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EA - Q2 2016 Electronic Arts Inc Earnings Call

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OVERVIEW:

Co. reported 2Q16 non-GAAP net revenues of \$1.15b and non-GAAP diluted EPS of \$0.65. Expects FY16 GAAP revenues to be \$4.4b and GAAP fully diluted EPS to be \$2.32. Expects 3Q16 GAAP net revenues to be \$1.08b and GAAP loss per share to be \$0.17.



CORPORATE PARTICIPANTS

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Andrew Wilson *Electronic Arts Inc. - CEO*

Blake Jorgensen *Electronic Arts Inc. - CFO*

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PRESENTATION

Operator

Welcome, and thank you all for standing by. (Operator Instructions). Today's conference is being recorded. If you have any objections, you may disconnect at this time.

Now I will turn the meeting over to your host, Mr. Chris Evenden. Sir, you may begin.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Thank you, Kai. Welcome to EA's fiscal 2016 second-quarter earnings call. With me on the call today are Andrew Wilson, our CEO; and Blake Jorgensen, our CFO. Peter Moore, our COO, 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. A quick calendar note: our Q3 earnings call is scheduled for Thursday, January 28, 2016.

This presentation and our comments include forward-looking statements regarding 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 today, October 29, 2015, and disclaims any duty to update them.



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 Andrew.

Andrew Wilson - *Electronic Arts Inc. - CEO*

Thanks, Chris. Q2 FY16 was a strong quarter for Electronic Arts as we delivered new EA SPORTS experiences and dynamic live services for our players. Revenue, margin, and earnings were above our guidance, and we are raising our full-year outlook to reflect continuing strength in our business and excitement for our upcoming titles, including Star Wars Battlefront.

To understand how Electronic Arts is delivering for our players today, we look at player engagement in our games and services. We see our opportunity along three key vectors: bringing in more players to experience our games and services, enabling them to spend more time with the games they love, and making it possible to connect through more platforms and delivery models. Time is the most valuable commodity we have in today's digital world. With every new game, every update in our live services, and every community interaction, we are focused on delivering more value for our players through deep and personal engagement.

Highlights from our second quarter demonstrate how more players are spending more time on more platforms in our games today. Monthly average players increased 30% year-over-year across our annual EA SPORTS franchises that launched new titles in Q2: Madden NFL 16, NHL 16, and FIFA 16. Our live services for Battlefield Hardline and Battlefield 4 are thriving, many months after launch, with more than 6 million monthly average players across the two experiences. Madden NFL Mobile launched a full game update this year instead of a new app download. The result was a seamless experience for players, which increased retention, and resulted in game sessions up more than 300% over last year.

And, last but not least, EA Access is accelerating. The subscriber base more than doubled in the last two quarters; we've added five new games to the vault this year; and we're excited about what we're learning, as players engage through this service.

These titles and live services, as well as many more in our portfolio, are giving us strong momentum moving into the holiday season. Looking ahead, they will be joined in Q3 by two of our most exciting and groundbreaking new experiences. First, the return of Need for Speed is here, with players able to join a trial by EA Access today, and launching for everyone on Xbox One and PlayStation 4 beginning November 3.

Excitement in the community has been growing as fans learn more about the cars, customization, and unique stories in the game. The game looks fantastic. And after a closed beta conducted earlier in October, the Ghost Games team has been working directly with community feedback to deliver the experience our players want. With more than 70 different customization categories, and twice the amount of road to race as our previous game, the passion for speed and car culture will be unleashed in a new Need for Speed.

Starting in just 19 days, the galaxy far, far away will once again be at the center of our universe, as Star Wars Battlefront launches around the world. Engagement in and around the record-breaking beta was huge, with more than 9.5 million players logging on to play, 19 million viewers tuning into video streams, and almost 3 mentions per second on social networks during the beta week.

Stability and scalability of our online services continues to be a top focus for us. In addition to our extensive internal testing, the millions of gameplay hours logged during the beta across multi-player, single-player, and co-op modes further tested our infrastructure to help prepare a stable experience for our players, at launch and beyond.

Over the next few weeks, innovative new experiences will allow players to connect and learn more about Star Wars Battlefront. Our most avid Star Wars Battlefront fans can sign up for free to receive exclusive content and advanced access to new information about the game. Through the

largest-ever user-generated content program we've ever launched, awesome and inspiring moments from the game will be shared with millions in the player community. And a fully immersive Web experience will put fans right in the world of Star Wars Battlefront.

Through it all, our integration with the upcoming film will ensure we're fully connected to the rising passion for Star Wars that is captivating the world. Come join us in Star Wars Battlefront, beginning November 17, or November 12 for EA Access members.

As we continue our focus on putting players first at Electronic Arts, we strive for quality and innovation in every experience. In addition to stability, security, and availability, we are taking creative leaps to make each game memorable and fun. We will always work to take the necessary time to get the combination right for our players. And early this afternoon, we announced that we are shifting Mirror's Edge Catalyst release to May 24, 2016.

We're going to take a few additional months to make the city of glass and the unique first-person action in Mirror's Edge Catalyst even more spectacular. With players spending more time in our games and live services, and two stunning new experiences launching this quarter, we're looking forward to the holiday season and the remainder of the fiscal year for Electronic Arts.

Now I will hand the call over to Blake for a deeper look at our financials.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Thanks, Andrew. EA's non-GAAP net revenue was \$1.15 billion, which was \$71 million or 7% above our guidance. The quarter's revenue was 6% lower than the prior year's, as a result of an FX headwind of \$110 million, and The Sims 4 launch last year. However, on a constant currency basis, revenue would have been 3% greater than last year's, thanks to strong launches of our EA SPORTS titles, led by FIFA 16 and Madden NFL 16, and from their associated Ultimate Team live services. As well as frontline success, we sought ongoing strength from our catalog, particularly The Sims 4, and Battlefield.

In addition to our strong performance, this quarter's revenue includes a \$30 million benefit from the recognition of some revenue from special editions of sports games sold in the quarter. It relates to Ultimate Team content included in these versions we had originally forecast to recognize in Q3.

Our non-GAAP digital net revenue for the quarter increased 6% year-over-year to \$480 million, 42% of this quarter's revenue. The trailing-12-month digital net revenue was up 15% to a record \$2.31 billion.

Breaking down our digital revenue into its key components highlights the performance of each of these businesses this quarter. Extra content and freemium contributed \$195 million, up 27% over the prior year. The principal driver of the growth was Ultimate Team across our sports franchises. In addition to the strength of these live services, we benefited from an extra week of FIFA 16 sales in the quarter compared to last year. The new games modes we added to Madden NFL 16 and FIFA 16 are proving effective in deepening engagement.

In addition, FIFA Online 3, our PC free-to-play title for China and Korea, continues to perform well, and is tracking to our expectations.

Mobile generated \$113 million in the quarter. The free-to-download component was up 2%, or 9% up at constant currency. During the quarter, we launched Need for Speed No Limits, EA SPORTS FIFA 16 Ultimate Team, and a full game update of Madden NFL Mobile. Madden has been a top 5 grossing game in the US on the iPhone Apple App Store in October. These new titles, together with the just-launched Minions Paradise, the upcoming Star Wars Galaxy of Heroes, and our existing live services, will help continue to grow our mobile business.

Full game PC and console downloads generated \$89 million of revenue, down 5% over the prior year, due in part to FX. At constant currency, this revenue would have increased, as the growth in console downloads more than offset the absence of The Sims 4 this year. Our new titles in the quarter averaged around 20% full game downloads, with the exception of FIFA, which skews lower, due to strong retail sales in Europe.

Subscriptions, advertising, and other digital revenue contributed \$83 million, down 9% from last year, due to the natural decline in Battlefield 4 premium revenues. EA Access is delivering strong, sustained growth. And, finally, with regards to subscriptions, we launched a major expansion for Star Wars: The Old Republic on Tuesday. Subscriptions are up 31% since the expansion was announced to their highest level since February 2014. We're optimistic about its continued performance in terms of both subscribers and free-to-play in the run-up to the first new Star Wars movie in a decade.

Moving on to gross margin, our non-GAAP gross margin for the quarter was 65.4%, a decrease from last year's 66.1%, but above our guidance of 63%. Last year's Q2 gross margin was exceptionally strong, due to The Sims 4. About 100 basis points of the margin outperformance this quarter was driven by the \$30 million in high-margin revenue mentioned earlier. A stronger-than-expected product and service mix also drove margin above our guidance.

Our non-GAAP operating expenses for the quarter were \$479 million, down \$18 million year-on-year, driven by FX. The improvement on guidance was driven by phasing and continued cost control. At constant currency, OpEx would have been up approximately \$16 million, chiefly driven by increased investment in R&D.

The resulting non-GAAP diluted EPS was \$0.65 per share, which is \$0.25 better than guidance, due to our strong top-line performance, continued cost management, and the revenue phasing described earlier. At constant currency, EPS would have grown year -- over last year.

Our cash and short-term investments at the end of the quarter were \$2.59 billion, or approximately \$8.32 per share. 57% of this cash and short-term investment balance is held onshore. This is down from 64% held onshore last quarter, the difference being driven by the redemptions of our convertible notes and stock repurchases.

During Q2, we settled close to \$200 million in early conversions of our convertible notes. And as of yesterday, we've received notices for an additional \$95 million to settle in Q3. We have updated the dilution table on our website accordingly. We also repurchased 1.8 million shares at a cost of \$126 million, leaving \$798 million in our two-year, \$1 billion buyback program we began in May 2015. The current rate of repurchases keeps us on track to complete the full \$1 billion in that time.

Net cash provided by operating activities for the quarter was \$9 million. Operating cash flow was down \$174 million from last year, as a result of fewer launches in Q1 of this year compared to last, and also due to the timing of various items. On a trailing-12-month basis, operating cash flow was \$818 million.

Turning to guidance. Due to our continued strong performance, we are again increasing our full-year outlook. The open beta for Star Wars Battlefront was exceptionally well received by players. Consequently, we are raising our unit forecast for sell-in during fiscal year 2016 to approximately 13 million units. This is partially offset by increased FX headwinds and our decision to move Mirror's Edge Catalyst into fiscal 2017. And remember that the \$30 million of the beat in this quarter was already in our annual outlook, as part of our anticipated Q3 revenue.

Our new full-year guidance for non-GAAP revenue is \$4.5 billion, up \$50 million on our prior outlook. Our guidance for non-GAAP EPS increased by \$0.15 to \$3 per share. We anticipate an operating margin of approximately 28%. Since the start of the fiscal year, we've raised guidance by \$100 million on revenue and by \$0.25 on earnings. The GAAP guidance becomes \$4.4 billion in revenue, and \$2.32 of fully diluted EPS.

Regarding cash flow for the full fiscal year, we are increasing our operating cash flow guidance to approximately \$1.2 billion. Our capital expense forecast remains approximately \$100 million, resulting in a free cash flow forecast of approximately \$1.1 billion.

Guidance for our third quarter is for non-GAAP net revenue to be \$1.78 billion, 24% higher than last year's. Growth is driven by the launches of Star Wars Battlefront and Need for Speed, plus the growth of live services, particularly Ultimate Team.

FX presents a year-on-year headwind of around \$110 million to Q3 revenues. Non-GAAP gross margin is forecasted to be 71.5%. We expect our Q3 non-GAAP operating expenses to be \$540 million, up slightly year-on-year, driven by increased investment in R&D and phasing from Q2, offset by FX. This results in a non-GAAP diluted EPS of \$1.75 per share as compared to \$1.22 last year.

Our Q3 GAAP net revenue is expected to be \$1.08 billion as compared to \$1.13 billion in the prior year. GAAP earnings per share is expected to be a loss of \$0.17, as compared to earnings of \$0.44 last year.

Our business exceeded our expectations again this quarter. FIFA 16 in particular had a very successful launch, as measured both by number of unit sales and by engagement level. This has provided a solid foundation upon which to grow our live services through the product cycle. Reception of the Star Wars Battlefront beta has led us to increase our unit forecast. And early indications for Need for Speed are excellent. The growth of our console installed base and powerful mobile devices continue to fuel the growth of our business. We're looking forward to an excellent holiday season, and another year of strong earnings and cash flow growth.

Now, I will turn the call back to Andrew.

Andrew Wilson - *Electronic Arts Inc. - CEO*

Thanks, Blake. Around the world, billions of hours a week are spent playing video games. No matter what device you're playing on, what type of experience you seek, or where you are in the world, games are becoming a more meaningful part of our lives. The opportunity to connect more people to amazing experiences, and to each other, through play has never been more profound.

At Electronic Arts, we are focused on delivering more stunning games and groundbreaking services that will inspire the world to play together. Epic fantasies like Star Wars Battlefront that span generations of fans; EA SPORTS experiences that unite millions of passionate players; mobile titles like Need for Speed No Limits, SimCity BuildIt, and Madden NFL Mobile, that can immerse you no matter where you are, or how much time you have. And services like EA Access and Origin that are helping players try more games and share the play experience with friends.

It has been a strong first half of FY16 for Electronic Arts, and we have amazing opportunities still ahead of us. The games and services we are delivering represent EA's greatest strengths: pioneering, creativity, and passion, channeled into experiences that will inspire play for a long time to come.

We're excited for the road ahead.

Now Blake, Peter, and I are here for your questions.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Kai, if you could open up the line for questions now, please.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Chris Merwin, Barclays.

Chris Merwin - *Barclays Capital - Analyst*

You obviously continue to make a lot of progress on the margin front. And you were at slightly more than 50% digital, as of last fiscal year. So as that shift continues, can you just update us on what the long-term margin target for the business looks like, just in terms of non-GAAP operating income?

And then secondly, extra content sales growth reaccelerated really nicely in 2Q. And I think you mentioned that the new launch of FIFA 16 and FIFA Online 3 were drivers there. So should we expect the momentum to continue there through year-end? And what are you implicitly including in your guidance, just in terms of extra content for the full year? Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

This is Blake. In terms of the longer-term target, we haven't really given detailed long-term targets. What we have told people is, if we continue on the same pace of digital growth as we've seen over the last couple of years, we should be able to generate at least 100 basis points of gross margin expansion each year. Historically, it has exceeded that level. But I think, at a minimum, we should be able to see that.

If you combine that with control around our operating expenses, and continued movement towards more digital marketing, we should be able to see earnings growth. And our target is to try to get to earnings growth at least above 10% or greater, or closer to 15% on a yearly basis, if we can. That's obviously general targets. We'll give you detailed guidance for FY17 at the end of the year. And to the extent we have an update on that, we'll let you know. But we continue to be excited, obviously, about where the business and the potential is.

In terms of FIFA, the guidance for extra content and Ultimate Team, in general -- the guidance for extra content that we originally gave for the full year was around 10% growth of extra content. We've been exceeding that, and we hope that we can continue to hit that target, or beat that target over time. And we're very excited about the continued engagement level that people are showing in all of our sports titles around extra content, as well as the potential for extra content in other places in our portfolio.

As far as FIFA Online 3 goes, in China we had originally given guidance that that should be around \$10 million to \$15 million a quarter. And we're seeing that levels, and we're pretty comfortable that that continues to grow over time.

Chris Merwin - *Barclays Capital - Analyst*

Thank you.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Next question.

Operator

Stephen Ju, Credit Suisse.

Stephen Ju - *Credit Suisse - Analyst*

Blake, you just raised your Star Wars unit guidance. I think you gave the overall revenue phasing guidance in the slide deck. But what is embedded in your guidance for how Star Wars will be phasing between your third and the fourth quarters? And also, secondarily, I think you mentioned 20% digital download. How far behind is the European consumer, in terms of full game download adoption on the console? Are you seeing that uptake curve follow on a similar path as what you've as what you've already seen in the US? Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Yes. Thanks, Stephen. Good questions. I don't have the number off the top of my head. But you should assume that a fairly large portion of the original sell-in comes in the third quarter. And then depending on how that does through the Christmas season, we'll see the rest in the fourth quarter. So, roughly probably 75/25.

In terms of the full game downloads, a couple things to remember: we still sell gen 3 products. And gen 3 products are typically doing full game downloads at a much lower level. And then second, our business, particularly FIFA, is skewed heavily towards Europe. And two factors bring down full game downloads today in Europe: one is bandwidth speeds in some countries; and two is many retailers in Europe, particularly in Great Britain, use FIFA as a way of driving traffic into the store, and they like a physical copy to help do that.

We're seeing very strong full game downloads continue in North America. And as a reminder, the PC business that we have, we see full game downloads there roughly 75%. And so there's still a lot of headroom, we believe, in the full game download opportunity for us, going forward.

Stephen Ju - *Credit Suisse - Analyst*

Thank you.

Operator

Colin Sebastian, Robert W. Baird.

Unidentified Participant

It's actually Ben on for Colin. I just had two questions, more strategically. Could you talk a little bit about your eSports initiatives, and, going forward, whether you might have the rights to from sports leagues to pursue some more formal tournament play?

And then secondly, are there any plans for annual sequels or franchise extensions for Star Wars? Or would the cadence of those look more like Battlefield or Titanfall?

Peter Moore - *Electronic Arts Inc. - COO*

Ben, I'll take the first question -- it's Peter -- regarding EA SPORTS. I want to remind everybody on the call that EA has been doing eSports since -- it's been a fundamental part of the way we've engaged with our consumers for over a decade, beginning with the FIFA Interactive World Cup. We partnered with -- in particular with FIFA -- with all of the individual leagues around the world, with tournaments, and have been doing that for a number of years now.

So from the perspective of our eSports strategy, it's well-formed at an executional level. When we think about partnering with the sports leagues themselves, we have those conversations. And whilst we've got nothing to announce yet, stay tuned, because I think there's a lot of energy around this right now. We're obviously a very important part of that. Our IP has been used by many of the eSports leagues to be able to drive their business. And we fully intend to be part of this, going forward here.

No real announcements yet at a higher level. But please rest assured it's very high on our radar.

Andrew Wilson - *Electronic Arts Inc. - CEO*

This is Andrew. To the second question around Star Wars and annualization, again, what we have talked about is we have a long-term partnership around the Star Wars license. And we expect that we will launch many titles as part of that long-term relationship. In terms of annualizing that in any particular way, we've made no announcements on that. And certainly what we're always looking at, as we think across our portfolio, is where there is an added opportunity for engagement.

What we talked about in the prepared remarks is we still have 6 million people engaging regularly in both Battlefield 4 and Battlefield Hardline. And it's important, as we think about our business not just as a launch business, but as a large service and relationship business, that we factor in when it's appropriate to launch new things.

So, more to come on that in the future; but certainly expect more Star Wars titles from us, but no decision made as to specific timing, as yet.

Unidentified Participant

Thank you. That's helpful.

Operator

Justin Post, Bank of America.

Ryan Gee - *BofA Merrill Lynch - Analyst*

This is Ryan Gee on for Justin. Thanks for taking my questions. The first is about Star Wars. Can you guys talk a little bit about the gross margin structure, what you can for Star Wars, relative to owned IP like Battlefield, or even licensed products like FIFA or Madden? And going back to the digital downloads, you are averaging around 20% for this quarter. Is there any reason to expect that Star Wars could be higher or lower than that number?

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Sorry, Ryan. Go ahead.

Ryan Gee - *BofA Merrill Lynch - Analyst*

No, go ahead. I'll follow up on FIFA in a second.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Okay. So on the gross margin structure, I think we've told people that the license with Disney is a fairly typical royalty license, and that most of our royalty licenses are in the high-single-digits or low-double-digits, so -- and assume that the Disney license is there. What we try to do is offset some of that cost by lowering our marketing expense. And, clearly, leveraging the strength of all the activities out there around Star Wars is allowing us to do that. And you'll see a lot of joint marketing between us and Disney, as well as us and Sony, to try to leverage our partners to be able to offset some of that.

It will impact gross margin slightly, as you've seen in our guidance for the quarter, but we don't see it as a big issue for the overall profitability of the Company.



On the full game download side, the one caveat I would add there is, normally it shouldn't really differ dramatically from any other title, with the one exception is it could be a title that's a heavy gifting title in the quarter, just because Star Wars is at top of the list of many kids and teens out there, what they want for Christmas.

And gifting titles tend to be more physical, versus a code, and so you might tend to see that. That could be, though, counterbalanced by the fact that we'll see another 10 million to 15 million new consoles sold in the next two months, in the Christmas time. And many of those people may choose to download digitally, particularly if they are the larger storage consoles.

And what was your second part of your question?

Ryan Gee - *BofA Merrill Lynch - Analyst*

Yes, great. That was great feedback. The second is on FIFA, and really the sports catalog. It's encouraging to see the 30% player growth. Is there any reason to expect Ultimate Team to not also be up 30%? Is there anything you can call out, either this year or last year, that would make that be up or down? Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

We were cautious at the tail end of last year, because we had some issues with coin farmers. We have adjusted the new FIFA Ultimate Team to try to prevent those issues. That's a constant battle. That would be our only caution, going forward. So far, we haven't seen any impact from that. What we are seeing is increased interest in Ultimate Team. We put in both FIFA and Madden this year, a draft mode, which was essentially a way to help people understand how Ultimate Team works, and how drafting and building a team works.

And we're finding that that increases the engagement, increases the interest in entering into Ultimate Team. And so, our hope is to continue to try to build that business across all of our sports franchises. And so far, things are going very well.

Ryan Gee - *BofA Merrill Lynch - Analyst*

Okay, great. Thank you, guys.

Operator

Brian Pitz, Jefferies.

Brian Pitz - *Jefferies LLC - Analyst*

Of the 9.5 million beta players on Star Wars, what is the overlap audience with the 6 million still playing Battlefield 4 and Hardline? Is Star Wars essentially bringing new gamers into the Battlefield type of game? And also, any updates on preorders, including the \$50 DLC Season Pass? Love to hear how the DLC attach rates compare to prior Battlefield releases. Thanks.

Andrew Wilson - *Electronic Arts Inc. - CEO*

I'll take the first part on the 9.5 million. I don't have that data on hand. Anecdotally, what we have seen is that Star Wars is bringing in two groups that are very important groups to us. One are gamers that have lapsed; traditionally who have been big gamers in the past, and maybe haven't played for a while. And that's certainly been a catalyst for those people to come back into the gaming universe, as it relates to console. And two, onboarding a new, younger age demographic.

And so, as we think about that 9.5 million, while there is absolutely a crossover around our core shooter category that we have very good and strong relationships with, we are very energized by the opportunity to bring in, one, that lapsed gamer group; as well as adding a new, younger demographic going forward. And remember, that this is a title, as a shooter title, that will be more appropriate for younger players than maybe some other shooter titles in the market.

Peter Moore - *Electronic Arts Inc. - COO*

Yes, on preorders, I think when you look back -- and you've heard from both Blake and Andrew how powerful this beta was for us, and that has certainly spurred tremendous preorder growth. Every week, subsequent to the beta, we had 9.5 million users who logged in 1.6 billion minutes of gameplay. On top of that, we were very fortunate, obviously, that The Force Awakens movie trailer came right on top of that. And that's allowed us to be able to generate even more publicity for the game, as people start to anticipate the movie in mid-December.

You combine that with all the engagement that our players have creating content themselves: a lot of user-generated content, with millions of hours now of gameplay coming out of the beta on YouTube and Twitch. Now, if Han Solo was here, we'd say great, but don't get cocky, kid. Our ability to be able to deliver against this is solid. And the preorders are excellent. So you've heard from both Blake and Andrew. We feel very good about 13 million units.

Andrew Wilson - *Electronic Arts Inc. - CEO*

Was there another question?

Peter Moore - *Electronic Arts Inc. - COO*

Battlefront Season Pass. As we've seen with Battlefield, with Battlefield Premium, our ability to extend, and as you've seen with 6 million people still engaged with both Battlefield 4 and Battlefield Premium, is key. The engagement numbers -- and we see a Season Pass as integral to that. What we've announced is four the extra packs over the next 12 to 18 months, coming post-launch.

And from our ability to view that -- be very clear that's FY17 revenue for most of it. You'll see both new universes. You're going to see new player actions; obviously new weaponry, as well. We think there's added engagement. And we think the ability for us to be able to deliver against what we need to be able to do, from a Season Pass, increases the engagement, and a very important part of keeping the content fresh and our players engaged.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Next question.

Operator

Arvind Bhatia, Sterne Agee CRT.

Arvind Bhatia - *Sterne Agee CRT - Analyst*

I'd like to congratulate you guys on another great quarter. I wanted to ask a couple questions. One is, Blake, if you could maybe talk a little bit more about the \$30 million revenue benefit, maybe some clarification there. And I think I heard you say it was already part of the guidance.

And then, Andrew, just your thoughts on virtual reality. Any update there, now that we have a little bit more clarity in the marketplace?



And then last one, can you maybe talk about Need for Speed, how the beta -- what was the size of the beta, and the unit expectations versus the last one? Thank you.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Arvind, first on the \$30 million -- when we planned our guidance, essentially we sell special editions of some of the sports games -- FIFA and Madden, for example. And part of those special editions include Ultimate Team currency. And we decide how to defer that over time, in conjunction with our internal accounting team and our external auditors. As we got into the quarter, we determined that some of the content we thought we would defer, we actually didn't defer. We were able to book it in this quarter.

And we wanted to be transparent on that so people, one, understood one of the sources of our overdelivery; and, two, understood that that was just shifting between two quarters.

Andrew Wilson - *Electronic Arts Inc. - CEO*

Thanks, Arvind. On VR, our position hasn't changed at this juncture. Again, what we have said in the past is that -- and I personally am very bullish on VR, and believe it will be an integral part of our industry and our business on a go-forward basis. As we think about what players are trying to do, which is immerse themselves inside of these wonderful worlds and experiences that we create, and that it overcomes the social disconnect created by sitting 10 feet or 3 feet or 1 foot from a screen.

With that said, we don't expect it will have a material revenue impact in the near future. We still think there is work to be done to get to a point where this is really a mass-market consumer proposition that delivers great VR, immersive experiences for a mass community. But at the same time, we are investing heavily in ensuring our Frostbite engine has all of the capability to deliver spectacular VR experiences. So we are well positioned as this market develops.

Peter Moore - *Electronic Arts Inc. - COO*

And Arvind, this is Peter. On the Need for Speed beta, very successful for us. As I think most of you on the call know, Need for Speed now is available to play if you are an EA Access member, as of today. The team, as it always does with a beta, used the beta results to tweak and do some last-minute polishing to the game. Every indication -- and preorders are very strong around the world -- every indication this will be yet another successful launch, having been two years away from consumers, as we see the numbers coming in in the final few days here for next week. So, Need for Speed goes live next Tuesday in the United States and Canada, and at the end of the week in the rest of the world.

Arvind Bhatia - *Sterne Agee CRT - Analyst*

Great. Thank you, and good luck.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Next question?

Operator

Drew Crum, Stifel.

Drew Crum - *Stifel Nicolaus - Analyst*

Can you remind us what the incremental FX hit is for fiscal 2016 now, and what the revenue foregone is from the shift of Mirror's Edge?

Blake Jorgensen - *Electronic Arts Inc. - CFO*

So roughly, Mirror's Edge, you should think about it as a \$70-ish million title for that quarter; so moving out of the fourth quarter. And our original FX guidance was that roughly \$250 million -- or \$290 million was -- originally it was \$250 million. And we think it's probably closer to \$300 million now.

Drew Crum - *Stifel Nicolaus - Analyst*

Okay, good. And then any launch metrics, aside from the mobile performance for Madden, that you can offer? And any commentary around full game download performance with that franchise? Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

In terms of the Madden franchise, you mean?

Drew Crum - *Stifel Nicolaus - Analyst*

Yes, Madden and NFL 16.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

It's been pretty consistent. Obviously, it's a dominant North America title relative to FIFA. And so we tend to see higher full game downloads on Madden than we have with FIFA globally, for the fact that I mentioned earlier. And so you are seeing north of 20% on Madden, obviously. And as the season goes on, we find that the initial purchasers tend to be the people who line up at the retail stores at midnight with their football jerseys on. Obviously that skews the early days of Madden. But by mid-season, we tend to see levels creeping up closer to 40%, at least based on last year's data. We don't know yet this year, but strong focus on that.

And the strength of Ultimate Team with Madden has been -- it was very powerful last year. I think that draws more and more people into digital purchases, as part of that ongoing gameplay.

Drew Crum - *Stifel Nicolaus - Analyst*

Okay. Thanks, guys.

Operator

Ben Schachter, Macquarie.

Ben Schachter - *Macquarie Research - Analyst*

A couple of housekeeping questions, and then a couple of broader questions. Blake, just to be clear, the 13 million unit Star Wars forecast -- is that for 3Q, FY16, or lifetime?

Blake Jorgensen - *Electronic Arts Inc. - CFO*

For full-year 2016, fiscal 2016.

Ben Schachter - *Macquarie Research - Analyst*

Okay. And then (multiple speakers).

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Stephen had asked earlier if I -- what I thought the split is. I said 75%; it's probably closer to 80% in Q3 versus Q4. I just looked up the numbers.

Ben Schachter - *Macquarie Research - Analyst*

Okay. And then if you could just help us maybe translate that 30% player growth into unit growth for FIFA and Madden? And then I have a couple of broader follow-ups after that.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

I wish I could translate it. But we don't think about it that way, because we think about it around engagements. Clearly, it will show unit growth. But the 30% really is a measure of not just people buying the initial game, but playing the game, so it's hard to put -- those are apples and oranges in that respect. But you should take that as continued unit growth in FIFA, which we are seeing.

Ben Schachter - *Macquarie Research - Analyst*

Okay. And then, as you know, given the strength this year, there are already concerns about comping revenue growth next year. I don't want to get too far ahead of ourselves in the guidance. But how should we think about the types of games, or the games that are going to come next year, that will help comp against Star Wars?

And then following up on Arvind's VR question, I have to keep asking these. But is EA going to wait until there is a mass-market installed base? Or could we see at least limited VR experiences during the launch window for some of the 2016 VR hardware launches? Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

I'll let Andrew touch on the VR one, if he'd like, but I'll touch on the other question. I think we try to resist giving full-year guidance ahead of time. We have mentioned in the past, on our past calls, that you should expect another Battlefield title coming next year. We've shown Mass Effect at E3 this year. You should expect that again. And there's some indication there will be some other titles, obviously, that are popular along those lines, like Titanfall or others.

But we are very confident we can continue to grow the business. And we also are confident that the Star Wars franchise will live, well beyond this year. And we think, like Battlefield, you'll get a long tail on Star Wars into -- or helping drive our FY17 business.

Andrew Wilson - *Electronic Arts Inc. - CEO*

On VR, what we talked about in our prepared remarks is our great strengths -- creativity, passion. And one of those things is pioneering and our desire as a Company to lead; and our belief that we have a responsibility, given our position in the industry, to lead. Part of why we are investing at an engine level is so that we can drive from a leadership position.

While we don't have anything to announce today, certainly for next year we are looking at opportunities to do things sooner and earlier than complete mass-market adoption. But again, we will be getting to a point -- it's less about is there mass-market adoption? More about, is the technology ready for mass-market adoption? And that's what we're working through right now. But we absolutely have a desire to lead, as is our responsibility for the position we have in the industry.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Next question.

Operator

Mike Hickey, Benchmark.

Mike Hickey - *The Benchmark Company - Analyst*

I also want to extend a congrats on another great quarter. I guess as much as you can, I'm sort of curious your view on Vivendi's recent investment in Ubisoft -- if you feel that perhaps there could be other potential acquisitions in the industry. And if you could update us on your current thinking around M&A and strategic partnership strategy, that would be great. And I have a follow-up.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Yes, we can't comment on Vivendi, because we just don't know. You probably know more than we do, so I'll just resist on any comment there. In terms of our acquisition strategy, nothing has really changed. We look at a lot of opportunities. But we are very excited about the opportunities we have internally, both our own IP -- we've got quite a few things cooking, as you've seen. We've hired Jade Raymond from Ubisoft to help us build some new products; Amy Hennig, as well.

So there's a huge opportunity for us to continue to build our own IP, as well as a leverage our great partnerships with people like Disney and Lucas to build off of Star Wars, or any of our other licensed IP. And so, we see very little need right now. But we keep our eyes open, and we're always interested in seeing how things are evolving out there.

Mike Hickey - *The Benchmark Company - Analyst*

Cool. Fair enough, thank you. And thinking about Nintendo's NX platform, the dev chips have apparently shipped. It looks like it's working towards a calendar year 2016 launch. Just wondering how you plan to manage your resources to that emerging platform. Do you anticipate being more aggressive on the front end? Or perhaps a little bit more cautious, given the Wii U underperformed expectations?

Andrew Wilson - *Electronic Arts Inc. - CEO*

I'm going to address that slightly differently. As we look to the future, we see a world where more people are playing on more platforms in more geographies than ever before. We see the platform cycle now, not just as a traditional six-year console cycle, but as a six-month refresh rate on mobile devices, smart TVs, Internet-enabled refrigerators, or whatever it might be.

And what we're doing, in terms of resource allocation, is really investing at a core digital platform level, at an engine level, and at a game architecture level, to ensure that we are able to deliver amazing experiences; 6 inches to 60 inches, and beyond; two minutes to two hour session times, and beyond; across any and all relevant devices where gamers are playing.

And as it relates to Nintendo, we've had a tremendous relationship with them over the years. And we will evaluate any and all opportunities with them, in the same way we do all platform opportunities.

Mike Hickey - *The Benchmark Company - Analyst*

All right, guys. Thanks.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Thanks, Mike. Next question?

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Operator, do we have more questions?

Operator

Neil Doshi, Mizuho.

Neil Doshi - *Mizuho Securities - Analyst*

Can you guys talk a little bit about micro-transactions, and how you guys think about micro-transactions for some of your larger games down the road, including Star Wars, Battlefield, and Need for Speed, as well?

And then, Blake, I think marketing spend was a little bit lighter than we were looking for in the quarter. Any more color in terms of -- whether you're finding better ROI in terms of marketing channels, or whether you had to just defer some marketing spend? Thanks.

Andrew Wilson - *Electronic Arts Inc. - CEO*

I'll take the first part of that question. As it relates to any and all of our products, what our players are telling us -- particularly as they engage online with their friends -- is that they want to play our games longer, and more frequently, and for more hours at a time, than ever before. And our objective any time we provide additional content, in any form, whether free or paid, is to ensure that in all cases we provide value for the investment of any money and the investment of their time; and that, in all things, we are extending and enhancing the experience, so they can continue to enjoy playing the games we make with their friends for many months and years to come.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

And on marketing expense, it's hard to look at any one quarter and see a major trend, because of how titles fall. And we may have marketing expenses in -- two quarters ahead of the title, or getting spread over multiple quarters. But our general view is we've been working very closely with all of the people involved in marketing to really leverage the engagement we have with our consumer base. We're connected to all of our consumers. We have a unique opportunity to better target our marketing activity to those consumers, and not needing to use some of the lesser -- or the more traditional marketing vehicles that have less effectiveness.

Now, you're going to see a lot more out of us in the future. You'll hear more. You'll see things related to Star Wars, for example, over the next couple of weeks, which really help people better understand the product, and help target market to specific cohorts. And it's just the way we're shifting marketing. The team has done an amazing job really re-dialing how we approach marketing, led by our new CMO, Chris Bruzzo. And we're going to see more of this. And we hope that it will help us continue to manage our marketing expense over time.

Neil Doshi - *Mizuho Securities - Analyst*

Great. Thank you.

Chris Evenden - *Electronic Arts Inc. - VP of IR*

Next question please, operator.

Operator

Eric Handler, MKM Partners.

Eric Handler - *MKM Partners - Analyst*

So, I'll ask another Star Wars question. When you look at the film, international revenues could potentially double what we're seeing here in North America. I wonder if there's any correlation in how you are thinking about sales for the game, on a North American basis, versus international basis.

And then secondly, just one housekeeping issue with -- you gave a couple reasons why guidance didn't move higher -- including FX, Mirror's Edge. With the dilution from the convert because of the warrants that are there, is that another thing we need to consider for reasons why guidance didn't move higher?

Blake Jorgensen - *Electronic Arts Inc. - CFO*

I'll let Peter address the Star Wars question, and I'll talk on the dilution question.

Peter Moore - *Electronic Arts Inc. - COO*

Yes, I think from the perspective, Eric, we look at the anticipation of what is arguably the biggest piece of intellectual property in the world, that has not seen a movie in many, many years. As I think you know, the anticipation -- whether it's North America, whether it's Europe, whether it's Asia -- is off the charts. I don't think it correlates necessarily to how we think about it. This is a global title. I've been traveling the world recently, and checking in on all of our retail and digital channels on a global basis, and we're fired up and ready to go.

The movie feels like one of the true global launches. When you start to speak with consumers around the world, the anticipation levels are high. I don't think there is a direct correlation to how we would phase our revenue from region to region. It's going to be big and bigger.

Blake Jorgensen - *Electronic Arts Inc. - CFO*

Yes, and in terms of the dilution issue, I'd just remind everyone that the current shares that are being redeemed -- we're issuing shares that are counterbalanced by the shares in the hedge transaction that we set up. So, until the actual bond is redeemed fully next summer, the clock then starts to tick on the potential future dilution around those shares. And so the dilution will be approximately 90 days after the bond is fully redeemed; thus, no dilution this year.



We have updated our table on our IR website to reflect that. The future dilution could occur late next year. And we'll be back to you with some of our ideas around how we're going to manage that.

Eric Handler - MKM Partners - Analyst

Great. Thank you very much.

Operator

Doug Creutz, Cowen and Company.

Doug Creutz - Cowen and Company - Analyst

Yes, you guys were, I think, close to flat year-over-year on your physical console revenue. According to NPD, and I think [some of the data] in the UK, you were down double-digits in sellthrough. Obviously had FX headwinds elsewhere. Can you help to square that circle? Is this case of your retailers taking more inventory?

Hello?

Operator

Excuse me, sir. Hello?

One moment, participants.

(technical difficulty)

Participants, thank you all; and the call is already over. You may now disconnect. Once again, at this time, the call is over. You may now disconnect.

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