GMO INTERNET

Fiscal Year 2013 Results Presentation: Summary of Q&A Session

Questions were asked by institutional investors and analysts in attendance at the GMO Internet, Fiscal Year 2013, Quarter Results Presentation on February 6, 2014. Responses were given by Group CEO and Founder, Masatoshi Kumagai, Group CFO, Masashi Yasuda, and GMO AD Partners CEO, Shintaro Takahashi as indicated.

Q1. You said that .tokyo is a stock revenue business, what are the costs associated with .tokyo?

A1. (Masatoshi Kumagai, CEO & Founder) In the registry business the costs are; systems investment, server costs, human resources, and fees paid to ICANN. We are already operating a registry in Indonesia so much of the investment in systems is already complete and you won't see much new investment on our P/L statement. ICANN fees only amount to a few million yen a year so this also has minimal impact on P/L. As you say, .tokyo is a stock revenue business and we believe it has high earnings potential.
In regard to impact on P/L, there will be promotion costs for .nagoya, and .tokyo, and these will be incurred by our domain registrar business. Our marketing strategy is always to invest in new domains at the launch phase to expand market share. This is because users will hold onto a good domain indefinitely, and having a large domain user base provides us natural cross-selling opportunities in the mid to long term.

*ICANN: Internet Corporation for Assigned Names and Numbers

Q2. How much do you expect to spend on promotion in the registrar business.

A2. (Masatoshi Kumagai) For .nagoya we are planning a press conference and television commercial, and for .tokyo a television commercial and large-scale promotion. In total promotion cost is expected to be around JPY 200 million.

Q3. How much do you expect to spend on auctions for .shop, .mail etc.

A3. (Masatoshi Kumagai) Past auctions have usually been settled for a few hundred million yen. We have spoken to our auditors about this and auction fees will be carried as an asset on our balance sheet and amortized over 20 years.

.shop is expected to attract the highest global demand of any new generic Top Level Domain. If we can acquire .shop, our customer-base will comprise ecommerce businesses from around the world. .shop will create new opportunities for us to cross-sell payment and security solutions. We believe that this is the catalyst that will drive us to become a key player in the global ecommerce space over the next decade or two, and for this reason we are very committed to acquiring the domain.

Q4. You mentioned that SEO profit temporarily declined but that the top-line had recovered. How are SEO profits now?

A4. (Masatoshi Kumagai) Our response to the change in search algorithms is already complete, so this is not a concern any longer. With the reorganization of the GMO AD Partners group, we have a strong technology foundation that enables us to build great products on top of which we now have a very strong sales force. I think we can expect positive results from this segment in the current term.

(Masashi Yasuda, CFO, GMO Internet) In the fourth quarter, Internet media profit totaled JPY270 million. The impact of the SEO decline on segment profit was over JPY200 million, compared on a year-on-year basis. If this temporary factor is excluded, we would say that earnings potential for this past quarter would be around JPY500 million, which would be slightly up over the third quarter.

Q5. Can you talk about the basis for your current fiscal year guidance?

A5. This term we are keenly focused on making the game segment “the fourth pillar of the Group’s earnings structure’ and reaching a level of profit contribution in the billions (of yen).If we do strike a hit game, it will be a further upside. We do take a conservative view on the Internet Securities segment, but the business is currently performing well. In the Web Infrastructure segment there will be promotion costs impacting profit growth to some extent, but we also consider the Infrastructure forecast to be conservative. Finally, in regard to Internet Media, now that the segment reorganization is complete, we hope to see more growth here.

(Masashi Yasuda) In regard to the billion-yen profit contribution we are talking about, at the end of last year we reported an operating loss of JPY1.2 billion in the game segment, and next year we forecast JPY1.0 billion, which means we expect to see a total of JPY2.2 billion in profit contribution from this segment over the next 12 months. The guidance issued for 2014 shows operating profit increasing JPY1.5 billion from

JPY11.0 billion to JPY12.5 billion. There are two factors I would highlight here, one is that we have taken a conservative view on the Internet Securities segment, and the other is that we are planning significant investment (promotion, human resources) in the Infrastructure segment over the coming year. I would stress again that overall we have forecast conservatively.

Q6. Can you provide details on investment costs in the Web infrastructure segment?

A6. (Masatoshi Kumagai) In the first half of the year we expect to spend about JPY 200 million on promoting .nagoya and .tokyo, and depending on the outcome there may be additional spending in that area. In the second half of the year we may see auctions for the contested domains, .osaka, .shop, and .inc. If we do acquire these domains we will also be investing in aggressive promotion, and you could expect to see an additional JPY500 million to JPY1 billion in promotional spending.

In regard to human resources spending, we want to recruit tens of so-called “super-engineers”. I am afraid I can’t give you costs on a per-engineer basis, but we expect the total cost to be several hundred million yen.

Q7. You have invested heavily in user acquisition for the Smart Soccer game, can you give us an indication of the schedule for monetization?

A7. In the first half of the year we will be promoting 2 game apps. First, as you mentioned, Smart Soccer. We have seen a 400% increase in Daily Active Users (DAU) as a result of television advertising, however, certain KPI are still weak and we continue to work on fine tuning. We plan to gradually introduce in-game payment programs and cultivate games that our customers will use for a long time.

The second title, Encounter, has already attracted a lot of media attention. The KPI are also performing well and we are planning aggressive promotion to acquire users.

Q8. You have said that strategy for the Internet Media segment going forward will be focused on using ad technology to enhance products developed by your own companies. However, competition in the DSP, SSP, and DMP spaces is increasing, what is GMO-AP’s strategy in response?

A8. (Shintaro Takahashi, CEO, GMO AD Partners) Firstly, let me address Demand Side Platform (DSP). GMO AP is predominantly an ad agency company, and we use the DSP trading desks of other companies to provide efficient ad distribution to GMO-AP customers.

In regards to Supply Side Platform (SSP), GMO-AP is traditionally a media rep agency, and we already have our own SSP for media acquisition, and this is what we are focused on growing at the present.

Finally, I'll talk about Data Management Platform (DMP). There are three kinds of private DMP, 1) ecommerce, 2) media, 3) ad agency. GMO-AP is involved with the third kind. GMO Internet Group holds various data assets. Our first goal is to use that data to create a private DMP that will achieve more effective promotion for GMO Internet Group products. Going forward, we also plan to provide private DMP platforms to our customers.

In the DMP market there is some debate over whether data is owned by the customer or the DMP. Our view is that we believe, the customer would prefer to own the data and therefore we support the latter model.