</i>, <i>Super Mario Party</i>, <i>The Legend of Zelda: Breath of the Wild</i>, <i>New Super Mario Bros. U Deluxe</i>, <i>SUPER MARIO ODYSSEY</i>, and <i>Splatoon 2</i>, among others, exceeded that of the same period of the previous year. We believe that one of the major causes for this is that consumers who purchased Nintendo Switch when <i>Animal Crossing: New Horizons</i> was released purchased one of these evergreen titles as their next game. Sales of our new title, <i>Super Mario 3D World + Bowser's Fury</i>, were also strong, and overall software sales were very high throughout the fourth quarter. We consider that one of the factors underlying this rise in sales was the increase in demand for home entertainment due to staying at home.</p> <p>And in terms of digital sales, consumers who purchased hardware during the year-end holiday season are relatively inclined to purchase their next game digitally, leading to a tendency for the ratio of digital sales in the fourth quarter to be higher than the third quarter. But even so, the fourth-quarter digital sales in the previous fiscal year were comparable to those in the third quarter, which indicates that purchasing software digitally has become quite widespread as an option for our consumers.</p> <p>With the level of momentum we're seeing in the business, our sales forecasts for this fiscal</p>

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	<p>year are based on the continuous promotion of already-released evergreen titles to all of our consumers including new ones. The financial forecast for this fiscal year is primarily based on the sales outlook for unreleased new titles as well as our evergreen titles, and does not take into much consideration the impact of COVID-19. We are paying close attention to any differences in consumption patterns that may emerge across regions as the situation with COVID-19 subsides.</p>
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Q4	<p>In recent years, research and development (R&D) expenses have been on the rise. What's the context for that? You're anticipating R&D expenses of nearly 100 billion yen this fiscal year, but could you give a general idea of what kind of development that is for?</p>
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A4	<p>Furukawa:</p> <p>Our software development costs, which include outsourcing, are increasing as we work to maintain a continuous stream of new titles for Nintendo Switch as it enters the middle of its lifecycle. Because per-title development costs are higher now than they were on past platforms, we anticipate that R&D expenses will continue to rise as we work to maintain a sizeable lineup of titles. We are also conducting a variety of studies, which include investigating ways to enhance our digital business, and future services that will help maintain long-term relationships with our consumers, as was touched on in the Corporate Management Policy Briefing last September. In addition, the development of the next generation of hardware needs to begin years before launch, so R&D expenses for that are gradually rising. We are aiming to grow by continuing our integrated hardware-software entertainment business, and that means conducting all sorts of research and development in various areas including both hardware and software.</p>
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Q5	<p>What is your stance on shareholder returns? Given your current cash position, is there a possibility of a share buyback? Also, is there a possibility of a stock split?</p>
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A5	<p>Furukawa:</p> <p>Let me explain our basic thinking on the use of cash. We are in the entertainment business, which is a very high-risk business where a company cannot expect to grow unless it continually takes on the risk of trying to develop new products. For example, to launch new hardware involves huge investments in areas such as research and development, manufacturing, and advertising, and that investment risk is growing year by year. In addition, we have embarked on several projects in our new visual content business, and the investment opportunities there will increase going forward. Accordingly, we need cash holdings not only for ordinary working capital, but also to withstand a number of unsuccessful projects, if by any chance such were to occur. We also believe they are a necessary means to ensure our financial stability to business partners and various other stakeholders.</p> <p>We can imagine using cash for M&A and the like, but we might also choose to conduct a share buyback as an implementation of our flexible capital policy. Our basic policy regarding a</p>
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	<p>share buyback is to conduct it if deemed necessary based on the business environment, our share price, and stock market trends. As for a stock split, we understand that it is one effective way to widen the investor base and further increase stock liquidity, but we want to carefully study the measure from various perspectives, with a comprehensive consideration of such factors as stock market trends, as well as our share price level and stock liquidity.</p>
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Q6	<p>Looking at your financial forecast and comparing the plans for sales volume of Nintendo Switch hardware and software with total net sales, it seems that sales volume is expected to decrease by 10% or more year-on-year, while total net sales are expected to decrease by 9%. Why are total net sales expected to decline by a smaller margin than sales volume?</p>
A6	<p>Furukawa:</p> <p>We don't disclose a detailed breakdown of sales, but for hardware, please note that Nintendo Switch and Nintendo Switch Lite have different unit sales prices. And in the same way, the unit sales price for our first-party software differs from the unit sales price for software from other software publishers. Therefore, net sales of both hardware and software will differ depending on how you look at the sales ratios. The financial forecast is calculated based on approximate numbers and also includes other factors, so sales and sales volume do not necessarily move in perfect alignment.</p>

Q7	<p>How is Nintendo Switch demand trending by region? Also, why is the software sales plan for this fiscal year lower than actual sales for last fiscal year despite the strong demand for software?</p>
A7	<p>Furukawa:</p> <p>Regarding the current situation for Nintendo Switch hardware, there are no major differences between regions, and demand remains strong overall. However, COVID-19 has caused declines and delays in freight traffic in markets outside of Japan, and retailers in some regions are experiencing temporary shortages. In particular, the accident that blocked the Suez Canal caused delays in the transportation of products bound for Europe, and retail inventories are tight in some countries. In the United States, sales were strong in March, and the supply of hardware is currently not keeping up with the strong demand. In the "Others" region, sales are also growing steadily. Regarding the software sales, there are small differences among countries and regions, but overall, sales of both new titles and evergreen titles are doing well.</p> <p>Total software unit sales including titles from other software publishers for the full fiscal year are not easy to forecast at the beginning of the fiscal year. The 230.88 million units in actual sales in the previous fiscal year included many units of titles from other software publishers. Annual sales at the level of 200 million units is a scale we have seldom reached in a single year for a single platform, so even sales of 190.00 million units (the software sales volume forecast for the current fiscal year) is by no means a small number. Moreover, to reach that volume of sales requires that we firmly convey the appeal of Nintendo Switch to consumers.</p>

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Q8	Regarding your efforts to expand new users going forward, which groups do you feel Nintendo Switch has not yet fully managed to reach? Also, do you have an update on the spread of Nintendo Switch in China?
A8	<p>Furukawa:</p> <p>In the previous fiscal year, household demand for multiple systems accounted for roughly 20% of unit sales of the Nintendo Switch family of systems. Going forward, we expect demand for multiple systems per household will increase even as hardware unit sales grow. By region, significant sales growth is continuing in Asia, and we believe there is still room for sufficient growth of new demand in Europe and the United States, considering the sizes of those populations. To this end, we must thoroughly convey the appeal of existing titles and future titles to consumers.</p> <p>Regarding business in China, we have no major updates, but according to Tencent Holdings Limited, which conducts sales on our behalf in China, sales during this Lunar New Year holiday season surpassed sales of the same period of the previous year. Titles including <i>Mario Tennis Aces</i>, released in January, and <i>Ring Fit Adventure</i>, which continued its strong momentum, sold well, as did evergreen titles like <i>Mario Kart 8 Deluxe</i>, and <i>New Super Mario Bros. U Deluxe</i>. We will continue to work persistently to expand sales.</p>

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