



**Haruhiro Tsujimoto**  
President and Chief Operating Officer (COO)

## Aiming for Medium- to Long-Term Growth through Opportunities in the Changing Business Environment

### New Sales Strategy Based on Digital Distribution

Games connected to the internet played with multiple people are already commonplace, and in recent years, even more online innovations are taking place in the game industry.

The biggest transformation is the "distribution revolution" spawned by the digital distribution of games. For the past several years, this trend has accelerated substantially, as can clearly be seen in Capcom's operating results. As the ratio of digital download contents sales increases, inventory return ratios improve and operating margins expand. Also, in line with the growth of digital distribution, performance has improved in Asia, where package sales had been virtually impossible until now due to the flood of pirated games.

In terms of game sales strategies going forward, the key to success will be the degree to which we are able to utilize digital distribution. The ability to distribute

games throughout the world without the significant labor and costs involved in overseas sales networks is paving the way for an environment in which we are able to compete with major overseas game companies on an equal footing.

Furthermore, support for multiple languages is another critical point. At present, games can be purchased online almost anywhere. There are many developing markets that can suddenly transform into promising opportunities. In anticipation of such developments, new games released in the fiscal year ended March 31, 2016, were available in 14 different languages.

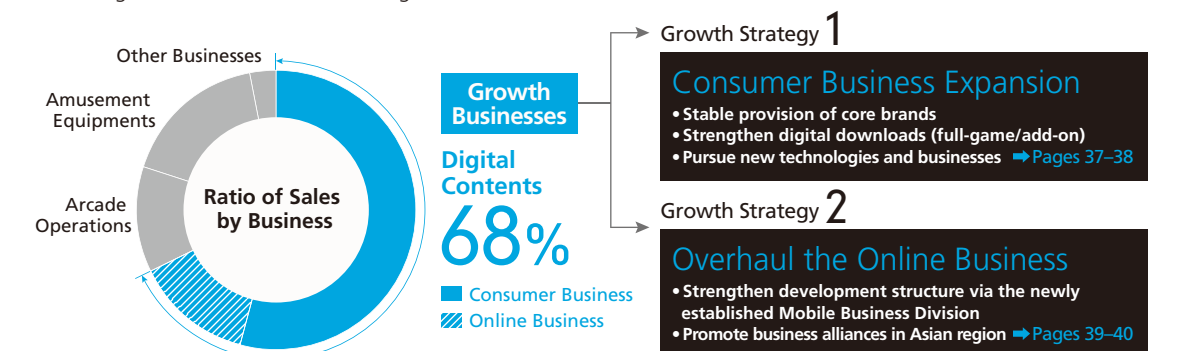
➔ Please refer to page 3 of The Latest Development Report.

In light of these new trends, Capcom will strengthen digital download contents in the Consumer business and implement measures to set the Online business on a growth trajectory.

### Investing 80% of Management Resources in the Digital Contents Business

The Digital Contents business is our core business, accounts for 68% of net sales and generates original content, which is the source of our corporate value. We are allocating approximately 80% of management resources in this business, which I believe is the key to achieving our medium-term business goals. For the

Digital Contents business to grow, in addition to further expansion of the Consumer business, we must overhaul the struggling Online business and establish a growth trajectory. On the following pages, I will explain our strategies for achieving these goals.



# Growth Strategy 1

## Consumer Business Expansion

### Establishing a High Earnings Structure and Stable Portfolio

One important strategy for Capcom to achieve ongoing and stable growth in the Consumer business—referred to as the hit business—is transforming the foundation of our Consumer business model from a traditional one-time sale “transactional model” to a continuous “recurring revenue model.” [Diagram 16] Going forward, the consumer market will continue to maintain a scale of 22 billion dollars as the number of game makers’ declines due to high barriers to entry. Companies that possess an abundance of popular IPs and strong technological capabilities will easily win the market and enjoy profits in this environment. For Capcom, the Consumer business is the source of our corporate value. We will implement the following three measures, each positioned as one of the most important strategies for growth over the medium- to long-term.

#### Measure 1 Stable Provision of Core Brands

Capcom’s biggest strength is the in-house creation of powerful brands and ownership of numerous popular IPs. At the same time, unit sales of major titles has fluctuated depending on the fiscal year, thus high earnings volatility was an issue.

For this reason, we shortened the sales cycle for titles in each series from three to four years to two and a half years and increased the number of titles released in a single fiscal year. Employing a medium-term strategic (60-month) map, we are forming a title portfolio enabling sustainable growth and establishing a structure

that appropriately allocates employees to teams when needed from 2,000 developers via a 52-week map. These two maps enable the stable release of multiple major titles each fiscal year and control earnings volatility. [Diagram 17] Furthermore, we think the creation of new brands that will become our future primary sources of earnings is indispensable for medium- to long-term growth. Thus, we are allocating approximately 20% of development investments toward new IP development.

#### Measure 2 Strengthen Digital Downloads (Full-Game/Add-On)

The merits of digital downloads include (1) avoiding inventory risk and reducing package production costs through full-game downloads, (2) additional earnings opportunities through full-game downloads of catalog titles whose package sales are difficult for retailers and (3) anchor users through ongoing add-on contents and stable acquisition of additional revenue over the long term.

These represent one measure to counter concerns over intense sales volatility due to dependence on hit titles in the Consumer business and skyrocketing development costs. In addition to the stable provision of core brands, the accumulation of steady digital download

sales each fiscal year will further the transition to a recurring revenue business model. [Diagram 18] At present, we are focused on points (1) and (2), but going forward, we will strengthen point (3) to increase the digital download ratio, which is currently 26%, to 50% over the medium-term. This will bolster additional recurring revenue by anchoring users for more than one year after launch, and as these games will have a large number of active users, it will also lead to the acquisition of new users, effectively controlling sales volatility each fiscal year.

#### Measure 3 Pursue New Technologies and Businesses

In the game industry, once neglected, it is difficult to pursue research on cutting-edge technologies. Constant technological research in new areas and continued exploration of gaming possibilities are the stepping stones for establishing a groundbreaking position in the next-generation.

In 2016, new devices including PlayStation VR and Oculus Rift appeared on the market and brought with them huge expectations in what has been called “VR year one.” Capcom’s specialty in the action and horror genres is extremely compatible with VR and by offering

new experiences with VR, our games will be even more appealing. This fiscal year, we are proactively approaching this development with *RESIDENT EVIL 7 biohazard*, which offers full Playstation VR support. We are also focusing efforts on eSports as a new genre. With the *Street Fighter* series in particular, we had held events mainly in North America, which were well attended. However, going forward we plan to develop activities in other regions. With these new business challenges, we will attempt to maximize earnings through the active use of content and enhanced brand value.



Monster Hunter series



“Catalog titles of major IPs creates a solid earnings base”

Street Fighter series

Resident Evil series

The penetration of digital download sales is driving the sales ratio of our recurring revenue model higher each year and generating continuous profits, unlike the transactional model.

Diagram 16

### Catalog Sales Volume and Ratio Increases

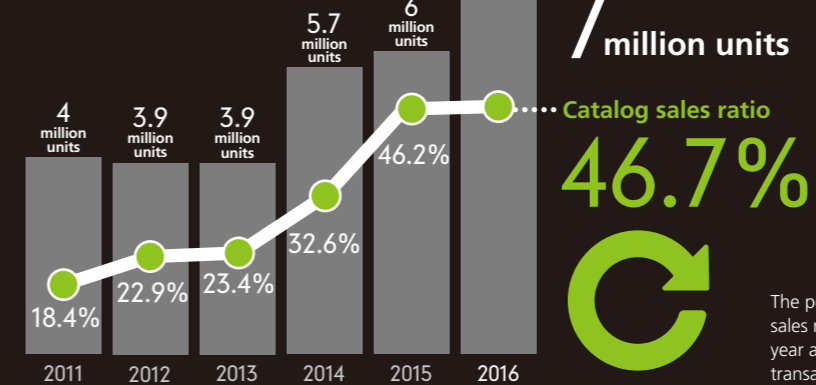


Diagram 17

### 60-Month Sales Plan and 52-Week Human Resources Plan

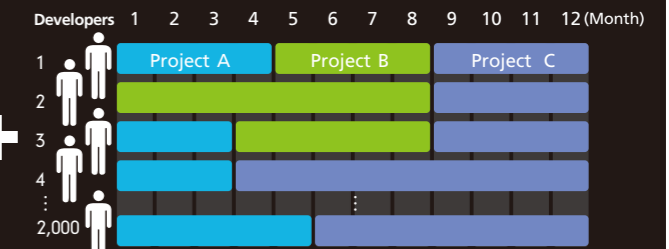
#### 60-month map

“Objective Stabilize annual earnings”



#### 52-week map

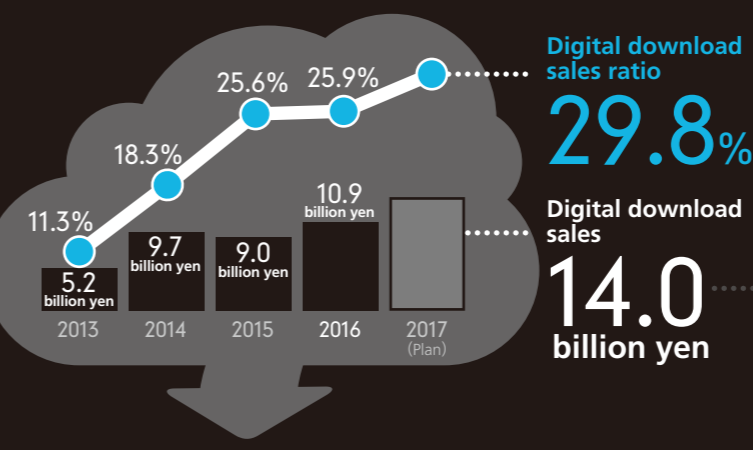
“Objective Effective utilization of R&D resources”



To achieve stable earnings growth, it is important to steadily provide numerous popular titles and shorten development periods.

Diagram 18

### Digital Download Sales Volume and Ratio Increases



Digital download sales of mainly full games (new and past titles) are growing on track and expected to comprise approximately 30% of the digital download sales ratio in the fiscal year ending March 2017. Going forward, we will strengthen additional digital download content and raise the digital download ratio to 50% overall.

- NEW Full game digital downloads**  
Download new full games
- Catalog digital download titles**  
Download catalog title full games
- Additional digital downloads**  
Download additional stories, stages, items, etc.

# Growth Strategy 2

## Overhaul the Online Business

### Supporting Capcom's Sustainable Growth Differently than the Consumer Business

Capcom has yet to make full use of its competitive advantage in the rapidly expanding online market (PC Online and Mobile Contents), namely, its rich library of popular IPs. In particular, the Mobile Contents business struggled in the fiscal year ended March 31, 2016 with net sales of only 3.3 billion yen. However, as success in the high-growth potential Online business is indispensable for corporate growth over the medium- to long-term, we are focused on this area as one of the most important issues for Capcom. Online games are a management business, providing a stable source of profit supporting Capcom's sustainable growth in a way different from that of the Consumer business. Furthermore, these businesses enable the creation of synergies with content (IP) created in the Consumer business, playing a significant part in enhancing brand value. To alleviate investor concerns, we will implement the following two measures.

#### Measure 1 Strengthen Development Structure via the Newly Established Mobile Business Division

The conditions necessary for success in the Mobile business include (1) ownership of popular content that can be differentiated amidst numerous competing titles and (2) management expertise in analyzing user trends and the incorporation of those trends into development.

Until now, we developed the Capcom brand, which utilized popular Capcom content in Japan, and the Beeline brand, which licensed content from other companies for global use in games targeting women and families. Under the Capcom brand, although we unified our domestic development structure and achieved a hit with *Monster Hunter Explore*, other existing titles struggled, adversely affecting sales for the past few years. Under the Beeline brand, we have been unable to generate ongoing hit titles since 2010 and sales have continued to decline. In April 2016, both structures were

integrated to establish the Mobile Business Division in order to focus on global development of Capcom IP. Next fiscal year, we will combine our library of popular content with our management expertise to release new titles in the *Sengoku BASARA*, *Mega Man* and *Monster Hunter* series and promote a structure for the ongoing release of titles. In addition, we will attempt to expand profits in Asia via licensing hit titles from Japan and overseas in the Asian region, while at the same time moving forward with M&A, targeting development companies as part of management line integration.<sup>[Diagram 19]</sup>

Through these measures, we first aim to acquire a 5% share in the domestic market over the medium term, then will attempt to maximize profit opportunities overseas by leveraging market analysis capabilities and management expertise cultivated in foreign markets under the Beeline brand.

#### Measure 2 Promote Business Alliances in the Asian Region

We believe the licensing of existing Online content in Asia has the potential to significantly accelerate Capcom growth.<sup>[Diagram 20]</sup> There are two ways to proceed in Asia: (1) engage in Capcom development and management through subsidiaries in the Asian region and (2) engage in development and management through business alliances with major Asian management companies. At present, we are focusing efforts on the latter.

In terms of an example of full-fledged development in Asia, we can point to *Monster Hunter Online (MHO)*, launched in collaboration with Tencent Holdings in China in December 2015. The game was well-received by users after distribution, giving us a solid footing in terms of content development in China.

The reason we are promoting business alliances in addition to internal development is to avoid country risk in Asia and gain management expertise. Thus, we have determined that at this time, alliances with leading companies in countries other than Taiwan are an effective means of maximizing earnings. Developing hit content from the Consumer business under our Single Content Multiple Usage strategy, making use of this content in the domestic PC Online business and licensing the content in Asia is a business model enabling Capcom to earn double or triple profits from the same content. In addition, we can also apply Online business management expertise to the Consumer business; thus promoting these strategies will enhance synergies with the Digital Contents business.

**Diagram 19**  
**New Mobile Game Strategy**

**Before Development Resources Split**

| Capcom Brand                      | Beeline Brand                              |
|-----------------------------------|--|
| Develop apps using proprietary IP | Develop apps using IP from other companies |
| Mainly in Japan                   | Global                                     |
| Capcom fans                       | Casual female users                        |

**After Development Resources Concentrated**

| Capcom Brand                                | Beeline Brand                               |
|---|---|
| Develop apps using proprietary IP           | Develop apps using IP from other companies  |
| Global expansion focused in Asia            | Global expansion                            |
| Broad segment including all genders or ages | Broad segment including all genders or ages |

By integrating the Capcom and Beeline Brand organizations, which until now had promoted independent strategies, development and management expertise has been concentrated in the Mobile Business Division. Quick decision-making enables global expansion of titles utilizing proprietary content.

**“ Strengthen the licensing business in the Asian region with planned distribution of four titles using popular brands including *Monster Hunter*, *Sengoku BASARA* and *Mega Man* ”**

**Diagram 20**  
**Alliances and Titles in the Asian Region**

| Title  | Region                                | Alliances  |
|--|---------------------------------------|--|
| <i>Monster Hunter Hunting Quest</i> (Simplified Chinese version)         | China                                 | Qihoo 360 Technology Co., Ltd.   |
| <i>Street Fighter Battle Combination</i>                                 | China, South Korea, Taiwan, Hong Kong | Teeplay Interactive Ltd.   |
| <i>Street Fighter IV Arena</i>   | South Korea                           | Nexon Korea Corporation  |
| <i>Monster Hunter Online</i>   | China                                 | Tencent Holdings Ltd.  |
| <i>Onimusha Soul</i> (Simplified Chinese version)                        | China                                 | Cayenne Entertainment Technology Co., Ltd. (Taiwan), BLUE PANDA Network Technology Co., Ltd. (China) |
| <i>Monster Hunter Mezeoporuta Kaitakuki</i> (Simplified Chinese version) | China                                 | Tencent Holdings Ltd.  |

**“ Reinforce business alliances with powerful local companies ”**

In the PC Online business, we are engaged in negotiations in China, the world's largest online game market, as well as in South Korea and Thailand. Similarly, in terms of Mobile Content, we are enhancing development making use of leading titles in the Asian market where the adoption of smartphones continues at a brisk pace.

Conversation

## Focusing on Growth: Adapting to the Operational Model and Maximizing Utilization of Proprietary Content

**Haruhiro Tsujimoto**

President and Chief Operating Officer (COO),  
Capcom Co., Ltd.

**Jay Defibaugh**

Senior Analyst, Research Division  
CLSA Securities Japan Co., Ltd.

**Analyst Jay Defibaugh and President and COO Haruhiro Tsujimoto discuss how Capcom will promote its growth strategy amid a major revolution in the Consumer game market driven by the expansion of digital distribution.**

**Jay:** The digital distribution of games has solved a number of distribution issues overall, and Capcom has been able to steadily grow its sales in the US, Europe and Asia as well. However, as some of your overseas competitors have already grown their ratio of digital distribution to nearly 40%, I feel that Capcom's ratio is still quite low. How do you plan on improving this going forward?

**Tsujimoto:** At present, the merits of digital distribution translate only to sales; however, if we utilize the always-online connectivity of consoles, we can offer new and improved ways to enjoy games as a service managed over the long-term, which will stimulate new needs. To this end, we plan to coordinate with first party developers, who maintain the user data.

**Jay:** In terms of improved profitability from digital sales, you are able to create sales opportunities in Southeast Asia and other regions where until now package sales had been impossible. At the same time, post-sales

management and marketing capabilities will become more critical. Does Capcom possess this operational expertise?

**Tsujimoto:** Although there is still room for improvement in this area, we will utilize our experience in the Online and Mobile businesses to create a new internal structure geared toward service-oriented management. We will pursue a policy whereby we gradually increase the digital download ratio while researching competitor products and user behaviors.

**Jay:** Investors consider Capcom to be a "company able to create powerful content," but my sense is that you haven't put out much successful new content recently despite the ongoing release of new high-performance game consoles. Going forward, will you be able to continuously release quality IP? Also, some overseas competitors have shortened the time required to develop sequels using a two-team system. What kinds of initiatives is Capcom engaged in?

**Tsujimoto:** The creation of new IP is the cornerstone of our business, so we must perpetually engage in it. If we are unable to continue generating content qualitatively equal to global AAA titles, Capcom has no future as a company specializing in games. In terms of shortening the time required for development, we are engaged in streamlining from a technical standpoint, including the development of our RE ENGINE and innovations in 3D scanning systems, which will enable us to develop major IP on a two and a half year cycle.

**Jay:** A lot of Capcom IP is lying dormant, and although

**Profile: Jay Defibaugh**

Graduated from Penn State University in 1989; began covering the game industry as an analyst in 1999. Joined CLSA Securities in 2013.

“Move toward maximizing usage of IP”

you are skilled at creating IP, I get the impression you are not as skilled in terms of marketing aimed at leveraging IP. The ideal scenario is one in which you make the most of your IP to maximize profits. What are your thoughts?

**Tsujimoto:** Despite our basic strategy of Single Content Multiple Usage, it's true at present there are some IPs we certainly have not made the most of. Titles that had large fanbases in the past are powerful assets, thus we are beginning to move toward maximizing usage through region-based testing of individual IP and the release of promising IP remakes and reimagined titles.

**Jay:** The subject of IP usage also applies to Mobile games. Capcom has yet to realize major success in this ever-expanding market.

**Tsujimoto:** Mobile platform strategy is one of the issues we must address in the Mobile business. Considering future smartphone performance enhancements, I think there is a significant opportunity for us to leverage our strengths. Recently, we switched over to a development structure mainly focused on Capcom IP and integrated our Mobile structure in order to create hit titles.

**Jay:** Alternatively, wouldn't focusing on the Consumer business, with its strengths in in-house resources, while

collaborating with other companies on licensing for Mobile achieve higher management efficiency?

**Tsujimoto:** Going forward, regardless of the platform, there is the potential to transition any category of game into the long-term operational model. Thus, the accumulation of data analysis, marketing and other Mobile management expertise will be effective not only in the Mobile business, but also in the Consumer business. If we license out titles, it will be difficult to accumulate in-house expertise. This is why we must continue to invest in comprehensive internal strengths—even in the Mobile business—to achieve success.

**After the Conversation**

I sensed the COO's confidence in terms of Capcom IPs. I have no doubt about his basic strategy of creating excellent content and maximizing the usage of these assets. Compared to competitors, Capcom has allocated a modest amount of resources to the Mobile business. Given their business structure this is understandable, but the fact is, when looking at the game industry overall, the mobile market is expanding rapidly. In certain situations, being flexible with regard to development and borrowing some of the strengths of other companies would be entirely acceptable from the investors' point of view. I feel this would present Capcom with significant opportunities. (Jay)