

## **FY2019 Q3 Earnings Announcement**

### **Analyst and Investor Briefing Q&A (Summary)**

Date: February 4, 2020 (Tue)

#### **IMPORTANT: PLEASE READ THE FOLLOWING STATEMENT**

For your reference, below please find an English summary of the question and answer session at the analyst and investor briefing for the financial results for the third quarter ended December 31, 2019, which was conducted in Japanese (except for questions asked in English, if any).

The English summary below is not intended to be a direct translation of the question and answer session and as a result, there may be some differences between the English summary below and the simultaneous English interpretation provided at the question and answer session. A recording of the simultaneous English interpretation can be found on the Sony Investor Relations website at <https://www.sony.net/SonyInfo/IR/>.

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#### Questioner 1

Q1: [I&SS segment] Regarding the upward revision to guidance for the I&SS segment, which was the greater driver, volume upside or product mix improvement?

A1: As in the 2<sup>nd</sup> Quarter, we believe contributions from volume and product mix improvement were roughly the same.

Q2: [I&SS segment] You revised down the outlook for fixed asset growth somewhat. Is this due to improved investment efficiency or some other factor?

A2: The change reflects our view that improvements in efficiency will allow us to reach our desired levels of capacity without the degree of investment we had initially anticipated.

#### Questioner 2

Q1: [I&SS segment] You mentioned your lack of optimism about the competitive environment for the I&SS segment in FY2020, but it seems that supply/demand conditions in the industry are still good, so how much of a risk do you actually see?

A1: It is difficult to answer in numerical terms, but based on our initial outlook, we made plans to build up strategic inventory in the 4<sup>th</sup> Quarter in anticipation of very strong demand in 1H FY2020 given how much production capacity we have by comparison. However, we will have to ship, during this fiscal year, almost all of the strategic inventory we planned to build for FY2020, raising the issue of whether we can sufficiently meet demand in FY2020. In addition, 0.8-micron image sensors, which have contributed significantly to FY2019 earnings, will be entering their second year of mass

production, so we expect our competitors will catch up to some degree and put pressure on prices. These are the main risks, but it goes without saying that because we have yet to factor in any potential impact from the coronavirus outbreak, we will need to reflect that, too, pending further research, etc.

Q2: [G&NS segment] In the game business, what was the degree of contraction in free-to-play games in the 3<sup>rd</sup> Quarter in comparison with the 1<sup>st</sup> Quarter and the 2<sup>nd</sup> Quarter, and, looking ahead to FY2020, should we expect the weakness in free-to-play games to have run its course by the end of FY2019?

A2: Most of the sharp decline in third-party software is in free-to-play titles. Other software titles in our library of new and existing games are roughly flat YoY, so this highlights the difficulty in predicting trends in free-to-play titles. In other areas, there were not many variances, so we would like to improve the accuracy of our forecasting here.

Questioner 3

Q1: [G&NS segment] Regarding the game business, until now I was under the impression from previous presentations that PlayStation Plus subscriptions tend to grow when triggered by the launch of a major title or other catalyst, suggesting this would be a difficult quarter. However, subscriptions went up despite the fact that software sales were not very strong. What is your take on that, and what are your expectations for subscriber numbers looking ahead to the next-generation console?

A1: It is a process of trial and error when it comes to securing stable growth in PlayStation Plus subscribers and retaining them more efficiently. As you know, as a part of the price revisions we implemented in August, we made an annual subscription more affordable with the intention of increasing the number of long-term stable users. Also, we included several incentives with the annual subscription such as online multiplayer gaming, free access to some PS4 titles, 100GB of storage for PS4 game saves, and exclusive subscriber discounts. We believe this made more users appreciate the value of the subscription. The number of subscribers tends to increase in the 3<sup>rd</sup> Quarter every fiscal year, but we would like to achieve more stable growth by inviting users to experience and appreciate these services. Looking ahead to the next-generation console, we aim to increase subscriber numbers as much as possible. There is very little I can disclose about the new console as of yet, but I look forward to sharing more at some point in FY2020 when we are prepared with more details.

Q2: [G&NS segment] The FY2020 earnings outlook for the game business is a frequent topic of discussion in the market given that the PS5 is to be launched for the 2020 holiday season. What are your thoughts, if any, on what would happen if we were to reach the end of April, when the earnings outlook is usually disclosed, and the price of the PS5 had still not been revealed?

A2: It is still difficult to discuss that at this time, but what I can say is that at present we plan to deliver our earnings outlook at the same time as usual.

#### Questioner 4

Q1: [EP&S segment] The implied 4<sup>th</sup> Quarter operating income outlook for the EP&S segment is for a substantial loss judging by your full-year operating income outlook. Broken down into the four main product categories, what are your assumptions regarding sales trends/levels, and what nature and size of non-recurring costs are you expecting? Also, how much of a profit improvement can the EP&S segment deliver in FY2020, including from the disappearance of non-recurring costs?

A1: Numerically, guidance does imply a 4<sup>th</sup> Quarter operating loss in the EP&S segment, but as I touched upon in my speech just now, we are expecting to post one-time restructuring costs in the Mobile Communications business, the impact of which is likely to be very significant. However, we are looking closely from various perspectives into how much this can be minimized, and we aim to keep costs as low as possible. We are not expecting anything outside the bounds of ordinary seasonality at present in the other product categories. 3<sup>rd</sup> Quarter inventory, as I just mentioned, was also kept very much within appropriate levels. At our previous results briefing, we talked about plans to launch some new products in our TV range in the 4<sup>th</sup> Quarter and, as of now, those plans remain unchanged. However, if concerns regarding the Chinese supply chain were to come to fruition, there is a risk of delays in ramping up some of the products.

Q2: [EP&S segment] Can we assume that these one-off factors will disappear in FY2020 and profit will increase?

A2: We have yet to put together our targets for FY2020, but our intention is to make a positive start to FY2020 without any negative hangover from past years, and to that end, we will continue to keep firm control on inventory and make solid manufacturing and marketing plans.

Q3: [EP&S segment] If approximately 13 billion yen, the remainder of your restructuring budget to be recognized in the 4<sup>th</sup> Quarter, is incurred in Mobile Communications, you still would have a loss of 35.8 billion yen for the wider EP&S segment. Is that correct?

A3: You can assume something along the lines of your analysis, but please understand that we are not disclosing a detailed breakdown.

Q4: [G&NS segment] In the game business, I understand that third-party software sales were not good, but what about first-party titles?

A4: I am unable to give you a quantitative answer as to how our results differed from our expectations, but I will give you a general impression. We were not able to meet our assumptions for catalog titles in the case of third-party full-length games or for first-party full-length games in general as those expectations were somewhat ambitious. Results in the PlayStation Plus business and elsewhere were more or less as expected.

#### Questioner 5

Q1: [I&SS segment] Where did production capacity stand at the end of the quarter in the I&SS segment? Also, what were wafer inputs and what do you expect inputs will be going forward?

A1: Available monthly capacity was roughly 115,000 as of the end of the 3<sup>rd</sup> Quarter. We had previously assumed 117,000, so this was down slightly. This is due to slight deviations resulting from factors including process mix and is not because we are behind on building out capacity. We expect capacity to be at 124,000 at the end of the 4<sup>th</sup> Quarter. As for inputs, we were at full capacity in the 3<sup>rd</sup> Quarter and expect to be at full capacity again in the 4<sup>th</sup> Quarter.

Q2: [Pictures segment] You mentioned having built up your franchises in the Motion Picture business. Could you share your thinking on the investments you undertook in the 3<sup>rd</sup> Quarter? Your deal with the production company for *Peter Rabbit* seems to be in line with your current approach, but your investment in the Game Show Network is of a somewhat different nature. Given that you are undertaking a review of unprofitable channels, could you comment on the intent behind that investment?

A2: We acquired the 42% stake AT&T had held in the Game Show Network and made it a wholly owned subsidiary. We had previously held a 58% stake. The Game Show Network is a multimedia entertainment company that distributes game shows, including original programming, via cable television in the U.S. A company under its umbrella called GSN Games also offers online and mobile games. Our thinking was that this business unit had potential from a variety of perspectives, so when presented with the opportunity, we increased our stake to 100% in order to be able to make strategic decisions with greater flexibility.

Silvergate Media is a company that develops and produces animation for children and also engages in licensing. It produces seven titles for SVOD and cable television. The objective of our investment was to acquire high-quality original IP and creative talent. We have seen this as an extremely attractive category for some time, and when this acquisition opportunity presented itself amidst various dialogues we were having, we acted and made our decision quickly.

Questioner 6

Q1: [I&SS segment] You mentioned a better mix and higher volumes in the I&SS segment in the 3<sup>rd</sup> Quarter. Could you tell us about the per-wafer sales momentum? It seems to have increased considerably in the 2<sup>nd</sup> Quarter. Is it fair to say it increased by a similar amount in the 3<sup>rd</sup> Quarter? Inventory fluctuations meanwhile seem to be a negative for profits this year. Could you share any quantitative data you have on that?

A1: Per-wafer sales momentum ends up being a discussion of the unit price per wafer, which is not something we disclose, so I will refrain from any quantitative commentary. Making larger sensors reduces the theoretical yield per wafer, which diminishes production yields. Therefore, the average price per sensor needs to be enough to offset that or it will not be possible to maintain the unit price

per wafer. As such, in order to correctly maintain the momentum of per-wafer sales or pricing, we need to be certain we are supplying a high added-value product and improve our production yields, or ensure that new products get off the ground as smoothly as possible. These things enable differentiation and we therefore want to continue to focus our efforts on them.

On the question of how inventory fluctuations impact profits, we saw a 7.8 billion yen decline in inventory between the 2<sup>nd</sup> Quarter and the 3<sup>rd</sup> Quarter, which was a negative for profits. I believe that the decline reduced profits by 10 billion yen or more on a YoY basis.

Q2: [G&NS segment] In striving for a “smooth transition” in the G&NS segment in FY2020, could you describe to the extent possible where you have visibility and where you lack visibility in terms of, for example, development or marketing costs you might be able to control, or things that remain uncertain regarding pricing or volumes perhaps?

A2: Firstly, we believe that we absolutely have to control our bill of materials cost. This ends up being a question of what we recognize as costs and is a point over which we must exercise control. Then there is our initial ramp-up. Our manufacturing and marketing efforts need to be solid so that we can determine how many units we need, and then produce the appropriate volume.

Given that we compete on price, it is extremely difficult to comment at present on where we lack visibility. In addition, pricing also determines the nature of our promotion efforts and how much we spend because of the balance that needs to be struck, so it is difficult to comment on all of that at this point in time.

In terms of making the transition as smooth as possible, we are engaged in ongoing discussions based on our belief that we should devise the best-balanced approach that enables us to ensure that the next-generation console is profitable over the course of its life.

Questioner 7

Q1: [I&SS segment] What sort of contribution should we expect from products other than image sensors in the I&SS segment in FY2020 and beyond?

A1: That would be sensing inclusive of industrial equipment, factory automation, automotive, and ToF applications. We have said for some time that we want to bring the proportion of products other than image sensors for mobile applications to around 30% by 2025. We have not made any particular changes to that objective and are doing what we need to toward that end. In the short term, our ToF sensors for mobile applications are getting off to a smooth start, so I believe that we will be able to tell you in FY2020 or thereafter what percentage of the business they will likely come to represent. We do not need to invest any capex specifically for ToF sensors, so we see them as having substantial potential. We also believe that we can derive an appropriate level of profit margin from them.

Q2: You said that you will be able to increase input without investing as much as you had anticipated. Is there any change in the 700 billion yen figure under your mid-range plan, including in terms of how much outsourcing you intend to use?

A2: We have been able to achieve a 15-billion-yen reduction in FY2019 thanks to greater investment efficiency. However, at present we do not expect any major change in our plan to spend 700 billion yen over the timeframe covered by the mid-range plan. The fiscal year ending March 31, 2022 will be the year that we release our next mid-range plan covering 2021-2023, so I believe we will be able to share our thinking on investment over that three-year span at that time.

Questioner 8

Q1: [I&SS segment] How is inventory in the I&SS segment likely to change in the 4<sup>th</sup> Quarter? That likely depends on demand, but could you comment on the general direction? It seems business was extremely brisk in the 3<sup>rd</sup> Quarter, but with a slight downshift in customer demand underway, do you think that, excluding the impact from the coronavirus outbreak, there will be so much demand in January-March and April-June that you will not be able to produce enough even at full capacity?

A1: Our original intention for the 4<sup>th</sup> Quarter was to build up strategic inventory for 1H FY2020. Thereafter, customer demand became so strong that it proved difficult to engage in strategic stockpiling, and we had no choice but to keep shipping what we had. I am not certain how meaningful it would be to try to describe our expectations exclusive of the impact from the coronavirus, but we believe that we may see some instances of slower demand. Taking all of this into account, we believe that 4<sup>th</sup> Quarter inventory may not change much, increasing only slightly versus the 3<sup>rd</sup> Quarter. That said, we have not collected enough information to say anything definitive.

Q2: [I&SS segment] What is your output plan for January-March?

A2: We do not disclose output plans, but our production lead time is 5-6 months, so please deduce what you can from that.

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**Cautionary Statement:**

Please be aware that, in the summary above, statements made with respect to Sony's current plans, estimates, strategies and beliefs and other statements that are not historical facts are forward-looking statements about the future performance of Sony. Forward-looking statements include, but are not limited to, those statements using words such as "believe," "expect," "plans," "strategy," "prospects," "forecast," "estimate," "project," "anticipate," "aim," "intend," "seek," "may," "might," "could" or "should," and words of similar meaning in connection with a discussion of future operations, financial performance, events or conditions. These statements are based on management's assumptions, judgments and beliefs in light of the information currently available to it. Sony cautions investors that a number of important risks and uncertainties could cause actual results to differ materially

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