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UBI.PA - Q1 2014/2015 Ubisoft Entertainment SA Corporate Sales Call

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PRESENTATION

Operator

Ladies and gentlemen, welcome to the Ubisoft first-quarter fiscal-year 2015. I will now hand over to Mr. Yves Guillemot, CEO. Sir, please go ahead.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Good afternoon and good morning, everybody. Thank you for joining our conference call.

With more than already 8 million units sold, Watch Dogs' historical launch epitomizes Ubisoft's capabilities. We know how to create brands -- blockbuster brands -- an extremely complex thing to achieve; we know how to regularly launch massive open world, a genre that it is taking an ever-increasing share of the market; and we constantly look for new innovation to enrich players' experience, notably with the integration of digital breakthrough in our titles, like the seamless multiplayer modes or cross-platform gaming using tablets.

Watch Dogs' successful launch is an important milestone for the Company. The first year of new consoles are key to establishing new long-term franchises and to winning market share. With Watch Dogs, we are adding another pillar alongside the likes of Assassin's Creed and Far Cry to our recurring flow of highly profitable products.

Thanks to its success, our first-quarter sales were up 374% to a record EUR360 million, above our target of EUR310 million. PS4 and Xbox One already represented more than 50% of our total revenues, and over two-thirds with the PC included.

In such a strong quarter, emerging markets totaled 12% of our revenues, which highlights their growing impact.

Digital revenues were up 149% at EUR84 million. This strong growth reflects the positive impact of Watch Dogs digital distribution, which stood at 14% of total sellthrough sales.

Season passes for DLC content were also strong, and it is worth noting that over 70% of them were sold through physical retailers, which highlights their marketing efficiency. We also had a stronger lineup of standalone digital titles this quarter with Trials Fusion, Child of Light, and Valiant Hearts.

Finally, we were very pleased by our mobile revenues, up 6-fold year on year. That performance was driven by the successful releases of Trials Frontier and CSI: Hidden Crimes, as well as by the positive impact of the recent updates of Hungry Shark. While this level of course should not be extrapolated to the rest of the year, we believe the step-by-step approach we are implementing to our mobile offering is bearing fruit.

Back catalog was down to EUR55 million, as well as we had benefited last year from strong sales of Far Cry 3. Assassin's Creed Black Flag, actually, back catalog was slightly better than the one of Assassin's Creed III in Q1 last year.

For Q2, we expect sales of approximately EUR85 million, down versus last year. For comparison, in the second quarter of last fiscal year, we had released Splinter Cell BlackList, Rayman Legends, as well as Just Dance 2014. This year, Just Dance 2015 will be released in the fiscal third quarter.

Now I would like to share with you our take on this year's E3. While 2013 was the year of the new hardware, 2014 was all about the next-gen games.

Ubi and the industry overall had a very strong show, with impressive levels of quality displays that showcased the wonders of next-gen gaming. This bodes very well for the momentum of the PS4 and Xbox One, and for the overall market.

Ubisoft came to E3 with a high-quality, comprehensive, and impactful lineup. The show gave credence to our goal of putting three titles to the top 10 bestsellers this year and hinted at the strong lineup for fiscal-year 2016.

We monitor both very closely via social media. Two years ago, those metrics were key in telling us that Watch Dogs had the potential to be a major success. This year's metrics are equally impressive.

For example, Assassin's Creed Unity videos had 16 million YouTube views by Thursday, June 12. They were the most viewed of E3 by far. The second title was from one of our competitors and had 7 million views, as an example.

Now, more good news. Far Cry 4 trailer was ranked number four in number of views [and I think] the game's very strong reception during the Sony's conference. They were confirmed by the recent GameSpot Trax data that found Ubisoft Best Publisher of the Show and Assassin's Creed and Far Cry 4 Best Games of E3.

Let's now review our games. As I just said, Assassin's Creed Unity is a great show. The French Revolution setting resonates with players, and many commented that this was the first true demonstration of new-gen wonders: beautiful graphics combine with a feeling of density and real life that are amplified by the possibility of adding thousands of nonplaying characters on the screen versus a few hundred in the past. The game will immerse players in the Assassin's Creed experience like never before.

We constantly innovate with the franchise, and this year we announced that players will be able to play some missions in co-op. This new addition was one of the main highlights of the Microsoft conference.

Following this strong showing, Assassin's Creed Unity is ranked as the most anticipated title in the GamePro 50. This is another great indicator. For reference, GameSpot's 50 is the leaderboard of the most anticipated upcoming games released, based on their data from more than 20 million gamers worldwide.

Now let's talk about Far Cry 4, which got the crowd roaring when we demoed the game at the Sony's conference. Leveraging the winning formula of Far Cry 3, Far Cry 4 brings the anecdote factory to an entirely new world where gamers can build their own unique stories and share them with their friends. The level of buzz and excitement for Far Cry 4 are very high, as confirmed by YouTube views.

It is also ranked second in GameSpot's 50 most anticipated titles, which again is very promising. Far Cry 4 also delivered the most innovative engagement activation mode, with the reveal of the Keys to Kyrat. This exclusive offer will allow PS and Plus members to invite their friends to come and play the open world of Far Cry 4 with them for a limited period, even if they don't own the game.

It is just one of the many exciting digital breakthroughs made possible with the new generation of consoles. Everyone walk away from our booth's demo noting the polished and varied gameplay and the incredible amount of fun the game has to offer.

After a strong debut at the last year's show, The Crew continues to be a pleasant surprise, especially for those who got their hands on the demo. Many noted they were impressed by The Crew unique take on MMO action driving.

As GamesRadar said: "The Crew is a racing game that has as much in common with World of Warcraft as it does with Need for Speed." The Crew won the Game Critics Award for Best E3 Racing Game. This is a great recognition of the game's quality and of the innovation it brings to the genre.

We will launch a closed beta for PC players in a few weeks. It will allow more players to discover first-hand The Crew's variety of driving adventures in a massive play [drama] populated with players from all over the world.

At the Microsoft press conference, The Division made its return to E3. Many commented on the amazing graphics made possible by the Snowdrop engine and the attention to details.

IGN called it a pretty outstanding demo, while CNET said: "The interface looks amazing, as does the open-world environment. It seems like this is one title determined to push the next-gen consoles to their limit." The Division will be released in 2015 and has already a strong community of followers with both consoles and PC enthusiasts.

Lastly, following the lead of Watch Dogs 2 years ago and The Division last year, we unveiled Rainbow Six Siege as the surprise of this year's conference. The Rainbows are back, and they were named Game of the Show by both PCGamers and IGN, two of the most influential publications for gamers.

It also earned the Best PC Game award in the Games Critics Award, an outstanding achievement. Reactions of diehard shooters fans have been very strong, and we believe we have established the basis for a strong comeback of the franchise. We will disclose more in the future, and notably about it solo and co-op, which we believe will also have a large appeal.

I would finally like to talk about Just Dance Now. As you know, the Just Dance franchise has proven its sustainability and its lasting strengths. Currently faced with a platform issue, we innovated to bring the true Just Dance experience to mobile, independent of consoles, and to leverage the huge catalog of songs in our library.

This expands the addressable audience for Just Dance to a potential of 2 billion smartphone owners. While it is too early to truly [guess] the game's full potential, we believe Just Dance Now, alongside Far Cry, Assassin's Creed, The Crew, The Division, Watch Dogs, and Rainbow Six, demonstrates Ubisoft's constant drive for innovation and our capacity to develop and sustain great entertainment franchises.

As a conclusion, I would like to make some additional comments. Watch Dogs clearly outperformed our expectation for the quarter, and we believe the game has the potential to outperform our anticipation for the full year.

We decided to confirm our full-year target as, first, it is too early to extrapolate for Q1 performance given the current market conditions, with very dynamic next-gen sales and very slow old-gen markets. Second, the achievement of our fiscal-year targets also depends on the successful launch of four major titles in an environment that will be competitive.

And third, we need to continue monitoring our progress in the free-to-play segment, and notably to confirm the growth we have seen recently on the mobile front. Still, we feel this strong start of fiscal-year 2015 as well as our very successful E3 provide us with more visibility and confidence regarding our full year's targets.

So, we are now ready to answer your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Edward Williams, BMO Capital Markets.

Edward Williams - *BMO Capital Markets - Analyst*

Good evening. A couple questions. Can you let us know how many of the 8 million units sold were full-game downloads, and how it bears on console full-game downloads or else PC full-game downloads?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Overall, it's 14% on -- once you get -- if we consider the download versus the sellthrough.

Edward Williams - *BMO Capital Markets - Analyst*

Okay. How many of the 8 million were sold through?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

I'm sorry?

Edward Williams - *BMO Capital Markets - Analyst*

How many of the 8 million were sold through?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

I think that if you look at it, the PC represented something like 10%, 12% of the total sales of Watch Dog. And I would say on the PC we are probably north of 70% download.

Edward Williams - *BMO Capital Markets - Analyst*

Okay.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Overall on console, I would say that on new-gen we are generally with -- around 10%. You are higher on the Xbox One and a bit lower on the PS4.

But overall if you take the two, the level of download is about 10% from what I have seen. On PS3 and Xbox 360, it is about 3% to 5%.

Edward Williams - *BMO Capital Markets - Analyst*

Okay, great. Thank you. Then can you comment a little bit about the differences between North America and Europe with regards to the game? Any material differences in those markets?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Yes, we can say there are more downloads in the US than in Europe. The digital sales on PC and console are higher in the US.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Yes, and on the other side, since in Europe, as we know, PC is stronger, that means that it's kind of balancing it. And as you probably have seen on this quarter, Europe did better than USA, North America. It seems that Watch Dogs has got more sales (technical difficulty).

Edward Williams - *BMO Capital Markets - Analyst*

Okay. Then the last question from me is: Can you update us on what is happening with regards to Montreal or in Quebec, with their commentary about the tax breaks?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Yes. What we can say is that when we decided to increase our investment in Quebec last year, we announced officially that we would do so, and we did it on the basis of a new binding agreement that gave us the guarantee of keeping the 37.5% tax credit until March 2019. That is all we can say today.

Edward Williams - *BMO Capital Markets - Analyst*

Okay, great. Thank you.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

I made a mistake. I said that Europe was a bit better. It was a bit better than last year, but it's actually 44% and 44% for both regions.

Edward Williams - *BMO Capital Markets - Analyst*

Okay, great. Thank you; and congratulations on that launch.

Operator

Mike Hickey, Benchmark Company.

Mike Hickey - *The Benchmark Company - Analyst*

Hey, guys. Great quarter, and congrats on Watch Dogs, and a good E3 show.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Thank you.

Mike Hickey - *The Benchmark Company - Analyst*

Just curious if you could give us any perspective on Watch Dogs, as it relates to supply in the channel in front of the holiday here.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

What we see is that the level of sell-in, sellthrough, is pretty healthy. We believe that we are in good shape.

And considering that Watch Dogs has just been launched in the first quarter, we do believe that we will see more reorder to come in the coming months. And therefore, we are pretty positive on that title for the whole year.

Mike Hickey - *The Benchmark Company - Analyst*

Okay. Obviously, this looks to be a strong franchise for you guys moving forward. Is this something that you feel you can iterate every couple years? Or how do you think about [pay from] that, I guess?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

We don't want yet to comment on that. We are very happy with the success. It's just one month old now, so we won't give more information on what our plans are. Not yet.

Mike Hickey - *The Benchmark Company - Analyst*

Yes. No, fair enough. I understand.

Then just -- obviously this is a ways out, but you had given some operating income guidance for fiscal 2016, a couple hundred million. Is that something you still think you can get to?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

No change.

Mike Hickey - *The Benchmark Company - Analyst*

For fiscal 2016 or --?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Yes. No change on those EUR200 million.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

That's right.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

So we still feel that we should be able to do that, yes.

Mike Hickey - *The Benchmark Company - Analyst*

Okay, good. Last question for me, just your confidence. Obviously, you have some big games coming out, just your confidence at this point that those games should be able to ship on time for the holiday period.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Yes, that's right. We have a good lineup and everything is in line to be launched.

Mike Hickey - *The Benchmark Company - Analyst*

Okay. Great, guys. Thank you very much.

Operator

Thomas Alzuyeta, Kepler.

Thomas Alzuyeta - *Kepler Cheuvreux - Analyst*

Good morning. Congrats for the figures. Just a quick question. I think I made the figure that you talk about 8 million sellthrough for Watch Dogs. Do you have the figures then for -- sell-in; 8 million is for sell-in. Do you have the figure for sellthrough, please?

Maybe my other question will be on digital sales. You mentioned a great performance there. Can we have a bit more color on the breakdown between Watch Dogs sales, Valiant Hearts, and Child of Light on free-to-play? Thank you.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Okay. On Watch Dogs, we gave the sell-in figure of 8 million, not the sellthrough, as you mentioned. And we gave only the sellthrough for the first week; we usually don't get the sellthrough all the time, so we will keep it this way.

In terms of -- I don't know when you speak about digital, in the case of Valiant Hearts and Child of Light, it's clear that those titles were both sold digitally and in the shops; but those titles were mostly digital.

Maybe Valiant Hearts was about 50-50 digital and physical; yes. And for the rest, it was more 75%, 85%.

Thomas Alzuyeta - *Kepler Cheuvreux - Analyst*

My question is, among the EUR84 million for the quarter, which part is related to these two games which were not there last year? And which part is related to Watch Dogs? And what is the [denimsen] for the free-to-play games?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Watch Dogs is much bigger than the other two games, much bigger. So within the EUR85 million, if we say that Watch Dogs is 14% of sellthrough, that means it's a quite significant amount. And you can estimate that it is quite big in those EUR85 million.

Thomas Alzuyeta - *Kepler Cheuvreux - Analyst*

Thank you.

Operator

Jean-Christophe Liaubet, Exane.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Yes, good evening. Just a question on Watch Dogs. Can you tell us what are your forecast implied for your Q2 guidance on Watch Dogs sales? And could you also give us in Q1 the sales mix between old-gen and the new-gen and the titles, please?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

As we said for the mix between the two, we have done more than two-thirds of our sales on [2P] and next-gen, and one-third on old-gen.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

I think your question was related to Watch Dog, and I would say that we are more than that if we look on Watch Dog.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Okay. In your Q2 guidance, what are your assumptions on reorder sales in terms of units sold?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

We haven't given that. We have some expectation, of course, but we prefer to keep our formula for ourselves.

What we confirm is that -- we already did it. Our goal was to have Watch Dog exceed Assassins Creed, which is already done. And we believe that there will be over the year some significant reorder; but we cannot comment on each quarter.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Okay. Could you give us also on the EUR84 million digital sales the mix between the new release and catalog, please?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

We don't know that right away. Jean-Benoit is to see. I would say there will be a great amount of new release on the digital coming from Watch Dog, coming from Valiant Hearts, from Child of Light, and Trials. So I would probably think it's -- but at the same time, there is the PC thing.

I would say it's, I'm sure, at least two-thirds of our revenue coming from new releases, minimum.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Okay. Last question regarding catalog sales. If I am right, I have not seen any figures where really you give some element what was (multiple speakers)?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Yes. I think it's about EUR55 million by catalog sales -- I think Yves mentioned it -- which is lower than last year. I think we were at EUR65 million last year -- EUR60 million.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Okay, super. Thank you.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

And we mentioned that we were expecting to be lower over the year because of the transition.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Also, we are also comparing --

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Smaller sales.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Smaller sales. Because last year we did EUR1 billion and the previous year we had EUR1.26 billion.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Okay. For the full year, the decline that you expect, what should be the magnitude? Do you have an idea?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

No, we have given an idea of a decline, but we wouldn't do it for 2% or 3%.

Jean-Christophe Liaubet - *Exane BNP Paribas - Analyst*

Yes, okay. Thank you.

Operator

Louis Bazy, Invest Securities.

Louis Bazy - *Invest Securities - Analyst*

Yes, hello. First of all, congratulations for the release of the Watch Dogs. I have a couple of questions, so I will start with Assassin's Creed.

Just to make sure I've understood well, you only have Assassin's Creed for your next-gen, nothing for current-gen at the moment?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

At the moment, that is what we have, yes. We said that we were going to give more intro soon on that, and it will come soon.

Louis Bazy - *Invest Securities - Analyst*

Okay. Then on Watch Dogs, a couple of questions. First of all, you said that 14% of sellthrough was through digital. And so that will increase the margin on Watch Dogs compared to other games?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Yes, it really helps to increase margins. It does more on console than it does on PC in US, for example. But on the whole it's very positive.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Yes. If you compare, I think on Assassin's Creed Black Flag we were at an average of 7%. So it's about double.

So it has of course a positive impact, which we had mentioned in the fact that we are were expecting for the year to increase our gross margin by 3 to 4 point.

Louis Bazy - *Invest Securities - Analyst*

Okay. Again on Watch Dogs, I have been looking at the transcript on the previous conference call, where you said that you were expecting more than 6.3 million. With 8 million sell-in, could you maybe give us a bit more indications on what you are expecting?

Because obviously, the 6.3 million is already beaten. So where will you see the final sales for the full [exercise]?

Alain Martinez - *Ubisoft Entertainment SA - CFO*

What we said is that we now expect, versus what we were anticipating -- when we said over 6.3 million, again it's because we feel it's -- we wanted to give an indication about the size and really the anticipation we had on that game. We do feel that right now, the game is ready to overperform even on what we were expecting.

So we are comfortable with that. But we have not given an indication whether it's 9 million, 10 million, or 11 million.

Louis Bazy - *Invest Securities - Analyst*

Okay. Final question. So you have pushed back Just Dance compared to last year's [front], so the Q2 to the Q3. Isn't that taking a risk with already a period loaded with a lot of releases?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

No, not really, because we are just pushing it by 1 or 2 weeks. So it's going to come very early.

Louis Bazy - *Invest Securities - Analyst*

Okay, perfect. Thank you very much.

Operator

John Taylor, Arcadia Investment.

John Taylor - *Arcadia Investment - Analyst*

Hi, congrats on a great quarter and a great E3 from me, too.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Thank you.

John Taylor - *Arcadia Investment - Analyst*

So, what are you expecting now as it relates to pricing for PS3 and 360 titles? It seems like there's occasional $39 and $49 prices out there.

So do you think you will be able to hold your $59 for whatever you do have in the pipeline for the holiday period? Or are we most likely going to see some price erosion there?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

No, we think we will keep the same level for the big products. There will be still in our model, there will be --

Alain Martinez - *Ubisoft Entertainment SA - CFO*

Promotions.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

-- promotions at some point. But we know that -- we think we can go with the $60.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

What we see on Watch Dogs is the level of average pricing that we have achieved up to now is pretty healthy. So we are very comfortable at least on Watch Dogs on the average price, what we have been able to obtain.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

And the two other games are coming for Christmas, so it's also a period where we can sell at that price.

John Taylor - *Arcadia Investment - Analyst*

Right, okay. Okay. Then with the introduction of the no-connect Xbox One, have you seen any change in the sellthrough ratios between PS4 and the Xbox? Or do you have any feedback from the channel on what that price cut has done to the Xbox One velocity versus what it was prior to that?

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

What we heard is that it improved a lot the sales of Xbox One. Now, we don't have exact details. We had GameStop saying that they were very happy with the sales, and we saw that in other regions.

So it seems to work very well to move the price. Now the season is a slow season, so it's really at the end of the year that it can make a huge difference.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

As you have been able to see, we have had a strong bias toward PS4 because Assassin's Creed -- because of -- sorry --

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Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

We had a deal on Watch Dog.

Alain Martinez - *Ubisoft Entertainment SA - CFO*

On Watch Dog we had a deal; and therefore Watch Dog was particularly strong on the PS4, which doesn't mean that it reflects the overall market.

John Taylor - *Arcadia Investment - Analyst*

Okay, okay. Thank you.

Operator

Thank you. We have no other questions for the moment. (Operator Instructions) We have no other questions for the moment.

Yves Guillemot - *Ubisoft Entertainment SA - Chairman, CEO*

Okay. So thanks very much for listening today, and have a great day. Thanks very much.

Operator

Thank you. Ladies and gentlemen, this concludes the conference call. Thank you all for your participation. You may now disconnect.
