

ELECTRONIC ARTS
Q2 FY17 PREPARED COMMENTS
November 1, 2016

CHRIS:

Thank you.

Welcome to EA's second quarter fiscal 2017 earnings call. With me on the call today are Andrew Wilson, our CEO, and Blake Jorgensen, our CFO.

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, our financial model, and a transcript.

We have a few events coming up: Blake will be speaking at the UBS Conference in San Francisco on Tuesday, November 15; Peter Moore will be speaking at the Credit Suisse Conference in Phoenix on Tuesday, November 29; Blake will be at the NASDAQ conference in London on Wednesday, November 30 and back in San Francisco at the Barclays conference on Wednesday, December 7. Finally, our Q3 earnings call is scheduled for Tuesday, January 31, 2017.

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, November 1, 2016 and disclaims any duty to update them.

During this call, the financial metrics, with the exception of free cash flow, will be presented on a GAAP basis. 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, Chris.

Electronic Arts delivered excellent results for the second quarter of fiscal 17, powered by a slate of the most advanced and innovative new EA SPORTS titles that we have ever delivered. We're thrilled with the quality and player excitement for the new games we launched in Q2, and even more excited for the exceptional titles we've launched in Q3. As a result, we're raising our full-year guidance for FY17.

More than 43 million players engaged in our breakthrough EA SPORTS games across consoles and mobile devices during Q2. On console, *FIFA 17* has given soccer fans around the world a revolutionary new experience, powered by our Frostbite engine. We introduced "The Journey," FIFA's first-ever story mode, which helped bring 20% more players into *FIFA 17* in the first week over last year's game. To date nearly two-thirds of all *FIFA 17* players, spanning 183 countries, have engaged in this critically-acclaimed new addition to the game. The FIFA Ultimate Team experience is more robust than ever in *FIFA 17*, and engagement continues to grow through new modes and global competitions. Players in the FUT Champions mode are now competing to advance to our live tournament events, the FIFA 17 Ultimate Team Championship Series.

Madden NFL 17 players spent more time in the game in Q2 than any previous Madden title in the last five years, logging 44 million gameplay hours during the quarter. Ultimate Team also continues to grow in *Madden NFL*, with engaged players in MUT up nearly 20% year-over-year in Q2. Our *Madden NFL* competitive gaming season also kicked off in Q2 with the Madden Classic, the first of four EA Major live events in the *Madden NFL* Championship Series. 1.5 million fans played 5.8 million ranked games in the online qualifying rounds, and the top 16 players will compete for the Madden Classic championship in Los Angeles in early December. The holidays are always a great season for football, and we're looking forward to more passion and engagement from our *Madden NFL* community in the months ahead.

EA SPORTS has been a leader in high-quality and immersive sports games across multiple platforms, and now we're delivering on that promise for mobile players as well. We now have top-performing mobile titles across three of our major sports franchises: *Madden NFL Mobile* continues to grow year-over-year in both unique players and sessions per day; *NBA LIVE Mobile* has brought in more players than *Madden NFL Mobile* during its launch period; and *FIFA Mobile* hit #1 on the App Store Free Games chart in 138 countries just after its early Q3 launch.

Each of these experiences are long-term live services that we will continue to grow and tune with the expanding player base in this high-growth genre.

Strength in our mobile portfolio reaches across other key genres. Our action-RPG *Star Wars: Galaxy of Heroes* continues to drive strong levels of engagement, with average gameplay per player holding at 2.5 hours per day in Q2 – one of the highest totals we've seen in a mobile game. Our deep roster of live services on mobile including *The Sims FreePlay*, *SimCity BuildIt* and *Real Racing 3* continue to deliver long-lasting entertainment. Mobile players today expect increasing levels of creativity, depth and polish in the games they play, and as a result only a few titles will break out. With decades of rich experience building high-quality and immersive games, a portfolio of leading titles and a strong pipeline of new projects, we're well-positioned for this evolution in mobile.

Throughout Q2, the energy around our two groundbreaking first-person shooter games – *Battlefield 1* and *Titanfall 2* – continued to build in anticipation of the Q3 launches.

Battlefield 1 has impressed at every turn. From the debut trailer to subsequent looks at gameplay, features and single-player stories, our *Battlefield 1* content has driven 100 million video views on YouTube, a record level for any EA game. Community influencers shared hundreds of hours of gameplay captured from play sessions around the world, bringing the world of *Battlefield 1* to life in unprecedented depth. DICE has redefined the shooter genre with *Battlefield 1*, which now stands as the most highly-rated *Battlefield* game of this generation. Player engagement since launch on October 21 has been phenomenal – *Battlefield 1*'s total player base for the first week was nearly double that of *Battlefield 4*.

Respawn has cemented *Titanfall*'s position as one of the most exciting new IPs in the industry with the bold vision and exhilarating action of *Titanfall 2*. This is a game that feels incredibly fluid and fulfilling to play. Critics agree that *Titanfall 2* is a fantastic game, with more than 40 top outlets from around the world rating it 90 and above in reviews. The thrill of multiplayer in *Titanfall 2* has the community buzzing, and rave reviews are also coming for the campaign that adds purpose and depth to the experience. *Titanfall 2* is being called one of the year's must-play titles, and we're excited to see more fans across the world getting their hands on this extraordinary game.

Heading into a holiday season that will include updated consoles and more mobile devices, Electronic Arts is in outstanding position. With *Battlefield 1* and *Titanfall 2*, we now have two of the top-rated shooter games of this console generation engaging a broad audience of players. Our EA SPORTS titles are delivering excitement for fans with thrilling new gameplay, challenges in Ultimate Team, and dozens of new competitive gaming tournaments from the community level to the global stage. Our mobile portfolio has a game for every player, with *Star Wars: Galaxy of Heroes*, *Plants vs. Zombies Heroes* and more. And we will also deliver our first virtual reality experiences this holiday with the *Star Wars Battlefront Rogue One: X-wing VR Mission* for PlayStation VR and *Need for Speed No Limits* on Daydream, Google's VR platform.

We're looking forward to another strong quarter ahead. Now, I'll turn the call over to Blake.

BLAKE:

Thanks, Andrew.

Before I talk about the quarter, I'd like to describe the steps we are taking to improve transparency in our new, GAAP-only reporting environment. As we mentioned on our Q1 earnings call, we are no longer reporting non-GAAP metrics, but will provide you with all the GAAP data you need to derive metrics comparable to our historically reported non-GAAP financials.

In addition, to give more visibility into the performance of the business, we have decided to add a new operating performance metric, net sales. We define net sales as the net amount of products and services sold digitally or sold-in physically in the period. Historical net sales have been added to our downloadable model posted on our website. In addition, please reference the tables in our press release as we discuss GAAP results and the GAAP adjustments that may be applied to compare them with our historical non-GAAP results.

I'll start by reporting our results on a GAAP basis, then use our new operational measure to discuss the dynamics of our business.

We are very pleased with the strong second quarter, in particular the great reception for *FIFA 17* and the strength of our mobile portfolio.

EA's GAAP net revenue was \$898 million, compared to \$815 million last year. Net revenue was below our guidance by \$17 million. However, the change in deferred net revenue was \$40 million above our guidance, at \$200 million. If you wish to compare our current results to our historical non-GAAP revenue, you will need to add GAAP revenue of \$898 million to the change in deferred net revenue of \$200 million. Thus, although underlying sales were above our expectations, because GAAP revenue is subject to the sales' timing within the quarter, a larger portion of the total sales was deferred into future quarters. The increase over last year's net revenue was primarily driven by the success of *Star Wars Battlefront* in Q3 fiscal 2016, compared to smaller launches in Q3 fiscal 2015. See the documents we posted on our investor relations website on July 19 for details on how to compare these results to historically reported non-GAAP results.

Our cost of revenue was \$401 million, including acquisition-related expenses of \$12 million and \$1 million of stock-based compensation.

Gross margin for the quarter was 55.3%, up 5.5 percentage points over last year. This reflects the strength of the launch of *Star Wars Battlefront* three quarters ago, in Q3 fiscal 2016. As I just mentioned, revenue deferred from *Star Wars Battlefront* drove higher GAAP revenues in Q2 fiscal 2017 compared to the revenue deferred from smaller titles launched in Q3 fiscal 2015. However, cost of revenue this Q2 and last Q2 were approximately the same, given that the respective launch slates were similar. Thus GAAP gross margin was up year on year.

Operating expenses were \$546 million, up \$21 million or 4% year on year, driven by increased investment in R&D, particularly in new franchises and in our Player Network infrastructure. The \$20 million improvement on guidance was driven by timing of marketing activities. The \$546 million includes \$47 million in stock-based compensation and \$1 million in acquisition-related expenses.

The resulting **loss per share** was \$0.13, which is \$0.04 better than guidance due to lower costs. It is \$0.32 better than last year. GAAP adjustments to derive a measure comparable to our historical non-GAAP EPS include: the \$200 million change in deferred net revenue; \$13 million acquisition-related expenses; \$48 million of stock-based compensation attributed to operating expenses and cost of revenue; and a management reporting tax rate of 21%. Note that, given our GAAP result was a loss, our share count was 301 million shares, as GAAP requires us to exclude the estimated 13 million shares that might be issued in future, such as

the shares expected to be issued this quarter for the settlement of the warrants. Those shares would be included in the diluted share count had we reported a profit.

Net cash generated by operating activities for the quarter was \$109 million, up \$100 million on last year. For the trailing twelve months it was \$1.1 billion. With capital expenditures of \$120 million, free cash flow was \$1.0 billion in the same period. See our earnings slides for further cash flow information.

During Q2, we settled the remaining \$136 million of our **convertible notes**. As a reminder, the warrants issued with our convertible notes are still outstanding and, starting on October 17, began to exercise automatically over 60 trading days. We have posted a document on our website that explains the impact on our share count. The most important takeaway remains that our diluted share count already includes the potential dilution at the current share price.

During the quarter, we also **repurchased 1.6 million shares at a cost of \$127 million**, leaving \$282 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.

Our cash and short-term investments at the end of the quarter were \$3.27 billion. 43% of this balance is held onshore. This is down from 48% last quarter, the difference driven primarily by the share repurchase and convertible notes settlement.

Now, I'd like to turn to the key drivers of our business this quarter.

Net sales for the quarter were \$1.10 billion, better than our expectations. Sales were driven by successful sports launches and growth in mobile. As discussed on our last call, *FIFA 17* launched only four days from the end of the quarter, so almost no digital sales, whether downloads or Ultimate Team, were captured in the quarter. *FIFA 16* launched 11 days before the end of Q2 fiscal 2016, allowing a whole week of digital sales to be captured. Using the first four weeks of sales to make a true like-for-like comparison shows that FIFA sell-through is up 13% year on year, and this speaks to how The Journey story mode has grown the market for our biggest franchise.

Digital net sales were \$486 million, up \$6 million on the year-ago quarter. The increase reflects strong growth in mobile and in digital downloads, offset by the *FIFA* timing. The long-

term trend towards digital is clear in net sales for the last twelve months, which were \$2.6 billion, 57% of the total. Looking at each of the components of this quarter's digital sales in turn:

- **Extra content and freemium** net sales were down nearly 12% year on year, to \$172 million, driven by the fact that the almost all of the first week of *FIFA 17* digital sales will be captured in Q3 of this year. Using the first four weeks of *FIFA Ultimate Team* sales for *FIFA 17* and *FIFA 16* reveals year-on-year growth of 23%, even in the face of ongoing currency headwinds.
- **Mobile** net sales were \$138 million in the second quarter, up 22% year on year, with growth led by *Star Wars: Galaxy of Heroes*. We launched *NBA LIVE Mobile* in July and *FIFA Mobile* after quarter end, and early indications from both titles are promising.
- Net sales of **full game PC and console downloads** were \$93 million, up 4.5% over last year, in line with our expectations.
- **Subscriptions, advertising, and other digital** purchases contributed \$83 million to net sales, flat year on year. Strong growth in EA Access and Origin Access were offset by decline in revenue from some older titles.

Turning to guidance, we are raising our full year guidance to \$4.775 billion in net revenue, and a \$150 million increase in deferred net revenue. We anticipate cost of revenue to be \$1.387 billion, including \$31 million of acquisition-related costs and \$2 million of stock-based compensation. Operating expenses are expected to be \$2.304 billion, including \$198 million in stock-based compensation and \$6 million in acquisition-related costs.

This results in **earnings per share** of \$2.69 for the year, also an increase from prior guidance. GAAP adjustments to derive a measure comparable to our historical non-GAAP EPS include: the \$150 million change in deferred net revenue; \$200 million of stock-based compensation attributed to operating expenses and cost of revenue; \$37 million in acquisition-related costs; \$2 million in debt-related expenses; and a reduction of 1 million shares from the convertible bond hedge.

Regarding cash flow for the full fiscal year, we are reaffirming our operating cash flow guidance of approximately \$1.3 billion. Our capital expense forecast remains approximately

\$110 million, resulting in a free cash flow forecast of approximately \$1.2 billion. We expect Q3 fiscal 2017 to be our biggest cash quarter ever.

We anticipate **net sales for the year** to be approximately \$4.925 billion. This reflects a modest increase in our expectations for our underlying business, primarily based on the early success of *FIFA 17*. We're delighted with the way players are reacting to *Battlefield 1* and *Titanfall 2*. Both are also reviewing very well and we expect them to sell strongly for a long time. However, we're only a week into *Battlefield* and just a handful of days into *Titanfall*, so it's still too early to update sales forecasts for either.

Guidance for the third quarter is for net revenue of \$1.125 billion, excluding \$910 million in deferred net revenue. We anticipate **cost of revenue** to be \$532 million, including \$3 million of acquisition-related costs. **Operating expenses** are expected to be \$652 million, including \$50 million in stock-based compensation and \$2 million in acquisition-related costs. Excluding the effect of stock-based compensation, expenses are up year on year, chiefly driven by increased investment in new franchises and our Player Network.

This results in a **diluted loss per share** of \$0.17 for the quarter. GAAP adjustments to derive a measure comparable to our historical non-GAAP EPS include: the \$910 million change in deferred net revenue; \$50 million of stock-based compensation attributed to operating expenses; and \$5 million in acquisition-related expenses.

We anticipate **net sales for the quarter** to be \$2.035 billion. This is up 13% year-on-year, driven by the combination of *Battlefield 1* and *Titanfall 2*. As you build models and make year-on-year comparisons, remember that the same timing issue that pushed FIFA digital sales into fiscal Q3 will also push some holiday sales into our fiscal Q4.

In conclusion: with the new innovations in FIFA we've increased the market size; in *Battlefield 1* and *Titanfall 2* we have two extremely high-quality games in place for the holiday season; and we're continuing to grow our portfolio of successful mobile games. Together, we expect them to deliver a record holiday quarter.

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

ANDREW CLOSING:

Thanks, Blake.

EA is leading across multiple growth vectors that are shaping our industry.

The audience for high-quality games on HD consoles and PC continues to expand. We believe the new console options will add depth to the hardware cycle, grow the install base and add to the player value proposition. The power of our Frostbite engine enables us to scale with platform capabilities to deliver the experiences our players want. From the groundbreaking gameplay in *Battlefield 1* and *FIFA 17*, to *Mass Effect: Andromeda* in stunning 4K, to extraordinary new VR experiences from our labs teams across the spectrum of high-end and low-end devices, we are pushing the boundaries in a multi-platform world.

The evolution of mobile games is another growth vector, where the tenets of great mobile experiences and great HD games continue to converge and open new high-growth opportunities. In this increasingly competitive world, where the number of players and the number of games grows on a daily basis, players are looking to major brands as markers for quality. Their expectations for creativity, innovation, polish and depth play directly to our strengths. Our EA SPORTS titles are strong demonstrations of social play blended with strategy and action that have proven to deeply engage mobile players over time. We will continue to infuse this same approach throughout our pipeline of new mobile experiences in development for the quarters ahead.

Players today also have more ways to connect and engage with the games they love. Millions of fans are competing in our global *Madden NFL 17* and *FIFA 17* competitions, beginning with in-game qualifications and leaderboards that will ultimately feed championship events on a world stage. In-game competitions have kicked off for Madden Bowl, our second EA Major event for Madden, and season one of the *FIFA 17* Ultimate Team Championship Series is underway, which will culminate with the FIFA Interactive World Cup in August 2017. Beyond competitive gaming, we're introducing new tools for our community to create content and share more of the amazing experiences they have in games like *Battlefield 1*. And building on the continued success of EA Access and Origin Access, we're exploring ways to provide subscription choices for more of our players.

In an ever-changing world defined by more content, more devices, and an increasingly global player base, finding great games and connecting with friends becomes increasingly challenging. We are continuing to invest in our EA Player Network to reduce friction and improve discovery, purchase and enjoyment across all of our games and player touchpoints. The player experience as you enter *Battlefield 1* is a good example of how this is beginning to roll out, with a new consistent interface that brings players into their personal Battlefield universe with the games they own, content recommendations, and faster ways to squad up with their friends. The Player Network will grow and attract more players with these personalized services, in-game and out-of-game, that add value and improve the experience with every minute of play.

We're energized to introduce our players to new experiences, new connections, and new ways to play. Now Blake and I are here for your questions.

Forward-Looking Statements

Some statements set forth in this document, including the information relating to EA's fiscal 2017 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, 2016.

These forward-looking statements are current as of November 1, 2016. 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, 2016. 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, 2016.