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EA - Q4 2012 Electronic Arts Inc. Earnings Conference Call

EVENT DATE/TIME: MAY 07, 2012 / 09:00PM GMT

OVERVIEW:
EA reported 4Q12 GAAP net revenue of $1.368b and GAAP diluted EPS of $1.20. Expects FY13 GAAP revenue to be $4.075b and GAAP loss per share to be between $0.36 and $0.16.

CORPORATE PARTICIPANTS

Rob Sison *Electronic Arts Inc. - VP, Investor Relations*

John Riccitiello *Electronic Arts Inc. - CEO*

Ken Barker *Electronic Arts Inc. - Interim CFO*

Peter Moore *Electronic Arts Inc. - COO*

Frank Gibeau *Electronic Arts Inc. - President, EA Labels*

CONFERENCE CALL PARTICIPANTS

Edward Williams *BMO Capital Markets - Analyst*

Neil Doshi *Citigroup - Analyst*

Arvind Bhatia *Sterne, Agee & Leach, Inc. - Analyst*

Colin Sebastian *Robert W. Baird & Company, Inc. - Analyst*

Justin Post *BofA Merrill Lynch - Analyst*

Brian Karimzad *Goldman Sachs - Analyst*

Atul Bagga *Lazard Capital Markets - Analyst*

Doug Creutz *Cowen & Company - Analyst*

PRESENTATION

Operator

Welcome and thank you for standing by. At this time, all participants are in a listen-only mode. During the question-and-answer session (Operator Instructions). Today's conference is being recorded. If you have any objections, you may disconnect at this time. I will now turn the meeting over to Mr. Rob Sison, Vice President of Investor Relations. You may begin.

Rob Sison - ***Electronic Arts Inc. - VP, Investor Relations***

Thank you. Welcome to EA's fiscal 2012 fourth-quarter earnings call. With me on the call today is John Riccitiello, our CEO, Ken Barker, interim CFO, Peter Moore, COO, and Frank Gibeau, our President of Labels, who will be joining us for the Q&A portion of the call.

Please note that our SEC filings and our earnings release are available at IR.EA.com. In addition we have posted earnings slides to accompany our prepared remarks.

Lastly, after the call we will post our prepared remarks, an audio replay of this call and a transcript.

This presentation and our comments include forward-looking statements, regarding the future events and the future financial performance of the Company. Actual events and results may differ materially from our expectations. We refer you to our most recent Form 10-Q for a discussion of risks that could cause actual results to differ materially from those discussed today.

Electronic Arts makes these statements as of May 7, 2012, and disclaims any duty to update them.

Throughout this call, we will discuss both GAAP and non-GAAP financial measures. The comparable GAAP measures for certain non-GAAP measures to be discussed are for Q4, net revenue of $1.368 billion, digital revenue of $419 million, gross margin of 72.7%, operating expenses of $629 million, and resulting EPS of $1.20 per diluted share.

For full fiscal year 2012, net revenue of $4.143 billion, digital revenue of $1.159 billion, gross margin of 61.4%, operating expenses of $2.510 billion and resulting EPS of $0.23.

During this call, unless otherwise stated, the financial metrics will be presented on a non-GAAP basis. Our earnings release and the earnings slides provide a reconciliation of our GAAP to non-GAAP measures. These non-GAAP measures are not intended to be considered in isolation from, as a substitute for, or superior to our GAAP results. We encourage investors to consider all measures before making an investment decision. All comparisons made in the course of this call are against the same period in the prior year unless otherwise stated.

Now I will turn the call over to John Riccitiello. John?

John Riccitiello *- Electronic Arts Inc. - CEO*

Thanks, Rob, and good afternoon. I;d like to start with short review of our recent history before addressing our FY 2012 performance, our FY 2013 guidance and turning the call over to Ken Barker. For those on the call, I might suggest you take a look at the slides we posted on our website. They will help you track through this a little bit better, particularly the last few years' review I am about to do now.

As all of you know, these past few years have been very dynamic for companies competing in the fast-changing game industry. Four years ago, we set out to turn around our core console game business while transforming EA from a packaged goods company to a truly global digital pure play. Throughout this time, we never lost our ambition to position EA as a global leader in digital in the same way we led the packaged goods market during the PS2 era.

Four years ago, our strategies could be described as essentially defensive, mostly about our turnaround, in getting the start in digital. At the time we had three strategies. Fewer, better, and bigger console games, getting started in digital, managing cost.

The numbers show we have done these things very well. On our last earnings call, we introduced a significant change in our strategies -- a shift to offense. One that will complete our transformation into a digital pure play company, one that will move us from being a top 5 global competitor in digital gaming into becoming the global leader.

Today, our three strategies are brands, platform, and talent. By brand, we mean that we have the strongest brand portfolio in the game industry. We will project that portfolio across all relevant digital business models and channels, while continuing to invest to grow the power of our brands. Leading the way for EA are blockbusters like Battlefield, Need For Speed, FIFA, Plants vs. Zombies, Bejeweled, Star Wars, Madden, The Sims, Dragon Age, SimCity, Mass Effect, and Medal of Honor.

We strongly believe this brand collection is unmatched by any competitor in our industry.

By platform, we mean we are building the underlying technology that enables us to project our brand across all digital channels and business models, seamlessly, direct to consumer and do so in ways that vastly enhances the consumer experience. Technologies like our Nucleus system with nearly 0.25 billion registered users ensure we can recognize and serve content to our players no matter where they are on a social network or a console.

These investments enabled us to launch Origin, our direct-to-consumer service for downloading games and connecting players with other gamers and friends. Origin is now the number 2 direct-to-consumer game service with more than 11 million registered users. And we built EA Play For Free, our proprietary platform that is modeled on the Asian companies like Tencent and Nexon.

EA Play For Free now hosts a number of EA brands including Need For Speed and Battlefield and has become one of our fastest growing businesses. We will be adding more brands to this platform in the coming year.

Our third strategic initiative is talent. This is an unusual strategy for a game company. For most, talent is a consideration. For us, it is a core strategy.

Streaming into EA today is an incredible torrent of new talent. People who add to our capabilities and make us more like Google, Facebook, and, yes, Zynga. This talent is creating and maintaining our most sophisticated online services. In some cases, it is veteran EA talent that is learning new skills. In other cases, it is new talent coming from key tech companies and great universities.

Two great examples of the new talent are two leaders now on my executive team, Kristian Segerstrale, the founder of Playfish, is now EA's EVP-Digital. He is assembling a team of quantitative end analysts, technologists, and Internet marketers who will profoundly change the way we acquire, engage, and monetize consumer gameplay. Rajat Taneja, recently from Microsoft, is now EA's CTO.

Rajat's team is building a deep infrastructure for creating and playing our games on every device. You'll be hearing more about these projects from both Kristian and Rajat at EA's E3 Investor Breakfast.

We are also doubling down on our creative talent, the creative teams that build our games, people who add a special magic that differentiates great entertainment from just ordinary games -- great games that are emotionally engaging, the consumers identify with the heroes and have fierce debates over the endings, storylines that create controversy because the audience, our players, care -- talent that creates games and builds brands that will win the test of time. We don't see any competitor doing both the text and art in the way our people do.

So those are our three strategies. Brands, platform, talent -- all designed to help us accelerate our transformation to being the leading pure play digital gaming company. And over the last few years, we have shown great progress towards this goal.

Let me call out a few of these milestones. In fiscal 2009, we published 67 package goods products -- each, generally speaking, a stand-alone game. In fiscal 2012, we published 25 major branded online game services, each online multiplayer experience with ongoing monetization. We have increased our database of Nucleus registered users from 27 million to 220 million. We built a $1.2 billion digital business, establishing EA as one of the top 5 largest global digital game companies. In doing this we delivered a revenue CAGR of 47% from fiscal 2010 to fiscal 2012 and most of this growth was organic.

We developed the strongest brand portfolio in digital interactive entertainment and, most recently, added PopCap brands like Plants vs. Zombies and Bejeweled to our own incredible brands like Battlefield, Medal of Honor, Need For Speed, FIFA Soccer, The Sims and SimCity. Our Origin platform was generated $150 million in revenue in fiscal 2012 and is poised for strong ongoing growth leverages, both EA content and that of our partners. We transformed our financials from an EPS loss in fiscal 2009 to $0.85 EPS in fiscal 2012; from fiscal 2010 to fiscal 2012, a 39% EPS CAGR, and we're just getting started.

With that, I would like to turn to our fiscal 2012 review. Both fiscal 2012 and our most recent quarter were very strong for EA. In Q4, we delivered $0.17 EPS at the upper end of our guidance and ahead of the Street, despite key challenges like the failure of a major retailer just prior to the launch of one of our major titles, Mass Effect 3. For the full of fiscal 2012 we exceeded our topline guidance and came in at the upper end of our EPS guidance at $0.85, up over 20% on EPS versus a strong fiscal 2011.

There are a few milestones I'd like to point out that helped drive our fiscal 2012.

We exceeded our $1 billion goal for overall digital revenue delivering a planned meeting total of $1.2 billion in digital revenue. STAR WARS -- The Old Republic was the most successful subscription MMO launch in history and is now firmly established as the number 2 MMO in the West. This service is extremely strong on the operations level.

We did what we said we would do with Battlefield. Battlefield 3 took very significant share from the leading competitor on its way to being one of the biggest selling titles in EA history. There will be exciting new developments for the Battlefield brand as fiscal 2013 progresses.

EA SPORTS FIFA reached new heights as a brand and a game service. Today, FIFA is probably the most successful brand in our industry in terms of serving more users across more channels and business models than any other brand from EA or from any of our competition. And it is all tied together in one cohesive service. And we brought PopCap into EA and, with them, an incredibly talented group of creators with a great collection of strong brands including Plants vs. Zombies and Bejeweled.

Next I would like to turn to our FY 2013 guidance. The key considerations for our FY 2013 planned as it came together these past months are these. At the foundation is another year of blockbuster brands -- Madden, NFL, FIFA, SimCity, Medal of Honor, Dead Space and Need For Speed as well as mobile hits like The Simpsons, Tapped Out and Bejeweled. Versus my original expectations we are pushing out one major packaged goods title. This is a function of our R&D investment priorities.

STAR WARS - The Old Republic now has 1.3 million subscribers with a much higher mix of ongoing credit card consumers, but on a lower absolute number of subs. The service is stable, profitable and we have strong plans to grow at fiscal 2013. We intend to invest $80 million in Gen4 console development in fiscal 2013. We are strong believers that console will return to strong growth and represent a great opportunity, one that is in lockstep with our digital plan.

We are expecting another year of 40% growth in our digital business. Growth in these very high margin contributors allows us to afford our investment and in particular our investments in Gen4, while delivering very strong earnings growth. Our guidance, which Ken will take you through in a moment, calls for over 30% EPS growth in fiscal 2013, off our strong fiscal 2012.

We are projecting to have another great year. I will now turn the call over to Ken.

Ken Barker *- Electronic Arts Inc. - Interim CFO*

Thanks, John. Starting with a review of Q4, EA's overall performance was in line with the guidance we provided on our last earnings call. Total Q4 non-GAAP revenue grew $977 million. We came in slightly ahead of the top end of our guidance, due to the successful launches of Mass Effect 3, FIFA Street 4 and Kingdoms of Amalur (technical difficulty) and the continued momentum of FIFA 12 and Battlefield 3.

As you may recall, in early March we indicated that the financial trouble with the Game Group in the UK could cost us mid-single-digit EPS for Q4. While that came to (technical difficulty), we were able to offset some of this as revenue exceeded our March expectations in both packaged goods and digital as (technical difficulty) [considered] were determined to get their hands on our product, especially Mass Effect 3.

EA's Q4 non-GAAP digital revenue increased approximately 60% year-over-year to $425 million and for fiscal 2012 exceeded $1.2 billion. Digital growth came from all areas of the business as we continued to see success in each of our initiatives. For the quarter, extra content and free-to-play were up 37% last year, led by FIFA.

We passed an important milestone this year in which FIFA 12 became our first packaged goods title to generate more than $100 million in non-GAAP digital revenue. And Battlefield 3 is on track to break the same milestone. I would like to highlight that this is happening while packaged goods revenue for these titles is increasing, relative to prior iterations.

But Sims Social and PopCap also contributed to our digital growth. On a standalone basis PopCap saw double-digit growth this quarter as compared to the same period of products a year ago, and was accretive to our Q4 results. Full game downloads were up 76% year over year. Origin contributed $48 million in non-GAAP revenue fueled by Mass Effect 3, STAR WARS -- The Old Republic, and revenue generated from our third party publishing relationships.

Mobile and other handheld non-GAAP digital revenue was up 23% year over year. This quarter we saw continued growth in our smartphone and tablet revenue as well as in our Asian mobile business. This growth offset a decline in standard feature phones. 72% of the quarter's non-GAAP revenue in this category came from smartphones as non-GAAP revenue from smartphones grew more than 80% year over year.

The 143% growth in subscriptions, advertising, and other revenue was driven by the December launch of STAR WARS - The Old Republic. Let me provide you with an update on Star Wars. Through the end of the quarter approximately 2.4 million units have sold through. In our last call we indicated that we had 1.7 million active subscribers, and as of the end of April, we now have 1.3 million, with a substantial portion of the decrease due to casual and trial players cycling out of the subscriber base, driving up people who are all percentage of paying subscribers. We have already launched a number of initiatives designed to growth subscriptions. Initial responses have been positive and we are encouraged by the gaming community's reaction.

In summary, we delivered an extraordinary launch of a solidly profitable long-term franchise which contributed to both our gross and operating margin improvement in fiscal 2012. We expect this title will further expand our margins in fiscal 2013 as we get the full year benefit of subscription revenue.

Let me give you two additional points of perspective as it relates to our current subscriber base as an impact on our fiscal 2013 guidance. First, the current number of active subscribers, 1.3 million, is very consistent with the original assumptions we made when we acquired [BioWare] in 2008. Second, while this franchise is very profitable it only represents a mid-single-digit percent of our total profitability in fiscal 2013.

Moving onto gross margins. As compared to our guidance, our non-GAAP gross margin for the quarter was down a couple percentage points because of a heavier mix of lower margin titles such as Kingdom of Amalur, Reckoning and stronger catalog.

OpEx came in slightly lower than our guidance. The resulting non-GAAP diluted EPS was $0.17 for the quarter, higher than the midpoint of our guidance.

Turning to cash. Our cash short-term investments and marketable securities at the end of the year was $1.8 billion or approximately $5.78 per share. Roughly half of this amount was held offshore.

Net cash provided by operating activities for the quarter was $287 million. This was driven by our solid results and continued focus on operating efficiencies, such as reducing our inventory balances and increasing inventory turns to 22 times on a trailing 12-month basis, the highest level we have seen in the last seven years.

Our operating cash flow for the year was $277 million, slightly higher than our forecast of $250 million. During the quarter, EA repurchased 14.1 million shares at a cost of $241 million. We also repurchased another 4.3 million shares in April at a cost of $71 million. Accordingly, the $600 million share repurchase program has been completed.

Since inception of the program we retired a total of 32 million shares. Looking back at fiscal 2012, we delivered great results that were in line or above the original non-GAAP guidance we provided last May with over performance in many areas that offset retailer challenges in Europe, a delayed Star Wars launch, PopCap integration and a debt financing.

In summary, fiscal 2012 was an excellent year in which EA had a third consecutive year of at least double-digit non-GAAP operating margin and earnings growth. We look forward to continuing this momentum into fiscal 2013.

Turning to guidance, rather than walk you through the P&L and give line by line guidance we have laid out all of the pertinent GAAP and non-GAAP data points in the earnings release in our slide deck. Overall, based on the midpoint of our guidance we look to deliver non-GAAP EPS growth of more than 30% in fiscal 2013, driven by an increase in non-GAAP revenue, further gross profit and operating margin expansion, all of which are a result of our digital initiatives.

GAAP revenue is expected to be $4.075 billion, relatively flat to prior year. GAAP loss for the fiscal year is expected to be between $0.36 and $0.16 per share. Please note that a significant driver of the GAAP loss in fiscal 2013 can be projected $225 million increase in our deferred revenue balance for online enabled packaged goods due to the phasing of our release schedule this year and a likely increase in the period over which we will be recognizing revenue for GAAP purposes.

As we have stated before, this is only an issue on the timing of recognition, not collectibility, and has no impact on non-GAAP earnings or cash flow.

With regard to non-GAAP revenue, our PC and console revenue will be fueled by 14 excellent packaged goods titles, each of which will have significant digital offerings. We expect to see continued growth in virtually all areas, utilizing our brands effectively across mobile, social, Play4Free console and PC.

In addition to the multiple digital titles, we already support, we expect to launch 41 new titles across social, mobile, and Play4Free. Non-GAAP digital revenue will be increasing to close to 40% of EA's total non-GAAP revenue in fiscal 2013. We see a point not far in the future when digital revenue will be more than half of EA's total revenue. The increased mix toward digital revenue will have a positive effect on our long-term gross margins. In the short term, we expect non-GAAP gross margins to increase by roughly 1% in fiscal 2013.

OpEx. We expect to keep OpEx relatively flat as compared to fiscal 2012. As we always do, we took a critical look at our spending. We made some difficult decisions to reduce our spend on the current generation packaged goods front and this approach allows us to make the necessary incremental investments in our digital platform and technology. In addition in fiscal 2013, we will be investing approximately $80 million towards Gen4 technology to be well-positioned to take advantage of this future opportunity. As a result of this focus to accelerate our digital transformation, we will be implementing a small restructuring program that will result in eliminating positions and terminating licenses that do not align with this strategy.

In summary for fiscal 2013 on a non-GAAP basis, total revenue is expected to grow, driven by another year of growth in digital revenue, partially offset by a decline in packaged goods. The increased mix in digital revenue will drive an increase in non-GAAP gross margins. The combination of higher gross margins and solid cost management should positively impact operating margin, allowing us to deliver over 30% growth in non-GAAP EPS based on the midpoint of our guidance.

A few other housekeeping items. PopCap is expected to deliver double-digit non-GAAP EPS in fiscal 2013, consistent with our statements last July. CapEx is forecasted to be about $100 million for the year, down from $172 million in fiscal 2012. This reflects investments in our digital platforms and technologies.

Headcounts. As of March, our headcount was roughly 9,200 with about 70% of that in R&D and we expect to increase total headcount to 9,700 by the end of fiscal 2013.

Litigation. In Q4 we booked a $27 million accrual related to a potential settlement of an ongoing litigation matter. This nonrecurring charge has been excluded from our non-GAAP results. And perhaps most importantly, we expect to generate operating cash flows of at least $400 million in fiscal 2013, up over 40% versus fiscal 2012.

Lastly, I would like to provide some context to our Q1 guidance and the revenue basic for the full year. Our Q1 non-GAAP digital revenue will continue to grow year over year, particularly given the benefit of a full quarter of STAR WARS - The Old Republic, a continued momentum in microtransactions and digital services. This quarter, we expect to launch 11 digital titles in one packaged goods title.

As we look to revenue and earnings [phasings] for the rest of the year I'd like to remind you that the revenue impact from some of our digital launches particularly in social and mobile is much greater in quarters subsequent to launch. This has the effect of increasing revenue and earnings towards the back half of fiscal 2013, similar to fiscal 2012. We also expect to see our second-quarter non-GAAP earnings to at least double on a year-over-year basis.

Now I will turn the call over to Peter Moore.

Peter Moore - ***Electronic Arts Inc. - COO***

Thanks, Ken. Today I am going to provide some context and proof points to the strategic priorities John laid out. Brands, platform and talent. Each of these reinforces how EA's digital business has grown and evolved.

I'll start with our brands and one that I am very familiar with and that is FIFA Soccer. The world's most popular sports videogame is in position to scale to an even larger audience online. Our vision for the future is multiplatform gaming, anytime anywhere. A day when EA SPORTS FIFA will recognize players across any device and store their achievements, rewards, and community status in the cloud. [Next in 33] you'll see FIFA 13 take a huge step toward that goal.

In Asia, FIFA Online 2 is a microtransactions based Free-to-Play game with more than 28 million registered players. In Korea alone an astonishing 8 million people -- a huge percentage of our target audience in that nation -- have registered to play. In fact, our internal estimates suggest that as many as 80% of Korean males aged 16 to 19 have played this game.

In November, FIFA World Class Soccer launched on the Green Network in Japan and became the top ranking 3rd party title on that system. It had a $1 million day last week and has racked up $30 million in just 5 months.

FIFA Ultimate Team, a fully digital service which allows players to build teams and trade players, does not show up on the retail charts but was our second best-selling offering in the UK last year. Let me say that one more time. Our second highest grossing product never appears on the retail tracking charts.

With content downloads, and cross-platform identity and rewards, FIFA is pioneering much of our thinking about the connective brand universe. In fact, all of EA's core brands are developing similar ecosystems and affinity with players. SimCity, one of EA's most beloved global brands, is returning this year to PCs and mobile devices. The new game will be always on, always connected. SimCity was unveiled at GDC this spring and received a tremendous response from fans.

Additionally, our Maxxus label is planning a big social title which is scheduled for release this quarter. Our Battlefield brand has been pushing the edge of online combat for 10 years and along the way assembling a huge community with tremendous expectations. As we predicted, Battlefield 3 took market share last year and more importantly millions of players are still online, deeply engaged in this game. Battlefield Play4Free, a game with great graphics and a rapidly growing community, is a substantial business generating solid revenue.

Need For Speed is another brand with a great reputation and millions of committed fans around the world. Two years ago, the breakthrough autolog feature brought the community online to set up matches, establish leaders, swap cars, and share video with the most spectacular wins and crashes. And Need For Speed World is another title generating impressive revenue on our Play4Free platform.

Our PopCap studio is home to many of the most powerful brands in casual gaming. Since joining EA last year PopCap has been innovating and growing. In December they shipped a new IOS adaptation of Bejeweled, which quickly became EA's top grossing game on the Apple App Store. Their free-to-play names are showing good ARPU on mobile and they've doubled their Facebook footprint with 2 new games -- Solitaire Blitz and Lucky Gem Casino. And in the months ahead, you can count on new iterations of PopCap franchises like Bejeweled and Plants vs. Zombies. PopCap's financial performance is tracking with our expectations and we couldn't be happier they are on our team.

Next, I would like to address our platform strategy. We have already discussed how Nucleus with 220 million registrations enables Origin, which has generated approximately $150 million in digital sales.

Another platform ramping to a high-margin future is EA Play4Free. This proprietary site features richly detailed browser games, which quickly scales with revenue from microtransactions. Battlefield Play4Free and Need For Speed World are just 2 of the EA franchises generating big audiences and significant revenue already. The Play4Free platform generated $1.8 million per week in Q4 fiscal 2012, up 80% over the same period last year.

Another intriguing aspect of free games is its potential to serve as a funnel, introducing millions of new players to our brand universe. With this kind of scale, revenue, and profitability you can assume that more EA brands will be available on this platform in FY 2013.

Our investment in platform technology provides a number of advantages that expand revenue and margins. With a database of more than 220 million users, we have a powerful media channel built into our own platform, one which generates ad revenue and saves those millions that would have gone to other marketing outlets. Couple this with affinity marketing and we can realize a huge savings in the cost of customer acquisitions.

A few years ago, we spent 12 months and tens of millions of dollars recruiting a new audience while a game was in development. Today, we begin that process with platform technology that keeps us in constant contact with that audience. They are easy to find because we never lost them.

Now, a quick comment on breakthroughs we made in measuring product performance. We have reached a point when the sale of a disk is no longer the largest revenue event in the financial performance of a game. Unit sales are just a first event in a larger set of economics.

At EA, we are developing new metrics to capture the true scope of our enterprise. We measure how many customers have been acquired by a game or a service. We measure the degree of their engagement, how many minutes they spent playing. Most importantly, we have modernized our approach to tracking and managing game play monetization from retail, subscription, to full downloads, microtransactions and other streams of revenue.

It is a unique and revealing way to view our business and we want to share more of that information information with you, our investors. At E3, EA will host an Investment Breakfast where my colleagues, Rajat Taneja and Kristian Segerstrale, will outline our strategy for providing a better understanding of the market and the performance of our products.

I will finish with a personal note on EA's talent initiative. When I arrived 5 years ago EA was a confederation of silo businesses. There wasn't much communication between brands, between studios and marketing, or between technologists and creative teams. And there was little contact with consumers beyond the initial sale.

Today, we are a much more cohesive team, from our executive staff to the creative and marketing teams to the corporate groups that support them. Everyone is focused on a clearly defined unified set of goals.

Our digital goals have provided a common denominator that links talent, brands, and consumers and we're seeing an incredible infusion of new date DNA in the Company. Our University Outreach program brings in fresh faces and perspectives. Rajat is recruiting a workforce of engineers. Kristian is assembling a formidable marketing and digital analytics team, and Frank Gibeau oversees a group of the best creative leaders in the entertainment industry.

I have never seen EA more focused, more cohesive, more joined by a common goal. Thanks and now back to John.

John Riccitiello *- Electronic Arts Inc. - CEO*

Thanks, Peter.

To summarize, fiscal 2012 was a great year. But fiscal 2013 will be much better, an historic year for EA. This is the year that we break away from the pack with a very different profile and the traditional game companies we grew up with and with access and capabilities that none of our new digital competitors can match; a dozen powerful brands projected over a variety of devices by a powerful direct-to-consumer network; more than 220 million consumers registered and linked by infrastructure that recognizes their game identity to preferences, rewards and friends; every event captured, measured, and reported with meaningful metrics; all of it created and maintained by the industry's most talented people.

The key is digital revenue, which has a multiplier effect on our business. Digital revenue provides topline growth on a cost structure that creates improvements in gross profit and operating margins. Better margins allow us to invest in the future in big opportunities like Gen4 consoles. We have been through a lot of change, change we undertook to drive greater shareholder value.

Let me finish by saying it is a good time to be at EA. We are well on our way to having transformed our business model, change the company from Tower Records to iTunes from Blockbuster to Netflix, from Sears to Amazon. But, unlike many of our digital competitors, we draw our growth from more than one revenue source. We have a much more diversified revenue base with each digital segment growing rapidly, including our own direct-to-consumer services.

Moreover, we are building this digital business more organically than most and our vast portfolio of great brands enables us to do it more artfully and, we believe, in a way that is far more likely to win the test of time. We have got the right brands, the right strategies and, most importantly, the right talent. Years of investment are starting to pay off. From here, we capture the rewards.

With that we would be happy to take your questions.

QUESTION AND ANSWER

Operator

Edward Williams, BMO Capital Markets.

Edward Williams - ***BMO Capital Markets - Analyst***

Good afternoon. A couple of quick questions.

First of all, can you just comment a little bit about the Star Wars trend lines? What we saw out of paying subs? Since the game kind of -- call it since February 1 to now, so as the first billing cycles got passed through how those paying subs or sellers settle down? And then also looking at the digital revenue can you give us some color as to whether or not digital at this point in fiscal 2013 should be above in line with or below the core operating margins of the Company?

John Riccitiello - ***Electronic Arts Inc. - CEO***

There was a couple of questions there. Maybe Frank and I will split the Star Wars question. I'll start on the broader margin issue and then Ken can help us out. So, Frank, you want to start on the Star Wars trend line?

Frank Gibeau - ***Electronic Arts Inc. - President, EA Labels***

Yes, sure. The trend line on Star Wars is as follows. When we launched the product back in December, it was an event launch and we brought in a lot of users, and with a brand like Star Wars it reaches out much past the hard-core MMO fan base into the broader market.

And as the service evolves from here what we're seeing is that some of those initial casual customers have gone through a billing cycle and decided not to subscribe to the game. But for the most part, we are seeing very good retention amongst core MMO users, which has given us a solid base of around 1.3 million subscribers.

The percentage of paying subscribers from our peak until now has actually gone up, and the folks that we have are as engaged as they were when they first bought the product. And in fact if you look at how we are going to be releasing content going forward, we have a lot of elder gameplay, a lot of extension content that will keep them engaged and continue to grow subs.

Make no mistake, BioWare tends to grow subscribers. This quarter alone we released 2 major content upgrades designed to drive subscription loyalty and, again, we have got many more plans throughout the year.

We are also having a lot of success with our free-to-play weekends and buddy key promotions which is helping us drive acquisition, and we will continue to hit those. And we are actively planning territory and platform expansions and extensions in Europe and Asia for STAR WARS - The Old Republic. So we feel like we have got a very strong base that for over the long term we are going to continue to grow.

John Riccitiello - ***Electronic Arts Inc. - CEO***

A couple of quick thoughts on Star Wars before we turn to digital margins. I understand that a lot of investors are very interested in Star Wars. I just wanted to put a couple of thoughts into perspective. This is something Ken mentioned on the call.

First off, Star Wars' performance right now is very much in line with our original assumptions and the assumptions in where we are guiding folks to over the last couple of years. Where that puts it in our portfolio is, in terms of profitability from a franchise, it's in our top 10 but it is not in our top 5. So as a business contributor, while important, it is not as important as Medal of Honor or Battlefield or FIFA or Madden or the Sims or SimCity but it is more important than Tiger Woods PGA Golf.

So while I understand there is an enormous amount of interest, I don't know that it warrants as much what we're seeing right now. But we love the franchise. We are going to grow the franchise and just like we want to see Tiger Woods Golf grow or SSX grow or Madden, for that matter, we are going to drive this one for growth.

The second thought that I would throw your way relates to your second question, which is digital margins. I would give you 2 bits of context. Where we are in terms of putting our digital services in the marketplace and how profitable they are long term.

In a number of cases, we haven't yet launched a product that is more informative than behind us. The overall business sector -- for example, social is less profitable than our console business as when it carries everything going forward that we have got on our development pipeline. But as we model business as it scales when these new products get into the marketplace and start generating revenue, it is a more profitable business. And in fact if you track EA's gross profit trends and operating margin trends over the last 3 years, the key contributor to having our gross profit percentage rise and our operating margin percentage rise is in the addition of visual [renovations] that makes us more profitable.

Some businesses get to a great profit profile very quickly like Play4Free. Others are breaking through and getting to good profitability like Origin. Mobile is in a good place. Social is moving to a good place. But all in all, it is a net plus in a big, big way. I think Ken covered it there. So next question.

Operator

Neil Doshi, Citigroup.

Neil Doshi *- Citigroup - Analyst*

Thank you very much. Another question on Star Wars, John. With a large competing brand coming out later this year potentially, but what else can you do to kind of maintain and grow sub to the back half of the year? And then secondly on mobile, we saw a kind of nice growth in the 20% plus range down for 2 quarters in a row. Is that the type of growth we should be thinking about going forward? Thanks.

Frank Gibeau *- Electronic Arts Inc. - President, EA Labels*

I will take the Star Wars question. You know, I think what's important in an MMO is to continually update the game and add new experiences and new features and elder game play that keeps people retained and keeps the viral component of the service active. And from that perspective, we have a very aggressive release plan of content for the rest of the year and beyond. And it is mainly focused in on adding a lot of new elder game content around PDP, around achievements, and a lot of other feature sets that the fan bases are asking for.

It is also important that we are going to be giving the guilds a lot of features and components that they are requesting as well. So we are cognizant of competitors coming, but none of them quite fit into the same competitive category as Star Wars. They are just -- they are different fantasies. They are not the Star Wars fantasy. It is not the big expansive universe that appealed to so many people worldwide.

And as you know, with MMOs, every day you are in operation, they get better and better and better. You continually perfect the experience; you continually improve the acquisition component; and so building from a base that we are at right now we feel very confident that this business is going to continue to stay competitive throughout the remainder of the year.

John Riccitiello *- Electronic Arts Inc. - CEO*

You asked a question about ongoing growth of 20%. But I didn't hear the sector you are referring to.

Neil Doshi *- Citigroup - Analyst*

Sorry. That's on the mobile side.

John Riccitiello *- Electronic Arts Inc. - CEO*

All right. So think of mobile as 2 businesses just to get a sense of it. There is the traditional marketplace of Java Brew, the old feature phone business. And then you got the smart phone business. In our most recent year and quarter we had better than 80% growth on the smart phone business. If you take a look at the slides, you'll see better than 90% growth.

So we are absolutely killing it there and we are seeing strong expansion. When it blends down into the 20s it is because we are still living on the tail end of Java Brew, but it is starting to evaporate. But I think we are doing practically fantastically well on the smart phone business.

Peter Moore - ***Electronic Arts Inc. - COO***

Just let me refer you to the slides as well for a little bit more color and texture on mobile. If you go to slide 22, you'll see the representation of our titles across not only mobile but social and free-to-play. 25 of the 41 we feature there and the phasing is on slide 25 is mobile. And what I can tell you is that the quality of the brands that we are linking mobile to in fiscal year 2013 is far superior than we did in FY 2012.

So the concept of mobile tying into our brand universe element is spot on. So look at that breakdown. You can see their 25 mobile titles being launched in FY 2013.

Neil Doshi - ***Citigroup - Analyst***

Great. Thank you.

Operator

Arvind Bhatia, Sterne, Agee.

Arvind Bhatia - ***Sterne, Agee & Leach, Inc. - Analyst***

Thank you. Couple of questions. One, I wanted to be sure I understand the revenue guidance for next year a little bit better. I think, John, you guys had talked about double digits before. You mentioned a shift of a title. Is there anything else that we should be factoring in the delta versus the prior guidance? And then second question on the next gen, is it fair to think that the next gen will not see the same step function increase that we saw in the prior cycle? Or help us understand how we should think about that.

John Riccitiello - ***Electronic Arts Inc. - CEO***

Step function increase in what? I didn't quite understand what you're asking.

Arvind Bhatia - ***Sterne, Agee & Leach, Inc. - Analyst***

In the cost -- I'm sorry, in the development cost for title you mentioned the $80 million that you are investing this year. Wondering and maybe it's early but just as you think about the next generation, what sort of cost increases should be factoring in on a per title basis?

John Riccitiello - ***Electronic Arts Inc. - CEO***

So, in terms of your first question was about our guidance. I numerated a number of considerations that went into our FY 2013 guidance in the prepared remarks. I'd say the biggest one versus my prior expectation in terms of the one downward movement was we removed a major packaged goods title. And in parallel with that, we added significant R&D for Gen4. In a lot of ways they are sort of offsetting.

We believe we are heading into a world where we won't have strong digital growth, partly offset by console declines. We believe we are entering a world where we are going to have strong visual growth complemented by strong console growth. And that console as it is today will be a blend of digital and packaged goods.

In terms of next-generation content, I really wouldn't want to get into that more than we are right now. But we are confident that EA is going to be able to continue to grow, accelerate that growth, and accelerate our margin expansion.

Arvind Bhatia - ***Sterne, Agee & Leach, Inc. - Analyst***

Okay. Got it. Thank you.

Operator

Colin Sebastian, Robert Baird & Company.

Colin Sebastian - ***Robert W. Baird & Company, Inc. - Analyst***

Thanks very much. So obviously, FIFA and Battlefield are 2 success stories you have in transitioning franchises through the hybrid online and traditional business model. Was curious about the timing of this transition for some of the other core EA games and if that represents a big part of the additional growth you are expecting in the year ahead?

Frank Gibeau - ***Electronic Arts Inc. - President, EA Labels***

We are definitely taking the model for Battlefield and FIFA and applying it to franchises like Need For Speed, [Massatec] obviously just released with multiplayer and MTX and we are having great results with that. So this is deftly a model that works for us and you'll see that expanded across the entire line of the console products going forward.

John Riccitiello - ***Electronic Arts Inc. - CEO***

So think of it as it is far from the first inning here. The middle of our range this year, I think it is fair to say it is fourth or fifth inning. You'll see lots of pieces. E3 will be an eye opener.

But we think EA is doing this uniquely because our competition doesn't have strength in console PC, mobile, social, microtransactions, subscription, packaged goods, et cetera. We do. And it is the rare exception for a franchise. It is not really hitting on the majority of those plus points in fiscal 2013.

Colin Sebastian - ***Robert W. Baird & Company, Inc. - Analyst***

Thanks and maybe just as one follow-up perhaps update your views on the state of the social game markets, at least on browsers. There was a little bit of a sequential slowdown in credit revenues reported by Facebook and potentially some regulatory issues coming out of Japan. If you could maybe just address that. Thanks very much.

Peter Moore - ***Electronic Arts Inc. - COO***

I'm not sure about the second half of your question but, certainly, when you look at the lineup we've got, we certainly expect to grow very strongly our share on Facebook this year. Based on the strength of what we're seeing in our social lineup we're again bringing brands to play and tying into Frank's earlier comments of tying those brands together, increasing the funnel, making sure that we are delivering I guess more free-to-play experiences for a broader base of users. And you can expect us to see that turn into market share growth on the Facebook platform in particular.

I can't comment on your second question about regulation. I am not sure what that is all about. Maybe we can get back to you on that one.

Frank Gibeau - ***Electronic Arts Inc. - President, EA Labels***

One point to note there, is that we do think a browser is broader than just Facebook. If you look at our Play4Free platform, we are offering quite a few game services there in that and they are now operating native through Explorer, Safari, Chrome, whatever. Those are actually considered platforms for us and they are very profitable and very global. So when we think of browsers, we're not strictly limited to Facebook.

John Riccitiello - ***Electronic Arts Inc. - CEO***

Yes, there is a slide in our presentation if I could find it -- I think it is slide 17. Think of Play4Free as EA's own -- that is the bottom right slide. Think of that as EA's own social network and within EA's own social network, which is just PC-centric, we have seen an 80% growth in weekly revenues from Q4 F 2012 to Q4 F 2011.

But we are also very successful partnering with Neowiz in Korea, [Gree] in Japan, you know there's no question that relative to Japan one of the challenges the social business is a little bit trapped on the feature phone. The transformation to mobile and smart phones is going to be an interesting one. I know that we are sort of in a win-win situation. We do well on the feature phone and we do well on the smart phone. So we are not particularly anxious about that transformation.

My sense is over time, now to get to your question, that as we are looking at the broader definition of what operates like a social network, a microtransaction-based model that's delivered free-to-play to the consumer that's supported for us on a microtransactions business in a largely social format, we are going to see Facebook be an important partner; our own platform likely to be our largest business; and then we are going to be partnering as we do today with Tencent and Gree and Neowiz and others. So it will be a multi-partner plus EA direct-to-consumer model.

Colin Sebastian - ***Robert W. Baird & Company, Inc. - Analyst***

Great. Very helpful. Thanks.

Operator

Justin Post, Merrill Lynch.

Justin Post - ***BofA Merrill Lynch - Analyst***

Looks like we are maybe approaching the third cycle. I have been -- since I've been following the industry here and usually earnings really get hit hard during the console cycle because the costs go up and you sell fewer units on the new platform.

Could you talk about maybe whether you already have the development kits? Is fiscal 2014 the transition year? And maybe why EA could be better positioned for this cycle than prior cycles? And then I have one follow-up. Thank you.

John Riccitiello - ***Electronic Arts Inc. - CEO***

Usually relative to what we know about the hardware and what is coming, et cetera, I really wouldn't want to get into that. I think I would like to refer you to Sony, Microsoft, et cetera. I would say if you were going to try to and analogize where we are today, this would be a down year for us, fiscal 2013, when we are investing the $80 million we would be otherwise reflecting a negative EPS trend. We are absolutely a different company in a different spot.

In the face of unfortunately somewhat of a headwind relative to console, we are getting topline growth, robust digital growth, robust margin expansion, robust EPS growth while affording the investment in the next gen console. I don't think going back to our foundation 82 that has ever happened before. So what we are guiding for is entirely unprecedented and it is a function of everything we've been saying on the call so far.

We built that digital business. We are tethered to consumers, we are monetizing in a very different way. Remember, we are not transitioning in the past 50, 60 individual packaged goods games. We have got -- think of it as being 20-ish core intellectual properties that are running across mobile, social, PC console, microtransactions, subscription, packaged goods revenues and a lot of that packaged goods revenue is actually digital break through the Origin store. So a very, very different business.

It is our hope to be able to accelerate topline through a transition and accelerate bottom-line growth through a transition. Because we won't be facing negative Console compares.

Justin Post - ***BofA Merrill Lynch - Analyst***

Great. And then a couple of other questions. Couple of success stories you've had on digital are FIFA and, I think, Battlefield. Maybe you could talk about what margins look like for the entire franchise for those versus when they were just packaged goods. And then I think you said 5 Facebook games on the last call. Is that still the number for the year? And the first one is still in Q1? Thank you.

John Riccitiello - ***Electronic Arts Inc. - CEO***

Well in terms we haven't put out -- great question. We haven't put out overall franchise profitability. But if you think about the fact that we've gone from 67 titles where we were making $0.30 a share and now we've got 14 titles that we are guiding to well north of $1 a share, obviously, franchise profitability is sky-high in terms of where we were and where we are.

So I mean the numbers have got to be virtually off the chart, because we have got 1/3 as many titles or 1/3 as many franchises, generating 300% the income. So I am very confident without having a debt at my fingertips that these things are moving up and to the right in a truly fantastic way.

In terms of launches on social, 5 is conservative. We have given you a combined number for mobile social and I hate to keep referring you to the slides but it is listed in the slides and the reason we are not trying to give much more guidance on mobile social titles is there's an awful lot of circumstance today where 4, 6, 8 weeks in front of a launch, people will sort of copy your name and take a spot on -- in the app store of certain of our partners and/or Facebook with a look alike, sound alike, feel alike.

So we don't do the advanced communications of the individual title so much as a surprise launch. We are not looking to get ambushed by folks that are trying to benefit from dropping in under our marketing window.

Justin Post - ***BofA Merrill Lynch - Analyst***

Thank you.

Operator

Brian Karimzad, Goldman Sachs.

Brian Karimzad - ***Goldman Sachs - Analyst***

2 questions. The first one -- and apologize if this was touched on in remarks about guidance. But when you look at the $2.5 billion of nondigital revenue for this year, for the publishing side, looks like you have cut the title count by about 1/4 and then backing in, that $2.5 billion looks like it is down about 15% or so. What are you baking in for like-for-like growth and packaged goods either in your industry outlook or title versus title where you have and you would compare? Just to get a sense of what you are baking and given what we have seen in the first quarter so far even in high-def packaged goods being weak?

And then the follow-up would be on your decisions for investment in social versus mobile, as you decide which one of those to put an incremental $1 towards on one side with smart phones, there really is no clear leader there; whereas in social you certainly have one and they have some interesting advantages. How do you take that into consideration and how is that evolved over the last year?

Peter Moore - ***Electronic Arts Inc. - COO***

Let me get that first question at least. We are projecting single-digit declines in packaged goods this year and, of course, high double-digit growth in the digital space. And it is something that we have seen over the last couple of years. We expect that trend to continue. We have got a very strong lineup of titles and, again, I will defer to E3 and see our lineup then, which will be presented fully, and you'll get a taste of that at the Investor Breakfast on the Wednesday morning.

But as I say, bottom line is we are looking yet again, single-digit decline in packaged goods, high definition package goods, and strong growth in digital.

As regards making decisions, investment decisions in social and mobile, it is really a difficult question you asked. It depends on where we are, what device, what is the brand, where we see the best return, what is the game play mechanic. It is a lot of things that we do. But I will refer you once again to the slide deck. You can see the amount of games we are doing, 41 across that titles. You can see the facing as well on slide 24 of where we are bringing it all to bear.

So Frank, I don't know if you have got any development --.

Frank Gibeau - ***Electronic Arts Inc. - President, EA Labels***

One addition. Just in terms of the sector performance in high def, low def for the year. I don't think our industry forecast of down single digits is different than most. It has been a little weaker so far this year. That is more of a function of industry level content availability.

There's -- we have got a strong compare to some titles last year in the first couple of months of the year and as we -- as the sector moves on later this year we expect to see the comparison favor well over 2011. So I think we are solid there. And we are basically participating, roughly, holding share in packaged goods against a smaller title count. So our revenue per title is rising dramatically.

In terms of mobile social, here's one thought for you. We are tending to bring the same intellectual properties to mobile and social, and we are increasingly getting very similar product execution because the mechanics. The amount of time people spend on them, the type of mechanics that's working, the business model, the free-to-play market which is working across mobile and social. And we are really programming against the Asian opportunity, the Western social opportunity, Android, obviously IOS.

Brian Karimzad - ***Goldman Sachs - Analyst***

Very well. Thank you.

Operator

Atul Bagga, Lazard Capital.

Atul Bagga - ***Lazard Capital Markets - Analyst***

I have a couple of questions on the platform side. You mentioned on Origin your install base. Can you talk a little bit about what does that give you their base and also in terms of revenue, what was the breakup of revenue within first party titles versus third party?

Peter Moore - ***Electronic Arts Inc. - COO***

So, yes, there are 11 million installs of the Origin clients active on desktops today. As regards your second question, the overwhelming majority right now, the revenue is first party, as you might imagine. We are anticipating very strong third-party growth. You can watch it every week as a number of third-party titles come onto the Origin client. I know you are a customer, and you can see as we grow that portfolio that third party in fiscal 2013 will be a stronger part of our portfolio when we think about our growth in Origin.

But for fiscal 2012, it was overwhelmingly first party and of course as might you'd imagine Battlefield and Star Wars.

Frank Gibeau - ***Electronic Arts Inc. - President, EA Labels***

Yes. The one thing to add as you look at games as a service, Origin is one part of the platform. When you are looking at the total audience size, again the Nucleus account data is really representative of the consumer base that we are marketing into, which is over 220 million as reported this quarter. So as we look at the cross-platform execution in our key franchises like FIFA and Need For Speed, Battlefield, there is an Origin component to that but then there is also an in game commerce component to that. And we are actually building audiences that we are carrying from version to version in a much more efficient and leveraged way.

So to your first part of your first question, it's a component of Nucleus and Origin that we look at in terms of how we are deploying our platform.

Atul Bagga - ***Lazard Capital Markets - Analyst***

And how does Play4Free fit into this? Do you expect to become 2 separate platforms or do you have any plans to merge these 2? And maybe if you can give some breakup of Play4Free, what is the current user base and how is that broken into Eastern markets versus the Western markets?

Frank Gibeau *- Electronic Arts Inc. - President, EA Labels*

Yes, the Play4Free platform has about 60 million registered users right now and it is predominantly Western-focused. I am not including the FIFA Korea data in that. If you include FIFA Korea it takes that number up substantially. But in general it is a platform that appeals to emerging markets, as well as first country markets like US and Germany, as an example.

It is growing aggressively and it is a key component of our cross-platform strategy to bring Battlefield not only to the Play4Free category but also on the consoles. And we are able to track users that are in either game service and be able to upsell and cross-sell them into the other one. So it is a highly monetizable platform. How it evolves from here with regards to Origin and the rest of the platform, that is something we are actively working on right now.

John Riccitiello *- Electronic Arts Inc. - CEO*

One thing for those of you that haven't attempted to take a look if you just type in EA Play4Free -- that's Play with the number 4 Free -- you can see the platform play it and try it. It is all up there. It also gives you an awful lot of data about who is doing what and when.

So for those of you that are asking questions if you haven't had a chance to take a look at it, we essentially modeled this off of some very successful companies that we admired that were generating strong digital revenue. One was Nexon, one was [Game Forage], a private company based in Germany, that have built very substantial businesses here.

It is more or less EA's version of a social network for micro-transaction games and it tends to attract consumers that are high monetizing and slightly more core than a straight up social network. It is a great business.

Atul Bagga *- Lazard Capital Markets - Analyst*

Great. Thank you.

John Riccitiello *- Electronic Arts Inc. - CEO*

We have time for one more question.

Operator

Doug Creutz, Cowen & Company.

Doug Creutz *- Cowen & Company - Analyst*

If I look at the App Store today, roughly 3/4 of the games that are in the top 20 grossing titles at any given moment are from smaller developers that aren't part of larger, well-capitalized entities. There's been 2 fairly major acquisitions in the space announced in the last 6 weeks. I am just wondering right now how you are looking at potential M&A opportunities in the mobile space and how you are feeling about that for the next year? Thanks.

John Riccitiello *- Electronic Arts Inc. - CEO*

Top line for me on this. First off, we are the leader in all mobile IOS and Android on a 2011 basis. We are second in social. Our competitors in San Francisco have a very strong lead in social and best I can tell, they are number 2 in mobile. And my guess is we are going to trade leads and we are going to gain share in social.

So I guess first observation is that a very large portion of the business comes from just the 2 of us and I think we are pretty well capitalized. Just not to disagree with the thesis, but I think there is a lot coming from the leading players. As is -- I would expect this to consolidate more and more around leading players, leading brands taking more and more share.

In terms of the acquisition, to be honest with you, I am pretty anxious about acquiring instant one-hit wonders in the space. There is an awful lot of noise that grows up around an individual franchise as it rises. Less so as that individual franchise went into decline. A lot of time, I think when people are acquiring individual new intellectual properties in mobile and social, they try to put an earnings multiple on it. Should it be a 10X or a 20X.

But the problem is that to put anything on it more than a 3 or 4X you have to have a belief that this thing is going to last a very, very long time. If something is going to come and go in 3 or 4 years, you can't put a multiple. You have got to add up 3 or 4 years' profitability to figure out what to pay for it and then do some sort of a risk-adjusted discount on that.

We actually think with The Sims, SimCity or with what we have got in Bejeweled and the rest of the PopCap IP, we are blessed with an unbelievable portfolio of brands. We don't need to buy a brand just to get a temporary lead on top of the charts or whatever is hot this quarter. That doesn't mean that we would never buy or never invest, we would.

But right now what I am starting to see is valuation expectations that assume that these things are all hockey sticks moving up and to the right with no end in sight, I think those are bad assumptions. Some of them will work, some of them won't. But they can't all be worth the multiples that I am seeing in the market right now.

Rob Sison - ***Electronic Arts Inc. - VP, Investor Relations***

And with that I think we'll cut it off now.

Operator

Yes. Thank you.

(multiple speakers).

Operator

This concludes today's conference. Thank you for your participation. You may now disconnect.