Armed with “World-Class Development Capabilities” and “Leading Contents”, Capcom Aims to Maximize Profits through Opportunities in the Rapidly Changing Game Market

Despite lower sales and profits in the fiscal year ended March 2012 due to the backlash of releasing of multiple major titles in the previous fiscal year, Capcom is realizing steady achievement with 21.7% growth in the Online business, the core of our growth strategy.

The following is an explanation of Capcom’s strategy for achieving its medium-term business goals by turning new changes in the game market into profit opportunities based on a robust development structure created via structural reforms up to now.

Capcom’s No. 1 Strength
Development Capabilities as Competitive Advantage for Global Success

In the contents industry, generation of new content is the source of a company’s competitiveness. One of the reasons Capcom has continued to grow is due to our core Consumer Online Games business’ “ability to provide superior content” through the utilization of strong development capabilities for creating a large amount of original game content.

Capcom’s superior development capabilities maintain “developer creativity” and an “organizational structure that enables developers to hone their skills”, two factors successfully realized through the next several structural reforms.

Capcom’s No. 2 Strength
Extensive Collection of World-Class Leading Content

The originality of content created by Capcom using the world-class development capability is, naturally, held in high esteem by users. We attempt to secure stable earnings by creating new million-seller titles once every two or three years, and introducing the sequels of these titles regularly, such as “Street Fighter” and “Resident Evil”, which have sold over one million copies worldwide. We possess the most popular contents among Japanese game software manufactures, and development capabilities continue to be one of our biggest strengths.

Furthermore, possessing scores of content with universal market appeal enables us to develop our Single Content Multiple Usage strategy worldwide. Based on our success in the Consumer Online Games business, we have engaged in the multiple development of popular content for various forms of media which has led to success in other businesses, and we are now creating a business model to realize multiple profits in the contents market as well.

Strategy for Growth
Three Growth Strategies For Achieving Medium-Term Business Goals

As a result of last fiscal year’s platform expansion, the game market was worth 52.9 billion dollars in 2011 (up 19.1% from the previous year). The market is expected to expand significantly, reaching 79.9 billion dollars in 2016.
The online game market expanded rapidly to 30.4 billion dollars (up 44.8% from the previous year) in 2011. Reasons for this include, in accordance with advances in broadband networks, (1) high-speed PC and mobile phone communications, (2) the spread of smartphones and tablets, (3) the expansion of social networking services (SNS) and (4) home video game console online functionality that enables online game platform connecting high-performance devices such as PC, smartphone, iPad and a wide range of other consoles to the home video game console. As a result, the online game market is expected to grow steadily to 58.2 billion dollars in 2016 (up 91.4% from 2011).

The traditional home video game market was worth 22.5 billion dollars in 2011 (down 3.8% from the previous year). The market is expected to remain flat, growing slightly to 21.7 billion dollars in 2016 (down 3.6% from 2011). Despite this outlook, we nevertheless foresee maintaining these operations as a primary point in the game market five years hence.

In response to the changing market environment, and to achieve our medium-term business goals (please see “CEO’s Discussion on the Summary of This Year’s Performance and Medium- and Long-Term Business Goals”, Q4, on P. 20), Capcom has outlined three major strategies for growth, which are: “strengthening of our Online business”, “expanding our line-up of games under development” and the “expansion of Single Content Multiple Usage”, and will allocate 90% of management resources to the Consumer Online Games and Mobile Contents businesses promoting these strategies.

One factor behind the forecast for Capcom’s best performance ever next fiscal year (ending March 2013) is that our growth strategy is already beginning to achieve success. Also, to further ensure the achievement of medium-term business goals, we will expand the platform and territory of the Online Games business and increase share in the mobile and PC online markets. Additionally, we will attempt to shorten the sales cycle of major titles through development staff enhancements and design process efficiency, creating a structure to deliver stable earnings every year. Furthermore, we will continue to focus efforts on the development of Single Content Multiple Usage, which is at the core of our business development.

On the following pages, I will explain each of our three growth strategies.

**Market Strategy** ➔ P25
Strengthening Online Businesses Worldwide, the Pillar of Growth

**Development Strategy** ➔ P27
Creating a Stable Title Portfolio by Shortening Cycle for Release of Popular Series

**Media Strategy** ➔ P29
Expanding Single Content Multiple Usage Development
Here, I’d like to explain the “strengthening of the Online business”, the first of our growth strategies for achieving medium-term business goals.

Online business measures include (1) increasing the number of mobile and PC social games, (2) enhancing downloadable content (DLC) for home video games, (3) developing PC online games by region and (4) enhancing development staff. By implementing these measures, we will grow Online business sales to 23,000 million yen (up 46.5% from the previous year) in the fiscal year ending March 2013 and 30,000 million by the fiscal year ending March 2015.

Aiming for Online Business Sales of 30,000 Million Yen in 2015

This measure has three points. First, expand domestic market share by increasing social game titles making use of the “Capcom brand”. Second, acquire a wide range of customers by strengthening “Beeline brand” management structure and releasing major titles. Third, introduce a new PC browser game into the market. These three actions will intensify connections with users and bring in new customers.

“Capcom brand” strategy, with regard to the first point in particular, is to attract mobile lights users to home video games and home video game core users to mobile content with the development of social games utilizing the brand power of popular Capcom titles created in Japan. Furthermore, we will actively provide content by significantly increasing the number of social games released through alliances with proven outside development companies such as gumi Inc. and gloops, Inc., while developing GREE and other domestic platforms for overseas distribution.

The second point is that we will continue to strengthen social games for smartphones with the “Beeline brand” strategy. The reason for creating a separate brand stems from Capcom brand games having an image of difficulty and complexity about them, creating a barrier that would prevent most light users who normally don’t play games from purchasing a casual download. The appeal of a new brand is more effective. Furthermore, development facilities in North America,
Europe and Japan are developing social games that incorporate distinctive characteristics to acquire users in developing regions where home video game consoles have yet to be adopted. With major title “Smurfs’ Village” ranking as the “top-selling app” in the App Store sales rankings in 80 countries and downloads of “Beeline” titles in Japan and overseas in excess of 56 million, we are already realizing the achievement of our growth strategy. Moreover, with 43% men, 57% women and approximately 1.5 million active players over 50 years old, “Beeline” user composition is extremely well-balanced. In terms of the overseas title lineup, next fiscal year (ending March 2013), Beeline will release 15 titles, including “Shrek’s Fairytale Kingdom” featuring popular Western character from another company “Shrek”, accelerating growth with Mobile Contents sales of 12,000 million yen (up 90.5% from the previous year).

The third point involves establishing a new revenue source with the release of PC browser games “Onimusha Soul” and “Browser Sengoku BASARA”.

Capcom will develop PC online games in Asia and South America, utilizing popular home video games with a global appeal. At present, we distribute “Monster Hunter Frontier Online” (MHF) in Japan with an eye towards development in China, soon to be the world’s largest online market, expanding distribution regions by region. Also, to avoid country risks and acquire management experience in these regions, we will develop business partnerships with leading local companies. At the same time, while releasing new titles in Japan, we will make regular major updates to MHF to maintain user interest and improve earnings stability. We forecast sales in the next fiscal year (ending March 2013) of 7,500 million yen (up 13.6% from the previous year).

In this second phase of structural reforms, Capcom Integrated its vertically segmented consumer, mobile and online development structures, switching to a new multi-platform development system compatible with all types of hardware. Additionally, we integrated global organizational functions with new facilities and absorption of organizations around social games.

Moreover, we will increase development staff and provide in-house training. We plan on hiring 300 new employees, mainly new graduates, next fiscal year to implement above measures 1-3.


**Development Strategy**

Creating a Stable Title Portfolio by Shortening Cycle for Release of Popular Series

Diagram 19  Shorten Sales Launch Plans of Popular Series Titles

At present  3-4 year popular series title development

<table>
<thead>
<tr>
<th>Series 1</th>
<th>Series 2</th>
<th>Series 3</th>
<th>Series 4</th>
</tr>
</thead>
<tbody>
<tr>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
</tr>
</tbody>
</table>

Sales cycle: 1 title every 3-4 years

Fans begin to lose interest

1st year  2nd year  3rd year  4th year  Ongoing fans  New fans

Lost interest increases sales risk for next title

Going forward  Shorten development period of popular series titles to 2.5 years, make use of downloadable content (DLC)

<table>
<thead>
<tr>
<th>Series 1</th>
<th>Series 2</th>
<th>Series 3</th>
<th>Series 4</th>
</tr>
</thead>
<tbody>
<tr>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
<td><img src="image.png" alt="Diagram" /></td>
</tr>
</tbody>
</table>

Sales cycle: 1 title every 2.5 years

Release DLC

1st year  2nd year  Ongoing fans  New fans

Increases fan numbers and earnings

Note: The above figures are provided as an example to facilitate understanding of the strategy. This is not the official plan.

**Aiming for Medium- to Long-Term Growth by Increasing Number of Package Titles Released in a Single Year**

This section explains the second component of our growth strategy, which involves “expanding our line-up of games under development”, necessary for achieving medium-term business goals.

For Capcom to achieve sustainable and stable growth in the game software industry, where the presence or absence of hit products dictates performance, we mapped out a 60-month title development plan that lays out a medium- and long-term development schedule for multiple major titles in the first phase of structural reforms. By organizing efficient development teams according to this plan, we are able to invest in sequels to multiple popular games each year, which enables stable growth in the Consumer Online Games business. Also, we must further increase single-year sales of major software to achieve medium-term business goals.

To this end, we are promoting (1) a shorter sales cycle for popular series titles and (2) the launch of new titles to create a title portfolio facilitating sustainable growth over the medium- to long-term.

Measure 1  Shortening the Development Cycle of Popular Series Sequels with an Efficient Development Structure

(1) “In terms of shortening the sales cycle of popular series titles”, we launch sales of popular series titles held by the Company approximately every 2.5 years. This is because the development of a single major title usually requires 3-4 years; in the event that there are few hits, it will be difficult to create a series title every year and earnings will be adversely impacted. For this reason, it is important either to maintain a large number of popular titles or shorten the sales cycle to ensure stable earnings. Among the multitude of major titles held by Capcom, such as “Monster Hunter”, “Street Fighter”, “Resident Evil”, “Devil May Cry”, “Lost Planet”, “Dead Rising” and many others, we will promote shortening of the sales cycle in pursuit of further earnings stabilization and growth.

Specifically, teams developing major titles will be limited to 100 members, with multiple sequel titles developed at the same time. Also, as it will be necessary to create a large-scale development structure for shortening the development process, we will strengthen in-house...
Having established the new brand, Capcom will allocate approximately 20% of development investment funds to enhance the strength of a new hit title-creating lineup. The reason is because popular games have a solid fan base, and when they become a series, there is a high probability that users and retailers will purchase and stock the sequel based on past game content and sales performance, which, in turn, increases the likelihood of a string of hits. In the next fiscal year (ending March 2013), we plan to release new titles including “Dragon’s Dogma”.

In this way, we will create a title portfolio enabling sustainable growth over the medium- to long-term by shortening the sales cycle, regularly distributing DLC during blank periods while releasing series titles at the appropriate time and strengthening our lineup with the launch of new titles.
Media Strategy

Expanding Single Content Multiple Usage Development

Multiple Revenue Streams from Single Popular Content

This section will explain the “expansion of Single Content Multiple Usage” in terms of the aforementioned three growth strategies formulated to achieve the medium-term business goals.

A “home video game” is an artistic media product that consists of highly creative, multi-faceted elements such as images, storyline, a worldview, music and interactive game play. This is exactly why each of these constituent elements can be individually developed into an attractive product through different facets of media.

Therefore, we can expect the following four effects by developing each of these elements into different business fields: (1) creating new profit opportunities other than the Consumer Online Games business; (2) creating heightened excitement through increased exposure by simultaneous multiple-field development (promotional effects); (3) absorbing customers obtained from other business segments as home video game users; and (4) reducing profit fluctuations through business portfolio creation (risk hedge).

We own scores of intellectual properties based on popular content. We are now creating a business model to enjoy multiple profits by promoting Single Content Multiple Usage strategy in several applications. This strategy will allow us to leverage the success of our Consumer Online Games business with the aim of maximizing profits and achieving success in other businesses (Mobile, Pachinko & Pachislo, Arcade Games, Movies, Publishing, Character Goods, etc.).

Media Development Incorporating Various User Segments

This fiscal year (ended March 2012) in the film-related business, “Sengoku BASARA -The Last Party-” drew 210,000 people to the theatre and brought in 300 million yen at the box office, while “Ace Attorney” was a big hit with a box office take of 520 million yen and 405,000 in attendance.

Other examples of multi-development include “Monster Hunter”...
with the launch of home video game “Monster Hunter 3 (Tri) G”, the release of home video games “Monster Hunter Freedom 3 HD Ver.,” and “MONHAN NIKKI POKAPOKA AIRU MURA G”, as well as the distribution of social games “Monhan Tankenki Maboroshi no Shima” and “Minna to Monhan Card Master”. In addition, we held “Monster Hunter Festival 2011” in six locations across Japan, the “Monster Hunter World” event at amusement park Greenland (Kumamoto Prefecture) where fans can experience the “Monster Hunter” world and “Monster Hunter the Real 2011” at Universal Studios Japan (USJ). Furthermore, we held “Monster Hunter Orchestra Concert: Hunting Music Festival 2011” with the Tokyo Philharmonic Orchestra and the “Monster Hunter X Shinshu Hot Springs” tourism event was held at the hot spring resort Shibu in Nagano Prefecture attracting many fans and creating synergy with games.

The film release and “BASARA Festival 2011 – the Summer Campaign” event were timed to coincide with the launch of home video games “Sengoku BASARA: Chronicle Heroes” and “Sengoku BASARA 3 Utage” and a “Sengoku BASARA” attraction was installed at Fuji-Q Highland. Also, we helped contribute to regional vitalization through tie-ups with the Bizen Osafune Japanese Sword Museum.

In collaboration with Pasela Resorts Shinjuku’s main store we opened the Capcom Bar, which serves Capcom game-themed food and drinks in an effort to create a buzz and expand our fan segment.

With the objective of continuous multimedia development of popular Capcom content focused mainly on “Monster Hunter”, “Sengoku BASARA” and “Resident Evil”, starting next fiscal year we will attempt to improve brand value and profitability by not only making as wide an appeal to as many customers as possible, but also by contributing to regional vitalization.
Accelerating Online Strategy

Capcom’s online development is garnering attention from the market. In particular, mobile social game “Smurfs’ Village”, released under the Beeline brand in 2010, was a global success; you have also begun aggressively distributing content on GREE and Mobage.

With regard to online development, we were a bit late to enter the domestic social game domain, but we have finally solidified our lineup and gained expertise along the way. From now, we will develop social games from popular package games with the objective of getting this area on track. “Resident Evil: Outbreak Survive” (GREE), which began distribution in June 2011, already has more than two million members. “Monhan Tankenki Maboroshi no Shima” (GREE) and “Minna to Monhan Card Master” (Mobage) have over one million members each, and we feel this response means we are winning support among a wider population outside traditional game users.

Besides social games, with PC online games like “Monster Hunter Frontier Online”, package game downloadable content and Capcom’s entry into the recently rising PC browser market, it appears you are stepping-up online development. How do you see each platform growing?

What is important for Capcom, rather than how each platform will grow, is to create better games that more people can enjoy playing for a longer time. For example, the traditional package game usually ended when the story was cleared, but upgrades to hardware and telecommunications technology and the advent of the paid content in-game system enable the download and enjoyment of new stories. Anticipating these kinds of changes, I think overall expansion of the online business domain is important.
and services will become integral to the game business going forward. Confirmation of user satisfaction linked to more satisfying projects with package games sold at stores, but now it begins after sales. Direct opportunity— I think this is the key to success. Traditional business ended through significant changes, so the issue is whether we can seize this companywide profit model. The game distribution structure is going through tremendous changes. However, I think these changes offer new opportunities for growth. For example, in Asian nations, even with brand recognition, there were profitability issues in the package business. However, going forward, with the rise of smartphones and tablets, we will attempt to improve profitability through the distribution of online content.

This means that the time has come to restructure this into a companywide profit model. The game distribution structure is going through significant changes, so the issue is whether we can seize this opportunity— I think this is the key to success. Traditional business ended with package games sold at stores, but now it begins after sales. Direct confirmation of user satisfaction linked to more satisfying projects and services will become integral to the game business going forward.

Capcom’s Strengths and Responding to Changes

In terms of promoting strategy, what are Capcom’s strengths? The first is the originality of our content. The majority of our games have highly original stories and characters. And, the root of all this is the ongoing creation of content intended to always satisfy users. Second, is the Single Content Multiple Usage strategy, which we have pursued for some time. We grow our fan segment by developing game content for multiple media. Our third strength is global development. I think expanding our content not only domestically and in developed countries, but also in developing countries and throughout the entire world, will enhance our brand power.

Because of expansion in the online domain, I suspect traditional thinking may no longer apply in some areas. In fact, given the extreme complexity of business composition, it is difficult to understand conditions looking at the stock market; have any new issues spring up in response to changes in the business environment? There is no doubt that the business environment is undergoing tremendous changes. However, I think these changes offer new opportunities for growth. For example, in Asian nations, even with brand recognition, there were profitability issues in the package business. However, going forward, with the rise of smartphones and tablets, we will attempt to improve profitability through the distribution of online content.

This means that the time has come to restructure this into a companywide profit model. The game distribution structure is going through significant changes, so the issue is whether we can seize this opportunity— I think this is the key to success. Traditional business ended with package games sold at stores, but now it begins after sales. Direct confirmation of user satisfaction linked to more satisfying projects and services will become integral to the game business going forward.

A Corporate Culture Able to Continue Taking on Challenges

Globally, there are many new players entering the game industry. It appears that market competition is entering a new phase; what is your outlook for future growth?

Many new players are evidence of the industry’s potential. An insular industry is one that is on the decline. Given present conditions where individual manufacturers are able to engage in steady and direct contact with each user, it is possible that a giant market may suddenly emerge unexpectedly. This age of unpredictability is also one of great opportunities. Platform diversification and global expansion are driving up development costs every year, but as it is management’s mission to generate steady profits, I want to aggressively invest in growth.

This fiscal year, you released the first new title in a while with “Dragon’s Dogma”. How is it going?

I think stable growth is difficult with only the titles we have now. We invigorate the company by creating new titles. Actually, from this year we increased the number of new graduates we employ, plan to increase our development staff by 100 people each year and are strengthening our educational system. Always striving to continually improve is Capcom’s corporate culture. I think that, just like life, this is growth.

After the Conversation

The important point when evaluating game companies is the strength of their content. In addition to this, global business development, approach to pursuit of profit opportunities and commitment to constant objectives are also important. Capcom aggressively engages in all these initiatives. In particular, I highly commend their pursuit of originality and acceptance of risk symbolized by new title “Dragon’s Dogma”. In terms of global development, I have high expectations that their use of the Beeline brand will increase user segment. Because of the complexities of online business, it is difficult to see progress in each area; from now, changes in the number of members for each titles and disclosure of other detailed information will further heighten market expectations. (Mia Nagasaka)

Mia Nagasaka (Profile)

Mia Nagasaka joined Morgan Stanley MUFG Securities in July 2010. Previously she worked at Bank of Tokyo-Mitsubishi UFJ and Barclays Capital Securities, and has covered the game sector since 2007. She graduated from Keio University’s Department of Humanities and Social Science and received a Master’s Degree from Keio Business School. While in graduate school she studied at the Wharton School at University of Pennsylvania.