

ELECTRONIC ARTS
Q2 FY14 PREPARED COMMENTS
October 29, 2013

ROB:

Thank you.

Welcome to EA's fiscal 2014 second quarter earnings call. With me on the call today are Andrew Wilson, our CEO, and Blake Jorgensen, our CFO. Peter Moore, our COO, and Patrick Söderlund, our EVP of EA Studios, 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 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 October 29, 2013 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'll turn the call over to Andrew.

ANDREW:

Thanks Rob.

I'm happy to be here today, and pleased to join my first earnings call as CEO of Electronic Arts with positive news to report.

Before I get into our results and a few other thoughts, let's take a moment to recognize the launch of *Battlefield 4* in North America today, the culmination of efforts by the incredible teams at our DICE studios. Patrick Söderlund and his team have done a spectacular job to deliver a game that not only represents the pinnacle of this console generation, but one that is also a defining title for the next-gen consoles launching in November. We're also launching *Battlefield 4 Premium* across current-gen and next-gen consoles to extend and enhance the experience, making this the biggest *Battlefield* ever. Congratulations to the team – we're proud to add *Battlefield 4* to the list of hit titles including *Madden NFL 25*, *FIFA 14* and others that we've delivered to gamers this past quarter.

As we get started here today, I'll cover a few things:

- A quick topline of our Q2 performance and key drivers,
- The opportunity in front of us and how we're positioning EA to deliver great games and services,
- And a quick look at EA's goals for the rest of FY14 and beyond.

Turning first to our quarterly results, EA delivered Q2 revenue and earnings above our guidance. Digital revenue, cost controls and delivering against our product plan all contributed to a very strong quarter. However, much of our work for this year remains ahead of us, as we prepare to launch our titles for the next-gen consoles this holiday.

Digital revenue remains a major driver in our overall performance as we deliver games and live services for our core brands across multiple platforms. We are tracking to meet or exceed our goal of generating more than 40% of our total non-GAAP FY14 revenue from our digital businesses.

From a product perspective, we delivered successful on-time launches in the second quarter for our major console titles from EA SPORTS, including *NCAA Football 14*, *Madden NFL 25*, *NHL*

14, and FIFA 14. Madden NFL 25 and FIFA 14 also launched on iOS and Android this quarter, and of course the much-anticipated *Plants vs. Zombies 2* landed on iOS in August. In line with our previous guidance, our current-gen EA SPORTS titles have seen some initial softness in sell through – a trend we expected moving into a console transition. However, this is tempered by the unique opportunity we have with versions of *Madden NFL 25*, *FIFA 14*, *Battlefield 4*, *Need for Speed Rivals* and *NBA LIVE 14* all launching on Xbox One and PlayStation 4 in November.

Cost control measures delivered better-than-expected results in Q2, coming in \$51 million ahead of our guidance. Our operating margin expansion effort is a great indicator of our increased financial discipline and focus on growing EA's bottom line. We are confident that we can continue to move faster and further than we already have on a go-forward basis.

With these factors driving our current outlook, we are raising full-year guidance today.

Looking ahead, EA is in a strong position as we move into a momentous season for our company and the gaming industry at large.

As our studio teams put the finishing touches on a powerful line-up of titles for Xbox One and PlayStation 4, we continue to be encouraged by the market reception and growing consumer excitement. The latest indicators from Microsoft and Sony, along with preorder data, show strong demand for the new consoles. Both Sony and Microsoft have also committed that they will continue to fully support the existing PlayStation 3 and Xbox 360 platforms.

Meanwhile, our industry is far more dynamic and diverse moving into this console transition than ever before. The global player base for mobile games is expanding, and we're also seeing strong performance in PC-based free-to-play games around the world.

Our strategy is directly aligned to each of these key growth opportunities – next-gen consoles, mobile and free-to-play PC. EA's blueprint for success is visible with fan-favorite brands such as *FIFA*, where we offer experiences tailored for each of these environments:

- *FIFA 14* for consoles, including Xbox One and PlayStation 4;
- *FIFA 14* for iOS and Android mobile devices;
- And free-to-play online experiences for PC such as *FIFA Online 3* in Korea.

Tens of millions of fans are engaging with our games every day. These titles are live services, with connected features and new content keeping the experience fresh for players long after launch.

Recent changes that we've made to EA's structure will help us more aggressively capture these opportunities. Key studio leaders Patrick Söderlund and Lucy Bradshaw have been elevated to lead our development efforts across next-gen consoles and PC. Frank Gibeau is leading a consolidation and double-down of our mobile efforts. COO Peter Moore continues to lead and transform our operational and publishing teams that bring our games to market, and Rajat Taneja, our CTO, continues to lead development of our world-class technology platforms. While not dramatic changes, these refinements will help us better leverage our IP and integrate successful development practices across our portfolio.

In a moment, I'll hand over to Blake to walk through the specifics of our financial results, but as this is my first quarterly call as CEO, I also wanted to take a moment to speak about three elemental beliefs that I have for EA moving forward.

First, delivering amazing games and services for gamers must be at the core of everything we do – the central strand of our DNA that defines who we are and the experiences we work to create. Our reputation as a company is built on our ability to develop strong relationships with players through the games we make, and we are committed to strengthening that bond.

Second, EA's biggest strengths are our people and our strategy. Our deeply-talented developers and business leaders are the lifeblood of EA, enabling us to bring powerful IP like *Madden*, *FIFA*, *Battlefield*, *The Sims*, *Star Wars* and more to gamers around the globe. Combined with our strategy to take these titles across different platforms, geographies and ways to play, EA has a foundation for decades of healthy growth.

Third, making games profitably is vital to EA's future. Simply put, we owe great games to our players and strong returns to our shareholders.

Each of these beliefs is borne out of my experience as a passionate long-time employee of this company, having had the benefit of working in multiple parts of our business across different

continents. These are the defining characteristics of a new era at EA, one that I'm incredibly excited to lead for our gamers, for our teams and for our shareholders.

With that, I'll turn the call over to Blake Jorgensen.

BLAKE:

Thanks, Andrew.

Turning to our Q2 results, EA's non-GAAP net revenue was \$1.04 billion, which was above our guidance and 4% lower than last year. The quarter's revenue was driven by our sports titles and continued strength in our catalog offerings, like *FIFA 13*, *SimCity*, *Star Wars: The Old Republic* and *Battlefield 3*. In line with our guidance, all of our sports titles except for *FIFA 14*, sold in less than the prior year. Lastly, positive foreign currency gains of \$9 million also added to the revenue upside.

Q2 non-GAAP digital net revenue also contributed to the solid quarterly performance. Digital net revenue increased by 11% year-over-year to \$348 million. Our digital business continues to be a diversified mix of high growth, profitable segments. The trailing twelve-month digital net revenue was up 22% over the prior year to a record \$1.75 billion. Breaking down our digital revenue into its key components highlights the performance of each business:

- First, extra content and free-to-play contributed \$127 million, up 11% over the prior year, led by continued growth in *FIFA Ultimate Team*, *FIFA Online 3*, and *Star Wars: The Old Republic*. This revenue relates to businesses on PCs or consoles, where consumers can enhance or extend their gaming experience by buying additional digital content. One exciting trend to note, our year-to-date results for each of our sport's Ultimate Team businesses – *Hockey Ultimate Team*, *NCAA Football Ultimate Team*, *Madden Ultimate Team* and of course *FIFA Ultimate Team* – demonstrated revenue growth year-over-year. However, our decision to sunset several of our social businesses offset some of this growth, as we saw revenue declines from *The Sims Social* and *SimCity Social*.
- Second, our mobile business generated \$105 million for the quarter, up 19% over the prior year. Smartphones and tablets continue to represent a majority of the revenue, accounting for \$87 million of the \$105 million total, and growing 34% year-over-year. *The Simpsons:*

Tapped Out, *The Sims FreePlay* and *Real Racing 3* continue to be key revenue generators, and the launch of *Plants vs. Zombies 2* also contributed to our mobile revenue.

Mobile growth was dampened by a \$15 million decline in our Japanese *FIFA World Class Soccer* business. This product was developed and hosted on social mobile platforms, and Japanese gamers have migrated to apps built natively for the iOS and Android platforms. Going forward we are developing and will roll out games built for the iOS and Android platforms in Japan and other key regions.

- Third, full game downloads represented \$54 million, up 42% over the prior year. This revenue is driven by PC-centric products. Strong demand for *SimCity*, as well as the deferral of Q1 *SimCity* revenue into Q2, were the drivers for the significant increase.
- And fourth, subscriptions, advertising, and other digital revenue contributed \$62 million, down 16% over the same period last year. In the previous year, *Star Wars: The Old Republic* was a subscription-only based MMO. This year, some of the revenue was recognized in the free-to-play category as we expanded this title to be both a subscription and free-to-play game.

Moving on to gross margin: our non-GAAP gross margin for the quarter was 61.7%, up over last year's 60.1%, and slightly better than our guidance. The improvement was due to our growth in digital, lower processing fees as we move away from the social business, and the benefits from our new digital platform.

Operating Expenses for the quarter were \$499 million, down \$82 million from last year, and \$51 million lower than our guidance. Lower operating expenses this quarter illustrates that our cost control programs are taking hold. However, we believe all of this benefit should not be factored into the full year results.

There continues to be risks associated with the transition to next-gen consoles. These risks could impact sales and marketing, and R&D expenses. In addition, some of the positive variances are due to the phasing of marketing expenses into the holiday quarter.

As we continue to manage expenses and headcount, we are progressing towards our goal of flat-to-down operating expenses, something we have not previously accomplished in a console transition year. Achieving this goal will help our efforts to deliver operating margins above 20%.

The resulting non-GAAP EPS was \$0.33 per share. EPS exceeded our guidance of \$0.12 per share due to lower operating expenses, stronger revenues and slightly higher gross profit margins.

Our cash and short-term investments at the end of the quarter were \$1.42 billion, or approximately \$4.60 per share. Roughly 60% of this cash and short-term investment balance is held outside of the U.S. Also, as seen in our GAAP to non-GAAP reconciliation, this quarter we recognized a \$40 million GAAP-only charge for an expected litigation settlement and license expenses related to our college football business.

Net cash used in operating activities for the quarter was \$6 million. On a trailing twelve month basis, operating cash flow was \$342 million.

During the quarter, we did not repurchase any shares. We remain committed to our program, which as a reminder, is a \$500 million share repurchase program initiated a year ago. At this point, the total shares repurchased under this program remain at 22 million, at a total cost of \$278 million.

Now turning to guidance:

Last week we announced that *Titanfall* will launch in this current fiscal year while *The Sims 4* will be released next year. We do not expect this change to have a material impact on our previous non-GAAP guidance as the launch date and the Q4 forecast for *Titanfall* is broadly similar to that of *The Sims 4*. Non-GAAP revenue and gross margin guidance remain at \$4.0 billion and 66%, respectively. However, due to the favorable results of our cost control efforts, we are now estimating operating expenses to be reduced to approximately \$2.10 billion, and we are raising our EPS guidance to \$1.25.

The GAAP guidance is estimated to be \$3.55 billion in revenue, and a loss per share of (\$0.72).

As we have pointed out in past quarters, our consumers are playing our games online over longer periods of time, and this longer period affects the length of time over which we are required to recognize GAAP revenue. This fiscal year, we are lengthening this recognition period, resulting in an estimated \$450 million of net revenue being deferred into fiscal 2015. This longer service period has no impact on our non-GAAP revenue or cash flows.

With respect to Q3 guidance:

GAAP revenue is expected to be \$775 million, as compared to \$922 million in the prior year.

GAAP loss per share is expected to be (\$1.42), as compared to (\$0.15) per share in the prior year. Again, this is primarily due to the longer revenue recognition period.

Non-GAAP revenue for the quarter is expected to be \$1.65 billion, a 40% increase over last year's \$1.18 billion. Our fiscal third quarter is expected to account for more than 40% of our full year revenue. This quarter we are launching major titles for current and next gen consoles.

Our Q3 non-GAAP revenue guidance is being impacted by certain upgrade programs we have rolled out in connection with the console transition. We are required to defer revenue associated with our current-gen marketing programs that allow consumers to buy a next-gen game at a discount. As a result, we believe that there will be some deferral of revenue until Q4 as some gamers delay taking advantage of this upgrade program.

Our Non-GAAP gross margin is forecasted to be approximately 68%, better than prior year due to our digital growth and revenue mix.

Operating expenses will be impacted by the phasing of some expenses from our previous quarters. We expect our total non-GAAP operating expense to be \$600 million.

This results in a non-GAAP diluted EPS of \$1.22 per share, as compared to \$0.57 last year.

Regarding Cash Flow: We are maintaining our estimates for fiscal 14 operating cash flow and capital expenditures of at least \$400 million and \$100 million, respectively. This implies expected free cash flow generation of over \$300 million dollars, or approximately 1.4 times what we generated in fiscal 13. While the higher EPS guidance should generate more cash flow, the

\$40 million GAAP-only charge related to our college football business that I mentioned earlier will likely offset this benefit, causing us to maintain our previous projections.

In summary: We recognize that the first half results were ahead of our guidance, but as I noted earlier, the upside is driven mainly by our cost control programs taking hold and phasing some operating expenses to the second half of the year.

Q3 represents more than 40% of our total non-GAAP revenue and 98% of our annual EPS. Similar to the World Series, where the remaining game or two will determine the season for Peter's beloved Boston Red Sox, the next few months will determine the success of our fiscal year. Our team is battle tested and ready, and today we are sending our ace, *Battlefield 4*, to the mound.

Now, with that I'll turn the call back to Andrew.

ANDREW:

Thanks, Blake.

Q2 was an exceptional quarter for EA, with digital growth, improved cost management and a slate of successful titles giving us strong momentum moving into the second half of the year.

Our attention is now looking forward to our next-gen launches, ramping up our mobile efforts and positioning our long-term IP development to deliver amazing new experiences to our gamers, wherever they want to play.

When the next-gen consoles begin to ship next month, EA will deliver an unprecedented line-up in the launch window. *Battlefield 4*, *Madden NFL 25* and *FIFA 14* will be available Day One for both PlayStation 4 and Xbox One. *NBA Live 14* and *Need for Speed Rivals* then join our next-gen roster just a few days later. In March, we'll launch *Titanfall*, a thrilling new first-person action experience from our partners at Respawn Entertainment.

In mobile, games like *Plants vs. Zombies 2*, *FIFA 14*, *The Simpsons: Tapped Out* and *Real Racing 3* are showing how major brands can break through the cluttered ranks to continually

engage players on smartphones and tablets. We will lean heavily into our key brands as we double down on mobile development to accelerate our growth in this vital segment.

In the last two weeks, you've also seen several announcements about our product slate for the remainder of this year and into FY15. We are refining our focus on our biggest brands and great new IP in development, including *The Sims 4*, *EA SPORTS UFC*, *FIFA World Cup* and *Dragon Age Inquisition*. Looking further out, we have a strong pipeline of new IP taking shape, including *Star Wars Battlefront*.

At our core, we're resolved to continue strengthening EA's relationship with the hundreds of millions of gamers that play our games around the world. Every day we hear from our gamers about what they'd like to see next from EA. This feedback is incredibly valuable, and shapes our decisions about the games we make.

Providing great experiences for our gamers, supporting our talent and executing on our strategy, as well as delivering profitable growth – these are the fundamental beliefs that define EA today. Combined, they drive us to deliver every day on commitments to our most important stakeholders:

A commitment to support our talented teams as they create the absolute best games and services.

A commitment to do the work needed to be known, loved and respected by gamers for the games that we create.

And a commitment to deliver profitable growth and continually improve returns to shareholders.

I look forward to sharing our successes with all of you in the years to come.

With that, Blake, Peter, Patrick and I will take your questions.

Non-GAAP Financial Measures

To supplement the Company's unaudited condensed consolidated financial statements presented in accordance with GAAP, Electronic Arts uses certain non-GAAP measures of financial performance. The presentation of these non-GAAP financial measures is not intended to be considered in isolation from, as a substitute for, or superior to, the financial information prepared and presented in accordance with GAAP, and may be different from non-GAAP financial measures used by other companies. In addition, these non-GAAP measures have limitations in that they do not reflect all of the amounts associated with the Company's results of operations as determined in accordance with GAAP. The non-GAAP financial measures used by Electronic Arts include: non-GAAP net revenue, non-GAAP gross profit, non-GAAP operating income (loss), non-GAAP net income (loss) and historical and estimated non-GAAP diluted earnings (loss) per share. These non-GAAP financial measures exclude the following items, as applicable in a given reporting period, from the Company's unaudited condensed consolidated statements of operations:

- Acquisition-related expenses
- Amortization of debt discount
- Certain non-recurring litigation expenses
- Change in deferred net revenue (online-enabled games)
- College football settlement expenses
- Loss (gain) on strategic investments
- Restructuring charges
- Stock-based compensation
- Income tax adjustments

Electronic Arts may consider whether other significant non-recurring items that arise in the future should also be excluded in calculating the non-GAAP financial measures it uses.

Electronic Arts believes that these non-GAAP financial measures, when taken together with the corresponding GAAP financial measures, provide meaningful supplemental information regarding the Company's performance by excluding certain items that may not be indicative of the Company's core business, operating results or future outlook. Electronic Arts' management uses, and believes that investors benefit from referring to, these non-GAAP financial measures in assessing the Company's operating results both as a consolidated entity and at the business unit level, as well as when planning, forecasting and analyzing future periods. These non-GAAP financial measures also facilitate comparisons of the Company's performance to prior periods.

In its earnings press release dated October 29, 2013, Electronic Arts has provided a reconciliation of the most comparable GAAP financial measures to the non-GAAP measures.

Forward-Looking Statements

Some statements set forth in this document, including the information relating to EA's fiscal 2014 guidance information and title slate contain forward-looking statements that are subject to change. Statements including words such as "anticipate", "believe", "estimate" or "expect" and statements in the future tense are forward looking statements. These forward-looking statements are preliminary estimates and expectations based on current information and are subject to business and economic risks and uncertainties that could cause actual events or actual future results to differ materially from the expectations set forth in the forward-looking statements.

Some of the factors which could cause the Company's results to differ materially from its expectations include the following: sales of the Company's titles; the Company's ability to manage expenses; the competition in the interactive entertainment industry; the effectiveness of the Company's sales and marketing programs; timely development and release of Electronic Arts' products; the Company's ability to realize the anticipated benefits of acquisitions; the consumer demand for, and the availability of an adequate supply of console hardware units; the Company's ability to predict consumer preferences among competing platforms; the Company's ability to service and support digital product offerings, including managing online security; general economic conditions; and other factors described in the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2013.

These forward-looking statements are current as of October 29, 2013. Electronic Arts assumes no obligation and does not intend to update these forward-looking statements. In addition, the preliminary financial results set forth in this release are estimates based on information currently available to Electronic Arts.

While Electronic Arts believes these estimates are meaningful, they could differ from the actual amounts that Electronic Arts ultimately reports in its Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2013. Electronic Arts assumes no obligation and does not intend to update these estimates prior to filing its Form 10-Q for the fiscal quarter ended September 30, 2013.