

FY2008 Third Quarter Financial Report Q&A Summary

Q. Can we expect that the Pachinko & Pachislo Businesses will grow during the next quarter? Or should we expect it to remain at the same level?

A. We recognize the overall market environment is poor, but we can predict our performance somewhat, because we employ a commission based production system, which provides some guarantee. Regarding the question of whether our business will grow in the next quarter and beyond, we can not answer the question explicitly, as we are currently finalizing our business plan.

Q. Six new stores in arcade facilities in the 3rd quarter seems quite a lot to me. Is there any factor involved which makes this favorable, such as lowering your cost for opening stores while other companies are closing their stores?

A. Answering the question of whether or not the cost of opening stores is generally getting lower, we believe the cost has not dropped considerably, but that negotiating terms and conditions is somewhat easier. Opening six new stores is a result of pursuing our policy: we would like to choose stores along the principal of scrap-and-build, closing unprofitable stores as much as possible and opening stores in profitable arcades. In this regard, there were some non-lucrative stores in the fourth quarter, so we are planning to close down such stores early.

Q. There is a line on page 3 of your Financial Results referring to investment in the company producing the “Street Fighter” movie, and I think that former Chief Operating Officer Tsujimoto acted in “Street Fighter” before. Do you have any idea who will appear from your company in the movie?

A. 1) No. Certainly the movie “Street Fighter,” produced about 15 years ago, was a great success. We are not concerned about the amount of money we spend this time as a part of the film production committee, since the movie is not a big investment. Regarding progress, the casting is mostly finished, and the movie will probably start filming soon. The production company is sound, so we are not going to take any risks. We forecast that probably the film will perform averagely and obtain ordinary results, making an acceptable profit.

2) Since we are not a film company, we do not intend to invest on a large scale in movies at all. The original purpose of the investment is collaboration between games and films. “Resident Evil Extinction”, distributed last November in Japan, was a great success. We released the game “Resident Evil: The Umbrella Chronicles” at the same time, and the number of shipments increased in a synergistic manner. This time, as we participate in the new movie “Street Fighter”, we obviously plan to release another “Street Fighter” game. We have been considering how to collaborate between the two media. In this context, we decided to invest in the movie “Street Fighter” now, as it stands.

Q. Today, Namco Bandai Holdings Inc. announced that they will close down about 20% of their game arcades, so I assume that your Arcade Operations Business is also grim. Do you think that we should accept that the Arcade Operations Business will be scaled down in the future? Please give us your opinion, including measures to strengthen the business.

A. Our company only has around 40 stores, most of which are large. There are quite a few small stores which are not at all profitable. However, the market environment has been changing. We are not considering a large scale closure of our stores, but may close down stores gradually, with some immediate closures based on the scrap-and-build strategy which I mentioned earlier. Yet, we are going to watch the situation, since there is a chance that customers will come back to game arcades when the market environment improves.

Q. Do you think factors such as Wii contribute a lot to this condition?

A. 1) One reason is that we had so-called “killer content” in the Arcade Operations market in the past, and at one time a lot of children went to the game arcades for card games. But that was several years ago. Now, we don’t have such killer content any more.

2) In addition, today, children play with home video games. Since the market for home video games is doing fine, not only children, but also adults purchase home video games. This is a big factor. When you look at past trends, you will notice that there have been a few years when the performance of the Home Video Games Business was good while the Arcade Operations Business was poor, as when there was a change in video game platforms with the release of PlayStation or PlayStation 2. We are currently in just such a cycle. Therefore, if such an environment or trend changes, customers are going to return. We will properly assess any such situation. We will closely review our store operations once more on an individual basis of whether the store is profitable or not, then proceed to scrap-and-build. This is our company’s strategy.

Q. First of all, please tell us how to view the Home Video Games Business situation. I remember you mentioned a total figure of 13.5 million units for the current period. I would like to know your view of the growth rate for the next period compared with these thirteen and a half million units, as well as any major titles you currently have in mind.

A. Our plan in the current term is to ship 13.5 million units (as announced in the revised projections for Mid-term Financial Results). In the next term, as I always tell each business department from the management side, we tentatively aim to grow by 10% in the next term. If the Home Video Games Business grows by 10% as well, based on 10% of 13.5 million units, in simple math, we will sell 15 million units. However, we can’t expect to target this level yet.

Q. In your Home Video Games Business, would you be willing to give us more details if possible, such as the breakdown between consoles and handheld computers, and how you prioritize regarding each platform? Also, I would like to know if there has been any change over the last half year.

A. There is no change in our strategy. Speaking in broad terms, we sort titles by their place of distribution, either for the Japanese market or the foreign market. The images of our influential titles overseas are remarkable. For PlayStation 3, Xbox 360 and PC, we are going to release games overseas for these three platforms. Referring to platforms in the domestic market, the market for Wii editions is quite large due to the number of units in the market. We believe that our company should actively develop software for Wii. Nevertheless, we are very cautious, and have revised our title line-up somewhat every month, because the games will be ineffective if we don't take their quality and attributes into account during development. Hence, there isn't a big change in our policy, and we are still pursuing multiple-platforms. As we are always saying, our company has good content. Our concept is to use such content properly in profitable areas.

Q. Do you think you are developing your young software producer talent pool? Capcom is able to produce world-class titles very consistently, so I suppose your company must have excellent human resources creating such titles. If there is any know-how or knack to developing such human resources, could you tell us?

A. If you are asking me whether we have capable human resources or not, I am proud to say that we do. Basically, our company mainly employs new graduates, and about 40-50 of them join our company every year. We also employ mid-career workers, so we have a good mix producing game software. However, more than 80% of our company's workers are specialists, and we have a lot of employees who have worked for our company more than 10 years. We assign each newly employed graduate worker to teams consisting of about three members, and give them a year's on-the-job-training. This software development human resource program is not a recent development, but has been in use for a long time. This method enables workers to create new content and achieve great success as game software producers. When they reach a certain level, we give them posts as lead programmers or designers for major titles, or we promote them to director positions. Our human resource development is fairly hands-on. Our company is located in Osaka, a unique region, and compared with other companies, our turnover is small, especially among the younger generation. We believe this is our strength.

Q. I would like to ask about the Arcade Games Sales Business. There was an unfortunate accident with Coin-operated game, but I see that Coin-operated game getting stronger in the future. Accordingly, please tell us about your strategy for taking firm steps on this issue.

A. We regret the accident that occurred due to trouble with a machine. Now we are making it our motto to go back to the drawing board, and start development from scratch again. We don't think we can immediately recover from the accident. We are currently prioritizing quality control measures. We apply basic quality control, such as removing the problematic part when we analyze the machine's structure. This is the basic philosophy of our product developers. We endeavor to inculcate such an attitude in our workers, but we sense this is not going to be easy. On the other hand, we don't worry too much about the Arcade Video Game Machines, as it is tied in with the Home Video Games Business. In fact, we believe the business is performing quite well. Consequently, in the area of Coin-operated game, we are striving to gradually improve them by introducing a mechanism for clearly controlling product quality.

Q. I would like to raise a few questions about the Arcade Operations Business. I presume Capcom's main stores are at malls, but you have also stepped up suburban stores lately. If you could classify your stores into these two types, which type of existing stores have poorer performance?

A. It's difficult to answer this question, because business performance in stores depends to a fair extent on the quality and size of the stores, as well as their locations. In addition, we know from our analysis that there are certain rules, and that if we open stores which don't fit the framework of these rules, they don't perform well. So we recognize that the success of stores is not simply a question of whether the store is in a mall or in a roadside arcade.

Q. According to previous explanation of strengthening measures, due to its small number of stores Capcom isn't really considering closing stores, and will instead focus on revitalizing existing stores. Is my understanding correct?

A. Yes. As you mentioned, we are not thinking of completely shutting down, for example, 10 stores at once. We usually close down about three stores a year, so we are considering shutting down three to four stores for the foreseeable future. The measures we are planning to implement are to improve the effectiveness of stores, and to review the kinds of products in them. If there are popular titles or gifts for prize-winning games, we will introduce them without any hesitation. We are pursuing this kind of system for stores.

Q. Do you expect these steps will increase profitability sufficiently?

A. Correct. We don't think that the situation will significantly improve in the next period, but we are aiming to reshape our stores by pursuing the right steps, in order to raise net profit when the market environment improves.

Q. Could you explain how to look at your upwardly revised net sales and operating income, by segment?

A. To put it very simply, the figure for the Home Video Games Business was revised upwardly.

Q. So you didn't particularly change the figures for the Arcade Operations Business, did you?

A. The figure in the business is lower than the original plan. So the situation is that the figure dropped in the Arcade Operations Business, but rose in the Home Video Games Business. We haven't changed the figures in the Arcade Games Sales Business or the Contents Expansion Business.

Q. You said that the figure for the Arcade Operations Business was lowered; how far did you reduce your assumption for existing stores?

A. The result in the third quarter was 80% on a year-on-year comparison, but it was supposed to be much higher in our plan for the total period. So we currently envisage 80% to 90% on a year-on-year basis.

Q. My question is about Home Video Games Business. You revised the sales plan for "Devil May Cry 4" in the fourth quarter up by 100 thousand units. Is this because you are taking its first shipment result in Japan into account?

A. We expect not only Japan's figures, but also worldwide anticipated figures to increase somewhat. That total figure is 100 thousand units, and the upward difference is not all due to the increase in domestic sales.

Q. Looking at in three-month period, over the past three months, your net sales increased 2% compared with the same period the previous year, while sales and general administrative expenses increased 21% by comparison. Since the net sales in the Home Video Games Business itself increased 57%, I wonder if you spent a lot of money for advertising. Is my analysis right?

A. Yes, you are right. As you pointed out, our Home Video Games Business advertising expenses certainly increased compared with the previous year.

Q. I think that the previous budget for advertising expenses including sales promotion was estimated at 5.4 billion yen for the whole period. I wonder whether this estimate has not changed.

A. I think the expense will be higher than the estimate to some extent.

Q. My question is about "Devil May Cry 4". As I presume you already have the initial number of shipments for that software, I would appreciate it if you could tell me that figure. Supposing the diffusion rates of video game platforms in PlayStation 3 and Xbox 360 are about 2 to 1, I would like to know the figures regarding video game platforms, if possible.

A. We don't have the breakdown for the figure by platform, but the initial shipment is 400 thousand units in the Asia region including Japan, 700 thousand units in North America, and 740 thousand units in Europe, totaling 1.84 million units at this point.

Q. Is there any breakdown by platform? You don't need to be precise. The ratio of 2 to 1 is not so far off, is it?

A. It might be a bit different from that. I think that sales for PlayStation 3 are better than we expected.

Q. My question is about the forecast for a total software shipment of 13.5 million units over the whole period, which, I think, has not changed from the previous estimate.

A. That's right, we haven't changed it.

Q. You mean you simply haven't changed it yet? The reason I asked is because you increased expected title sales for "Devil May Cry 4" and "Monster Hunter Freedom 2 G". Do you expect lower sales than before for other titles?

A. No, we just haven't reviewed total sales yet. Some titles, including distribution titles, which we originally planned to release in the fourth quarter, will be released the following quarter, so we haven't recalculated the total number for the whole fiscal year yet.

Q. Do you expect not to publicize the revised net sales and operating profits by segment?

A. We haven't announced them yet.

Q. I've just now heard the figure in the initial shipment of "Devil May Cry 4". I get the impression that Capcom manages its marketing very successfully in North America and Europe. I assume that your company is also offering downloads of its demo this time. Compared to other companies, your operations in North America stand out. I would like to get your comments on whether there is any concrete difference in your operations in this regard. I presume that with this strong marketing clout in North America, your company will start to develop titles overseas in the future. So I would like to hear about this possibility on a mid-term basis.

- A. 1) We are aware of our strong marketing ability, but we can't sell many popular titles even with strong marketing clout. Therefore, the key to our success with "Devil May Cry 4" and the existing "Lost Planet" and "Dead Rising" is, first of all, that our development teams in Japan created exciting titles as games. On that basis, we also changed our marketing style from television advertising only into diversified forms, such as internet advertising, and offering demo versions.
- 2) This time, in North America, we took active steps to promote sales, filling retail stores with pop art for "Devil May Cry 4" in cooperation with Game Stop Corporation. Consequently, we now do things we couldn't have done before, and our current status has improved considerably. Yet, there are more marketing steps which we are going to implement later.
- 3) Regarding the second question about titles being developed at our overseas affiliate company, we first released "Moto GP '07" and sold slightly less than 300 thousand units in Europe and North America. Its sales and profit are almost as we planned. As we will release new titles in the fourth quarter and later, we will be better able to forecast their success and failure. Nevertheless, we haven't increased large scale investment much in title development overseas. If we develop titles properly overseas and are able to collect profits as we plan, we will slightly increase the amount of our investment. Thus, the major products contributing to our performance are titles developed in Japan. Our basic concept is that we are going to push sales of titles in Europe and North America that were developed mainly in our Osaka office.

In closing, I would like to speak briefly. As I have mentioned repeatedly since last year, our president changed last July, with former President Kenzou Tsujimoto becoming Chairman, and former Vice President Haruhiro Tsujimoto becoming President and Chief Operating Officer. We considered the importance of strictly separating management and the executive. Now, we feel that within half a year, our preliminary step toward this will have been established. Currently, President Tsujimoto and other executive committee members are reviewing what kind of measures each business segment can implement. Although we haven't gotten the final period result yet, we have all made a commitment to fulfilling the revised forecast properly by working harder toward the end of this fiscal period. Concerning the next period and later, Chairman Tsujimoto and our management have asked for a 10% increase in net sales and 15% increase in operating income, and we are working toward a mid-term target. Hence, in order to definitely achieve this, we are now examining how much we can expand. Consequently, although we are still in the process of improvement, we are going to manage the situation to the best of our abilities. That's all I would like to say. Thank you for your attention.