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Global Video Games Investment Review - <http://bit.ly/buA71D>

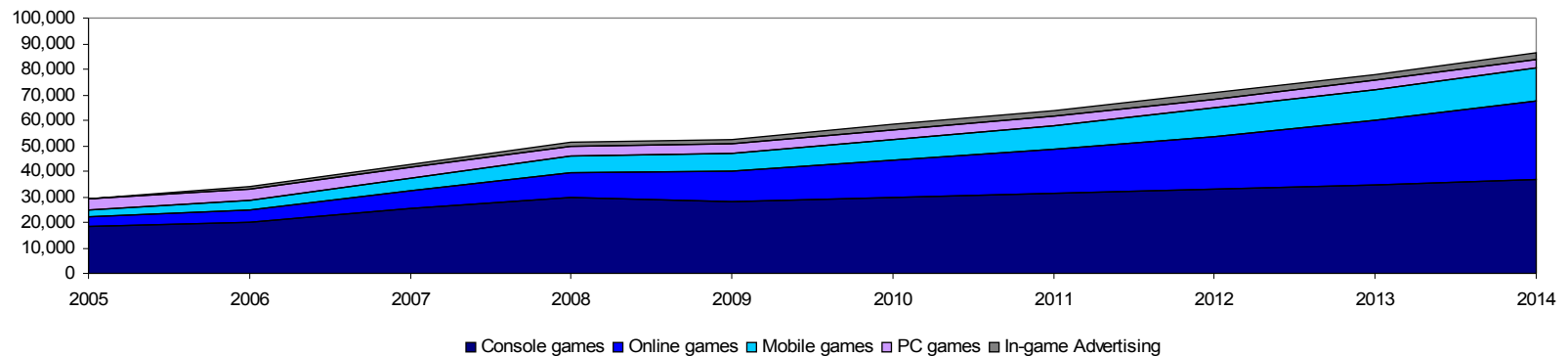
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The video games industry is big, getting bigger and changing

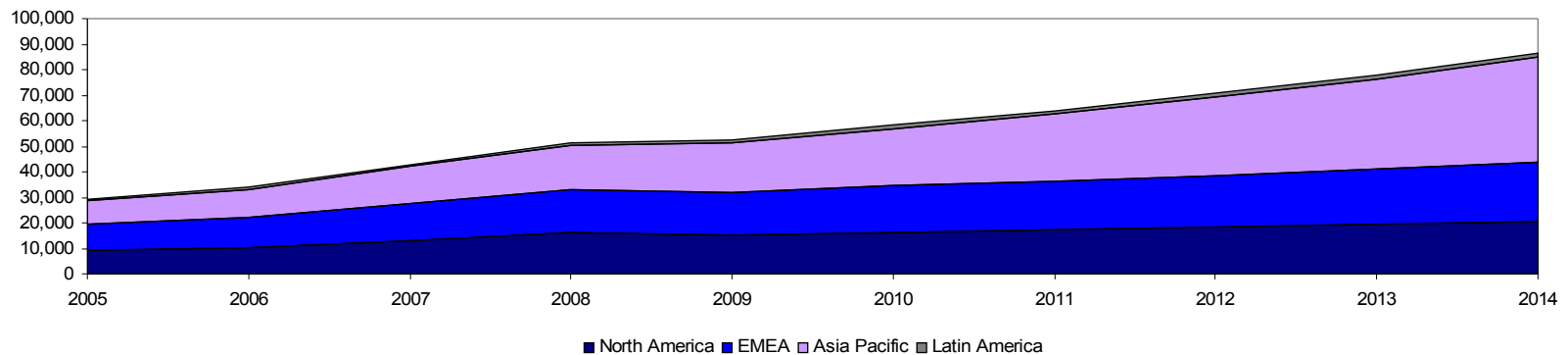
Pure console* remains the largest low growth sector, online† and mobile drive market growth

Global Video Game Sector Revenue (\$M)



Asia Pacific and Europe to pass North America driven by higher online and mobile growth rates

Regional Video Game Market Revenue (\$M)



Console game costs, revenue and risks are accelerating

Investment per game is accelerating

- Average game development costs are growing
 - Xbox, PS2, Gamecube: \$3-5M
 - Wii: \$5-7M
 - XBox360, PS3: \$15-30m
 - Next console cycle: ?
- Strong development project management is crucial
- Marketing costs are substantial
 - Equivalent to development cost or higher
- Retail, distribution and hardware royalties are significant
 - 30-40% of retail turnover
- 500K to 1M units just to break even (ex-overheads)

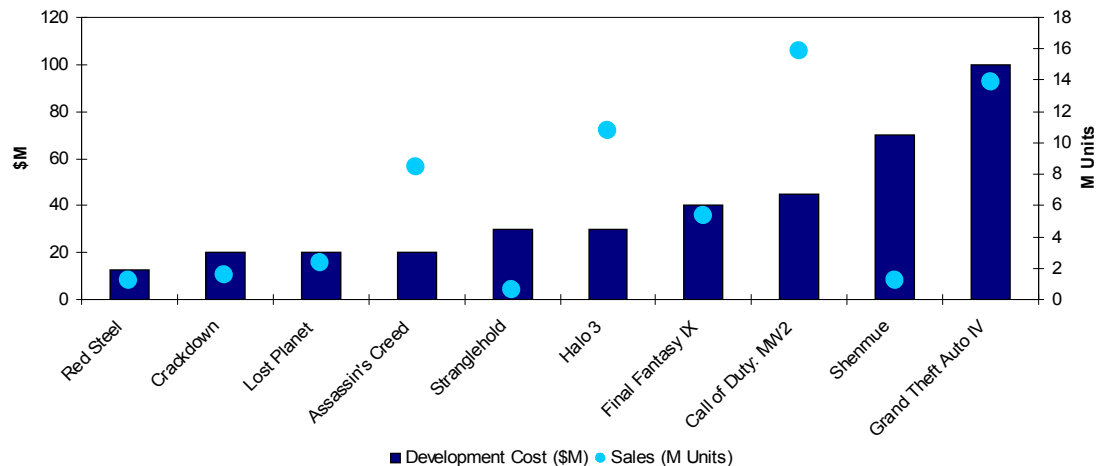
Video games rivalled Hollywood in 2009

- Hardware: \$22B Revenue
- Software: \$55B Revenue
- Total \$77B video games vs \$85B film global revenue
- Up to \$60 per game sold vs \$10-20 per cinema ticket/DVD
- Video games growth to be driven by online, mobile and next console cycle

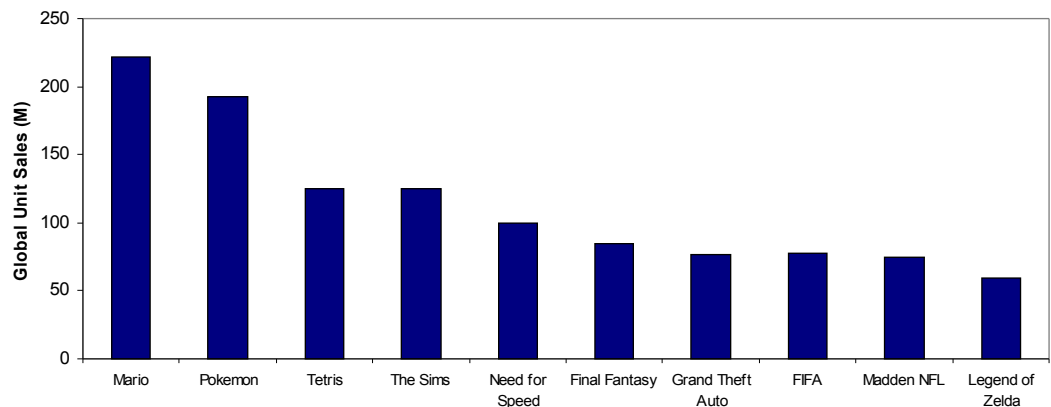
But failed games can be deadly

- 2001 Daikatana – ION Storm Dallas closed
- 2004 Malice – Argonaut into receivership
- 2008 Hellgate – Flagship into receivership
- 2008 Haze – Free Radical into receivership
- 2009 Tabula Rasa – NCSoft closes \$69M MMO after 15 months sales following 7 year development
- 2009 Duke Nukem Forever – Take2 closes 3D Realms without any game release following 12 year development

Console games are hit driven, with investment no guarantee of success



Franchises selling tens of millions of units are lower risk



Online/mobile games are growing and fragmenting the market

Online*/mobile growing scale and share

- 2009 \$19B revenue = 32% share of total video games
- 2014 \$44B revenue = 50% share of total video games

As consumer markets fragment

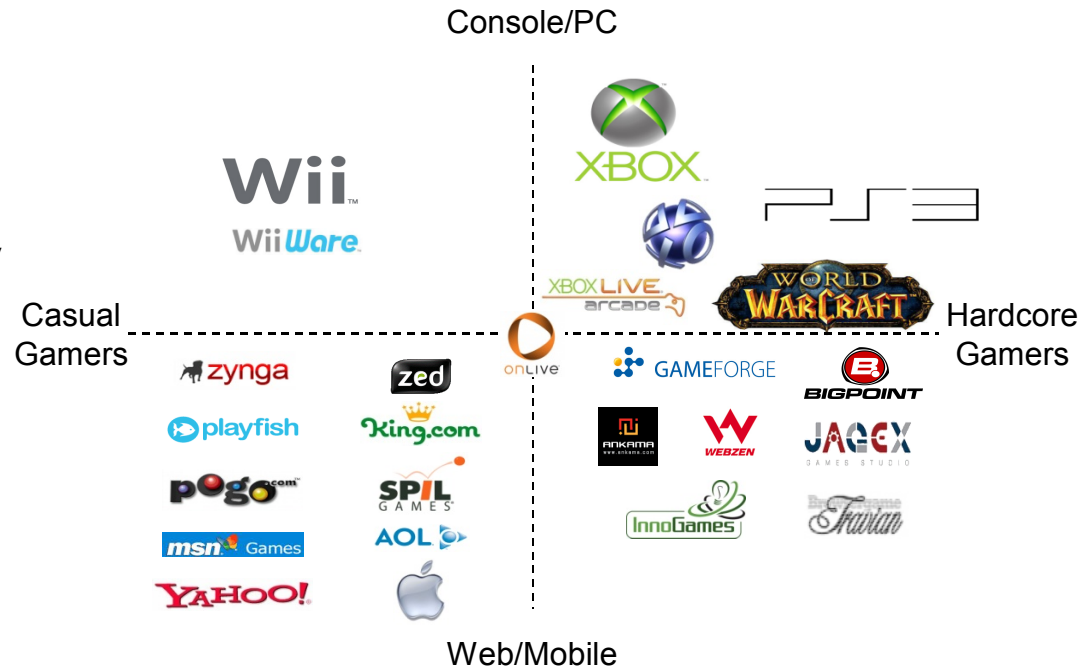
- Wii grew Casual Console market (60M+ Wii's sold)
- Apple grew Casual/Social Mobile market (3B Apps sold)
- WoW grew Hardcore Online market (11.5M+ subs)
- Zynga, Spil, Playfish, Yahoo! grew Casual/Social Web market (200M players)
- King.com grew Casual Skill Web market (20M players)
- Bigpoint bridged Casual to Hardcore online market (web delivery, PS2 quality, no downloads)
- Online hopes to expand Casual to Hardcore markets across TV and web (digital delivery, no console, PS3 quality)

Supported by profitable business models

- Best companies growing revenue 100%+ annually while also generating 20-30%EBITDA margins
- App Store: free to \$10 per game
- WoW: \$12.99-\$14.99 monthly fee
- Spil: free, advertising supported
- Zynga: free, micro-transactions, lead generation
- King.com: rake of user bets, micro-transactions
- Bigpoint: free, subscription and in-game item sales (micro-transactions), no advertising

And requiring different skills and approaches

- Multiple, parallel game development business platforms (not "one game" hit driven companies)
- Multiple distributors (not just Facebook)
- Rapid, low cost game development and continuous daily redevelopment cycles for rapid market response
- Fast failure (cut commercial losers, back commercial winners)



With investment dynamics entering a new phase

Majors focus on franchises, digital and cost

- Highest game sales come from existing franchises
- Retail market increasingly hit driven with downward retail volume and margin pressure, similar to filmed entertainment
- Majors adopting similar strategies to maximise short to medium term earnings, but risking declining long term growth:
 - Activision Blizzard: 75% revenue from franchises, with "select few new properties"
 - EA: "fewer & bigger" hits in core, drive digital (Playfish acquisition), manage costs
 - THQ: "fewer, better games"
 - Ubisoft: new franchise refresh "every 12-18 months"

With negative impact on independents

- Independents rely on advances and third party work from majors
- Narrower major focus = fewer advances and less third party work
- "Fewer, bigger" hits for majors increases investment per game, competition and risk for independent releases
- Hit driven, high risk market has lead to many independents struggling to adapt and survive

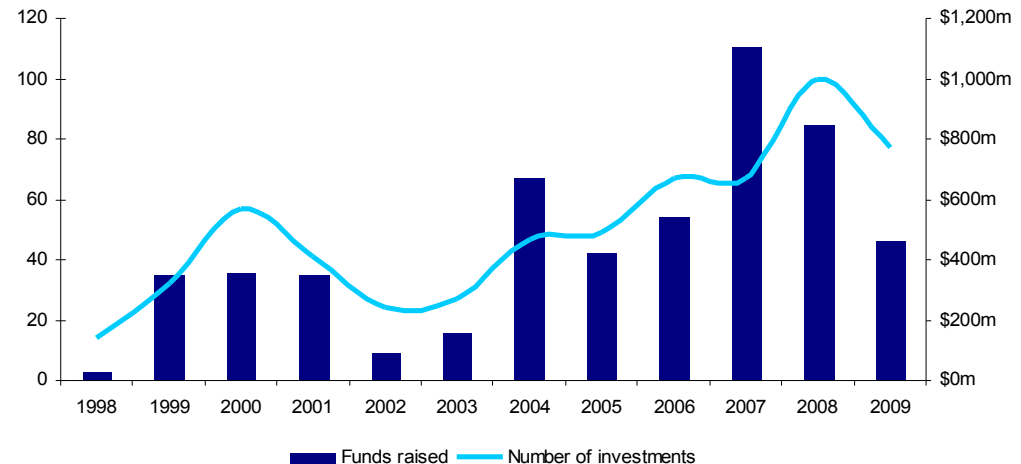
Fundraising remains robust for the right pitch

- Casual/Social
- MMO
- Mobile/iPhone
- Educational
- Digital distribution
- Niche (geography/culture) console games
- Video games technology (3D game engines, motion capture etc)

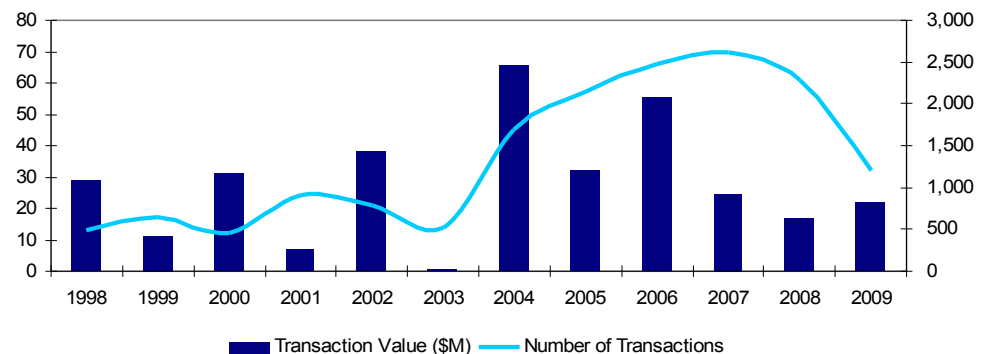
Quality consolidating M&A set to rebound

- Consolidation of major publishers and online (EA/Playfish)
- Consolidation of major media and online (Disney/Playdom)
- Consolidation within crowded casual/social market
- Consolidation of offline and online gambling

Global Video Games Private Fundraising

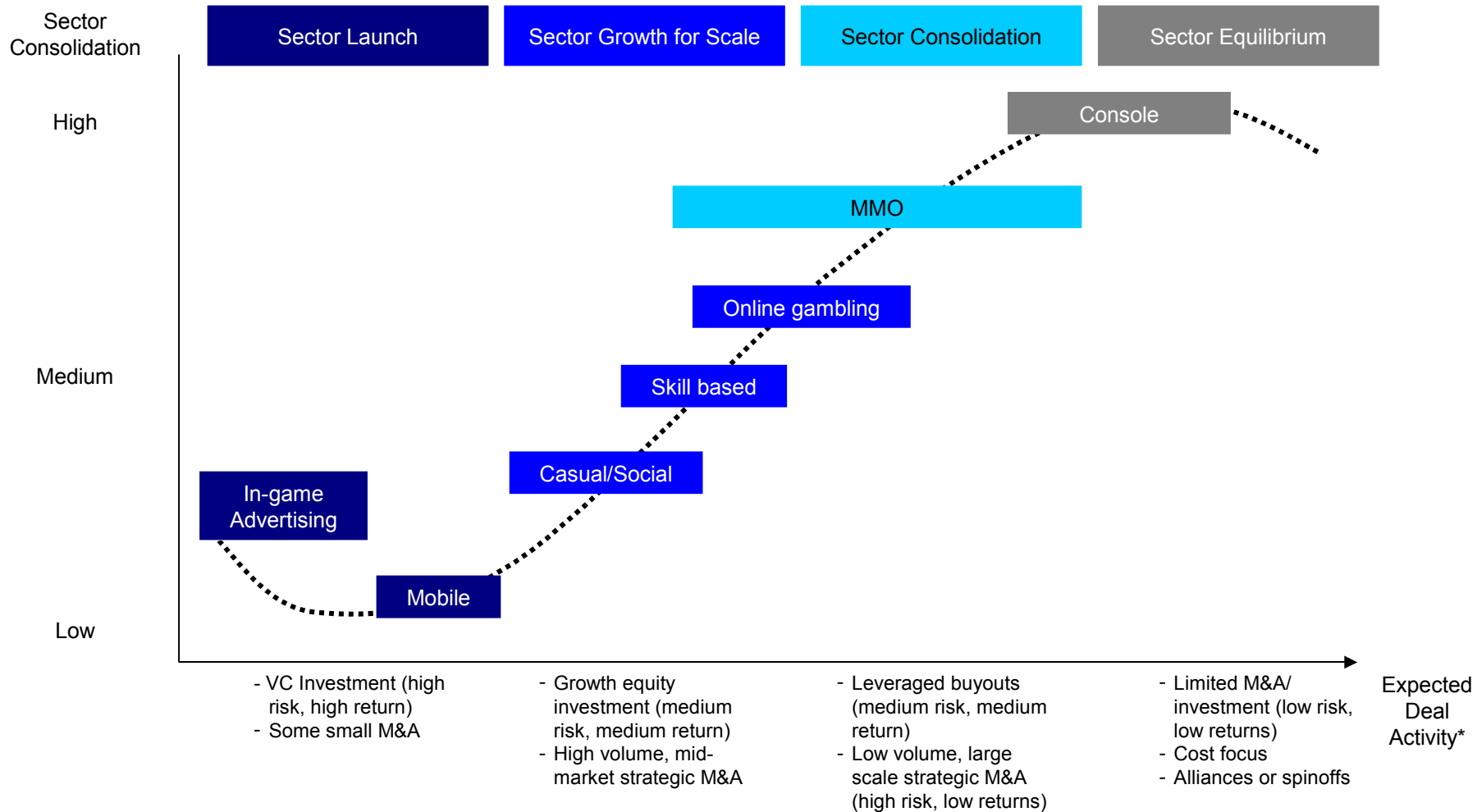


Global Video Games M&A



Deal activity is being driven by subsector consolidation

Consolidation Curve for Video Games

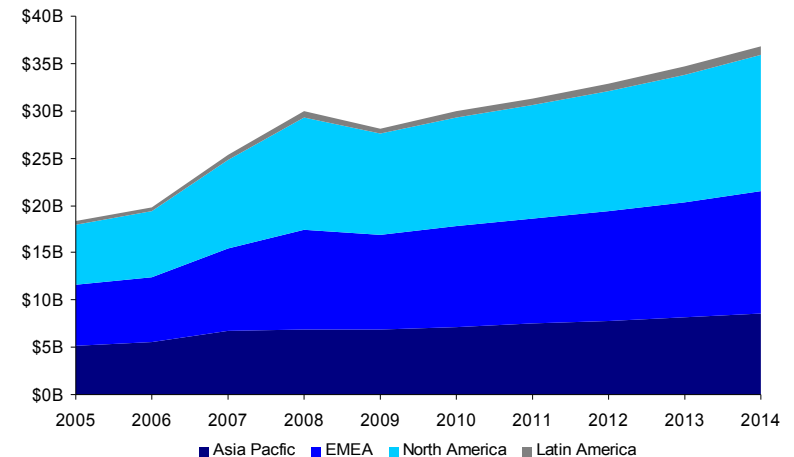


Console games have driven the video games market

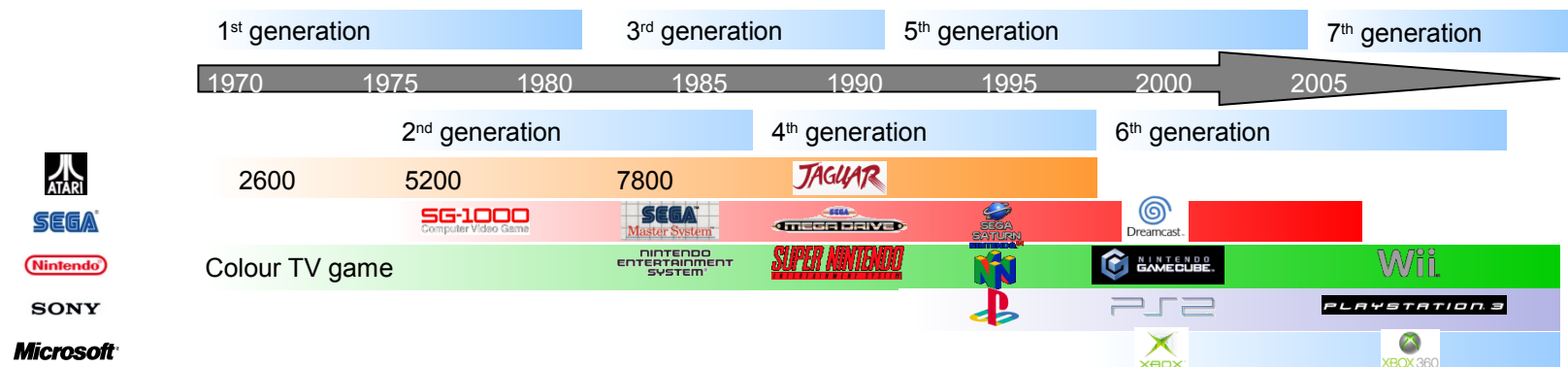
A consolidated sector driven by hardware cycles

- Wii dominates current 7th generation consoles with 47% of global platform revenue, followed by the Xbox360 at 35% and PS3 at 18%
- Market forecast of \$37B revenue by 2014, fuelled by North American and European growth from anticipated 8th generation platforms (2014-2016). Asia-Pacific growth limited by piracy and high share of MMO/casual/social online games
- Console games profits for Sony/Microsoft come from software, as consoles sold at a loss. The lower cost Wii has generated hardware profits for Nintendo
- Software pureplays can be highly profitable, but decline in packaged goods retail sales led to losses for many firms in 2009
- 8th generation console cycle forecast to drive growth, but such growth is likely to be constrained by growing MMO, casual/social online and mobile games marketshare
- The launch of Apple's iPad and imitators may change the console market in ways that are likely to be greater, but take much longer to occur, than anticipated
- Digital downloadable content and game delivery reduce likelihood of a 9th generation console cycle, creating potentially significant long term issues for Sony, Microsoft, Nintendo and GameStop

Worldwide pure console* software market

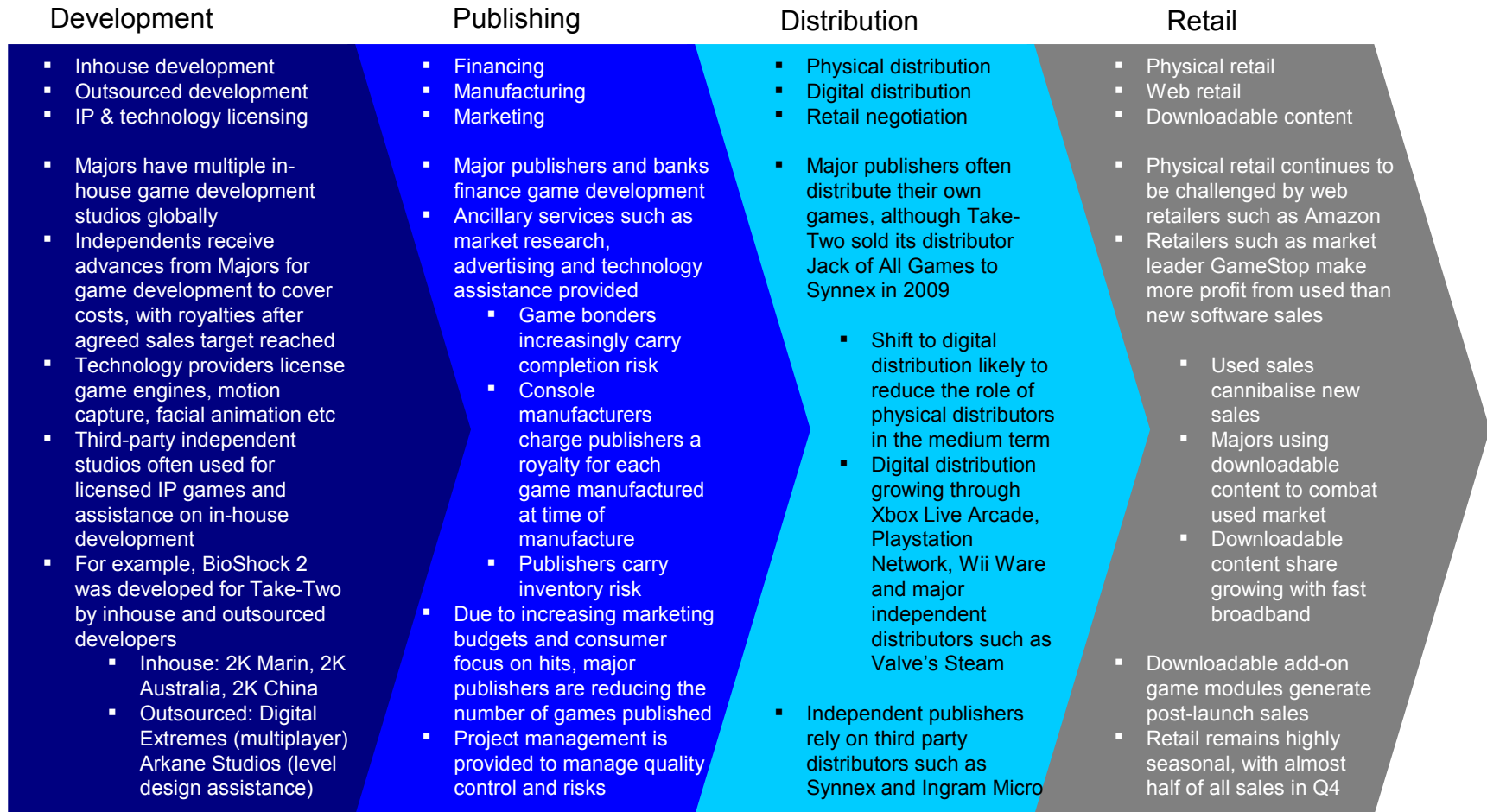


The console market has gone through 7 overlapping platform/technology cycles

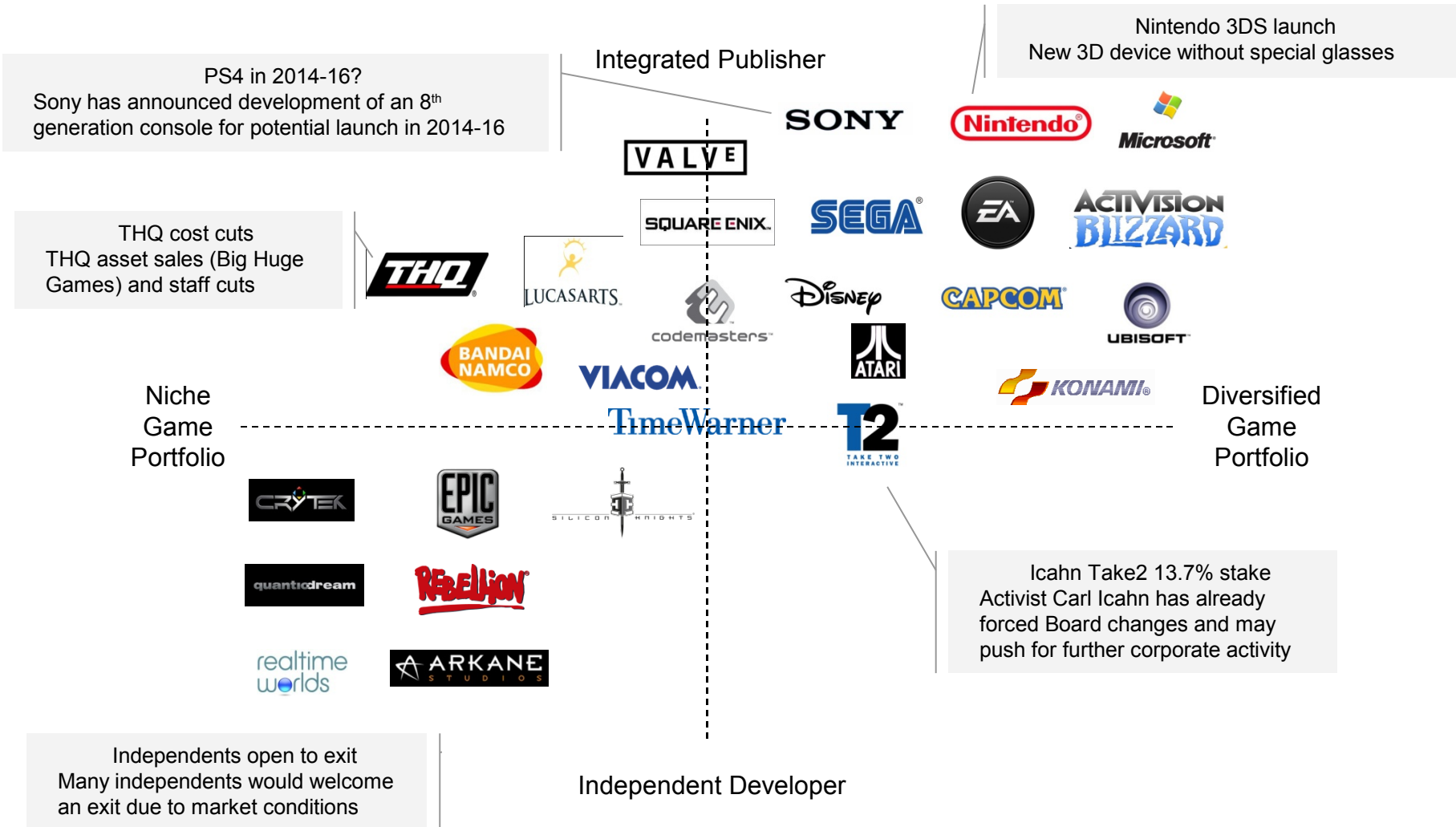


But its mature value chain is changing

Changes in industry dynamics impact all stages of the value chain



The console software market is still driven by major publishers



The MMO sector is both high growth and consolidated

The MMO sector is highly cash generative

- MMOs are video games with thousand of simultaneous players
- Business models are retail, subscription, micro transactions (in-game currency commission and items) and advertising
- WoW customers pay \$12.99-14.99 monthly fees
- MMOs operate across all major platforms

Market growth rates are forecast to accelerate

- There are currently over 15M paying MMO subscribers globally, with a strong presence in China and South Korea
- The MMO subscription market is forecast to reach 30 million by 2012 based on regression analysis of recent data

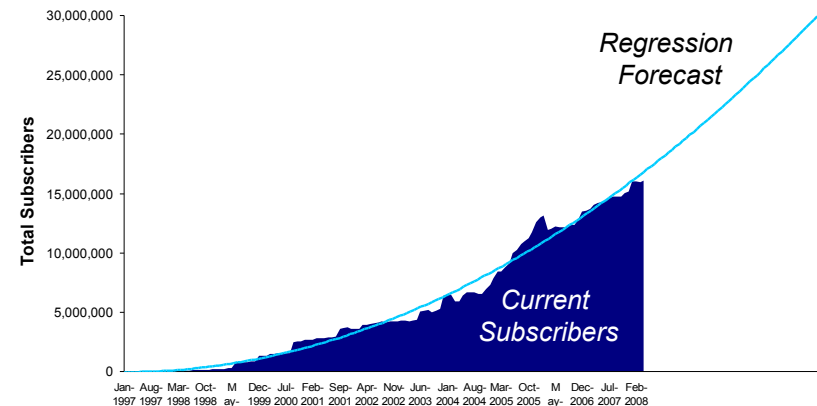
But MMOs are also hit driven and high risk

- Many retail MMOs have grown during their launch year, followed by up to 3 years of stability before an often sharp decline
- MMOs that rely purely on digital distribution tend to grow slowly
- MMO expansion packs help to manage churn and ongoing retail presence
- Poor launches are generally fatal: NCSoft shut \$69M Tabula Rasa after only 15 months of sales and a year development

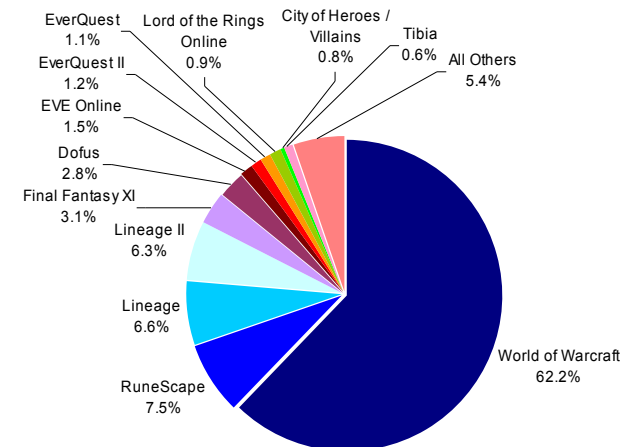
World of Warcraft currently skews the market

- World of Warcraft accounts for ~2/3 of subscriptions, and is a significant profit driver for Vivendi
- The strength of the “fantasy” MMO market (>90% subscriptions market share) has prompted many copycat offerings, with 35+ males the largest player demographic
- There appears to be significant untapped potential for MMOs in other game genres, suggesting a “Blue Ocean Strategy” approach to opening new genres (as with Nintendo Wii in the console market)
- APB from independent RealTimeWorlds attempted to expand a different MMO genre in 2010 following \$50m investment

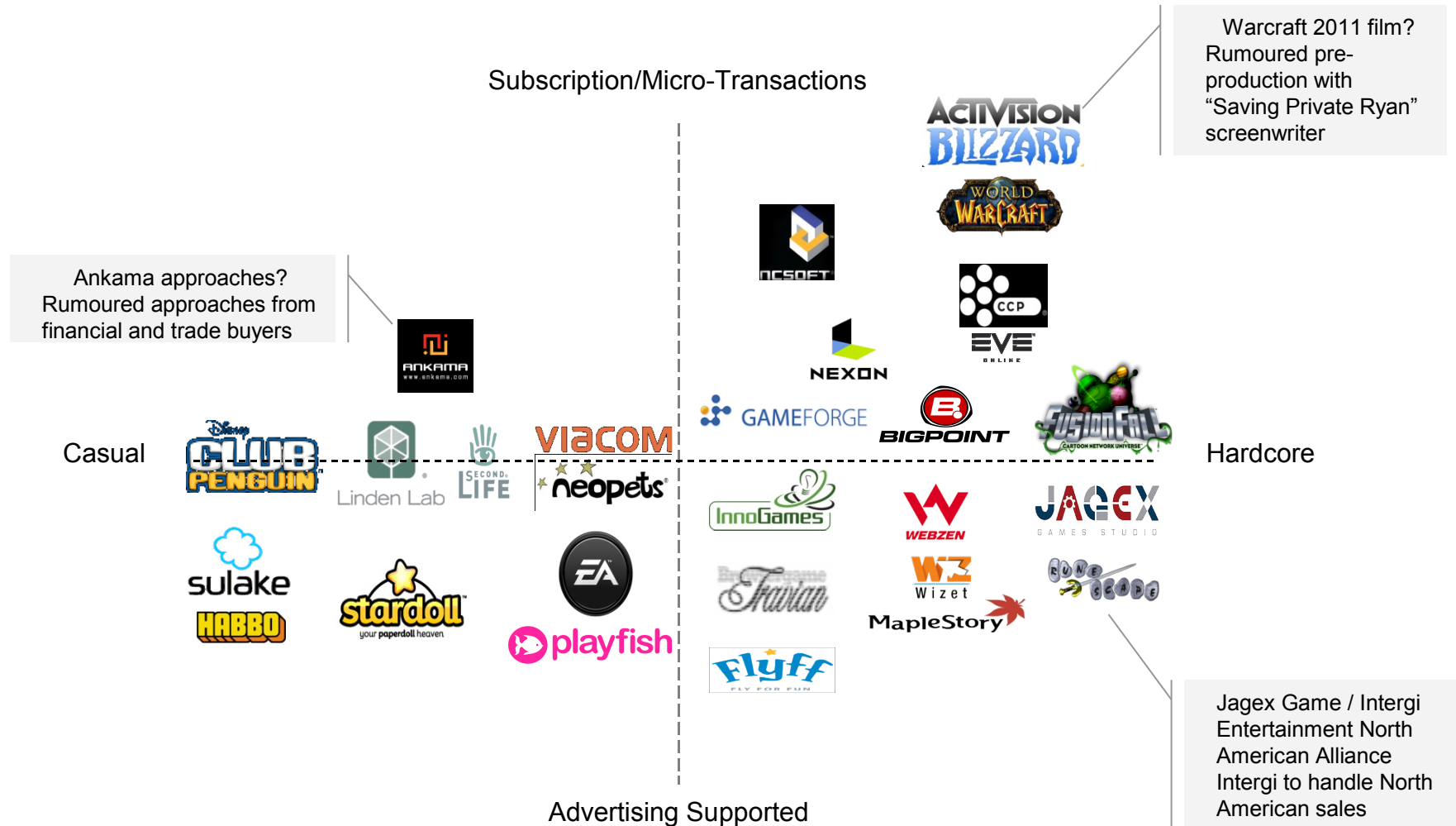
MMO subscriber growth forecast



MMO subscriptions market share*



Yet remains an early stage market with evolving dynamics

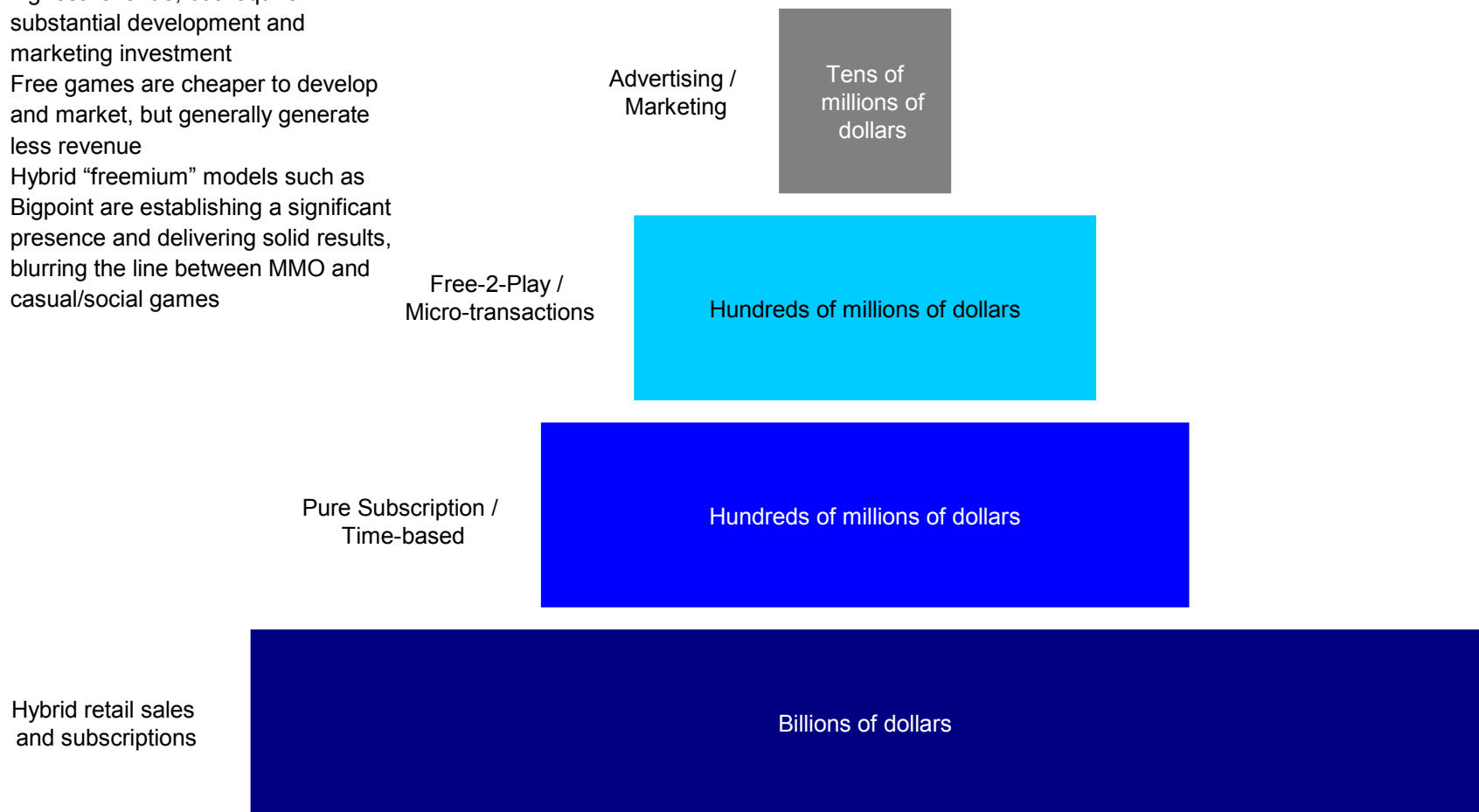


And a clear hierarchy of successful business models

Business models are solidifying

- Subscription-based models generate highest revenue, but require substantial development and marketing investment
- Free games are cheaper to develop and market, but generally generate less revenue
- Hybrid “freemium” models such as Bigpoint are establishing a significant presence and delivering solid results, blurring the line between MMO and casual/social games

Revenue Potential



Casual/social online games are growing extremely rapidly

Casual/social online games have two primary forms

- Casual/social online games require little experience or time commitment, with simple rules and gameplay accessed through a web browser
- The primary forms of casual/social online games are:
 - Casual: single player, played on a casual games platform such as Spil
 - Social: multiplayer, played either on a casual/social games platform (e.g. Bigpoint) or via a social network such as Facebook (e.g. Zynga)

The global market is high growth

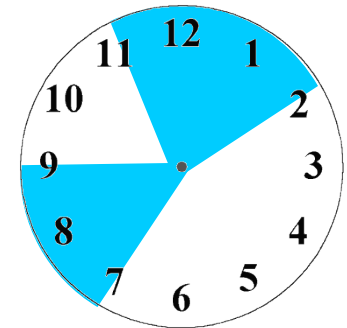
- \$2.25B revenue 2007, \$3B revenue 2009*
- >200m monthly unique players globally
- China and Korea generated \$1B revenue in 2007
- Casual/social games have a high proportion of paying female customer (74%)
- Popular casual games include:
 - Bejeweled (PopCap Games)
 - QQ Games Collection (Tencent China)
 - Diner Dash (Playfirst)
- Popular social games include:
 - Farmville (Zynga)
 - Dark Orbit and Deepolis (Bigpoint)
 - Pet Society (Playfish)

With multiple business models

- Subscription and in-game item sales (micro-transactions) models most profitable
- Advertising supported models are cyclical, with generally lower margins
- Bigpoint (browser “core” – between hardcore and pure casual gameplay): free, subscription and in-game item sale, limited advertising
- Zynga (social): free, in-game item sales (micro-transactions), lead generation
- Spil (casual): free, advertising supported, micro-transactions
- Casual/social game development costs of less than \$500k are much lower than console game development costs

Peak casual/social games hours

- Heaviest play times are 7-9pm and 11-2pm around lunch and dinner
- Casual/social gamers who pay for a subscription and/or are community users average 7-15 hours of online play per week

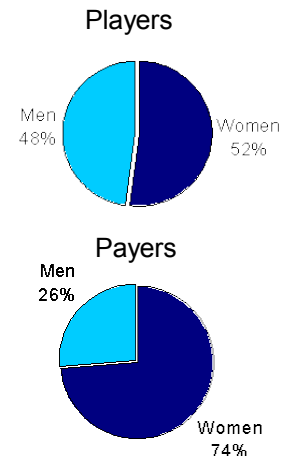


Casual/social players vs payers















































Women account for 52% of casual/social game players



Women account for 74% of paying players



Providing opportunities across the casual/social value chain

Developer	Publishers	Portals	Aggregators	Tools & Technology
Creation, design and development of a game	Funding, distribution and project management	Casual/social game destination websites	Intermediary between developers, publishers and portals	Enable the creation and distribution of casual/social games
          	      	                      	     	   
<p>More SPIL acquisitions?</p> <p>SPIL acquired Onrpg.com to enter the MMO sector, opening the door to acquiring other developers to extend its offering</p>	<p>Disney and GameStop buys</p> <p>Disney buys Playdom for \$763M and GameStop buys Kongrate</p>	<p>Next after Playfish/Playdom?</p> <p>Zynga, Bigpoint and GameForge are subject to constant speculation about IPO or exit</p>	<p>Google investment in Zynga</p> <p>Unconfirmed rumours of Google investing between \$100 million and \$200 million in Zynga</p>	<p>Microsoft's casual expansion</p> <p>Microsoft has boosted the video game-related capabilities of Bing, integrating around 100 casual games directly</p>



But there is a gap in online/mobile games investment

Major publishers aren't structured for online/mobile investment

- Major publishers' core competencies focus on management of \$20m+ serial, high risk, complex developments, launches and commercialisation
- Online/mobile games require rapid, multiple, small scale parallel development platform investments, completely different to major publishers' business cultures
- Major publishers are not investing significantly organically
- Major publishers are wary of large scale online/mobile video games M&A in early stage, fragmented markets where market dominance is not yet clear

Generalist VC video games investment is in decline

- Despite rapid market growth, VC investment across video games in 2009 had dropped by 60% from its high point in 2007 due to general VC market weakness and limited knowledge and relationships across complex, fast moving online/mobile games sectors
- High quality, high growth online/mobile video games companies are struggling to secure VC investment to maximise growth during the critical stage before industry consolidation
- Quality demand exceeds quality supply of investment and board representation

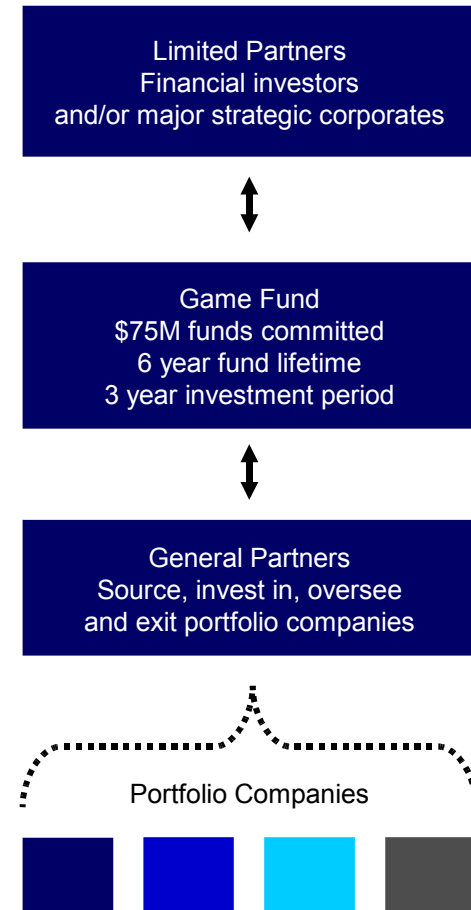
So a growth capital game fund offers substantial opportunity

- Growth capital game fund investing in online/mobile game companies, not individual games
- Working capital and equity investments in multiple, parallel game development business platforms (not "one game" hit driven companies)
- Growth capital returns (>30% IRR, 3-6X money multiple), not lower return project funding

To profit from opportunities and manage risks in a complex market

- Say \$75M online and mobile game fund, investing \$25M+ per year
- Online/mobile video games working capital, VC A, B, C rounds and growth equity
- Both US and European focus (possibly China, Japan and South Korea with partners)
- General Partners with strong industry, financial and entrepreneurial track records
- Both strategic (major video game and media corporates) and financial Limited Partners
- Co-investment with Tier 1 VC/PE firms and/or Limited Partners for larger deals
- Market leading video games investment market analysis
- Follow-on fund sizes could be increased if outstanding returns delivered

Game Fund Structure



Mobile games are being reinvigorated by smartphone growth

Smartphone marketshare is accelerating

- Global mobile phone penetration 67% in 2009, 5B subs in in 2010F
- Mobile phone penetration >100% in many developed markets
- Total global mobile phone market volume growth Q1 2010 = 21.7%
- Global smartphone market volume growth Q1 2010 = 56.7% (18.8% of total market volume in Q1 2010 vs 14.4% in Q1 2009)

Driving mobile games revenue growth

- Global mobile games market forecast to grow to >\$13B by 2014
- The mobile games market landscape is adapting to consumer trends and market demand:
 - Mobile game publishers are bypassing network operators to sell directly to consumers
 - High connectivity and multiplayer games becoming mass market due to unlimited data packages
 - In-game advertising being used to supplement mobile game revenues
 - Integrated applications increasing to allow converged gameplay with console/MMO/casual/social games

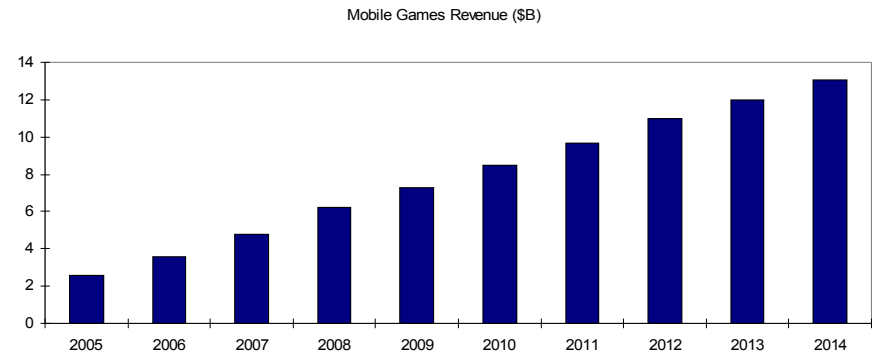
New players are entering from multiple markets

- Network operators (e.g. Vodafone Live!)
- Manufacturers (e.g. Nokia Ovi, Apple App Store)
- Web advertising platforms (e.g. Google)
- Console games majors (e.g. EA Mobile, THQ Wireless)
- Independent games companies (e.g. Glu Mobile)

With low barriers to entry

- Development costs tens to hundreds of thousands, not millions
- >3B iPhone Apps downloaded, many of which are independently developed games

Global mobile games revenue growth is strong

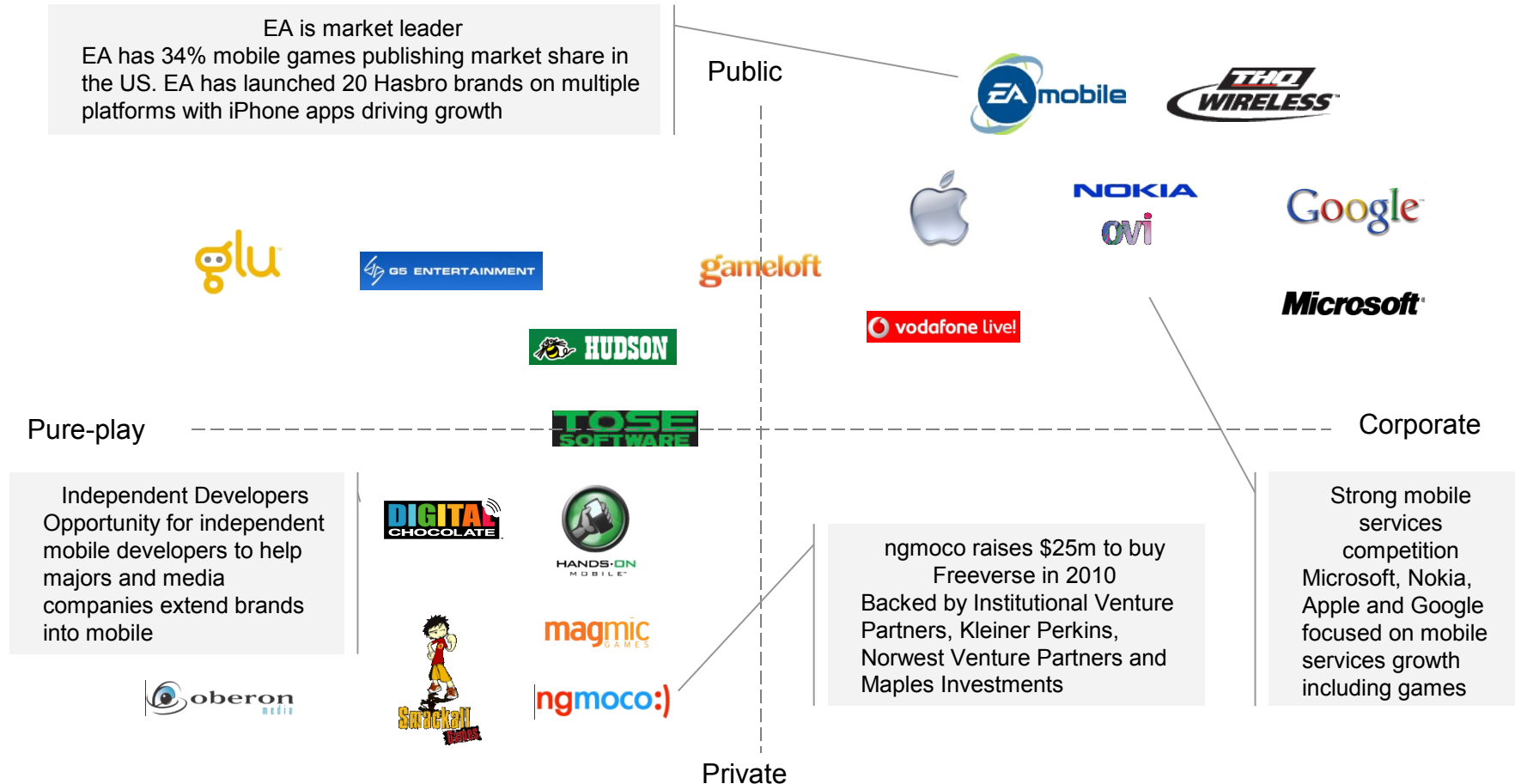


Mobile games platforms

Java is the most common platform for mobile games, but limitations require native binary formats for sophisticated games. Apple is blocking the use of Adobe's Flash platform on its own mobile devices



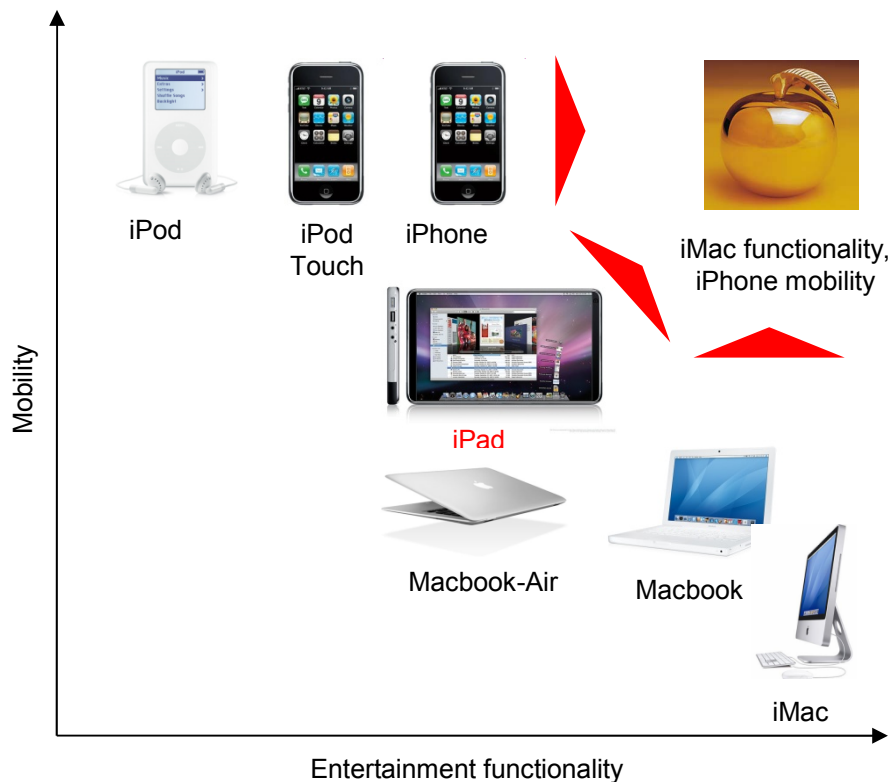
Attracting both corporates and independents



Apple is aiming to be *the* mobile entertainment company

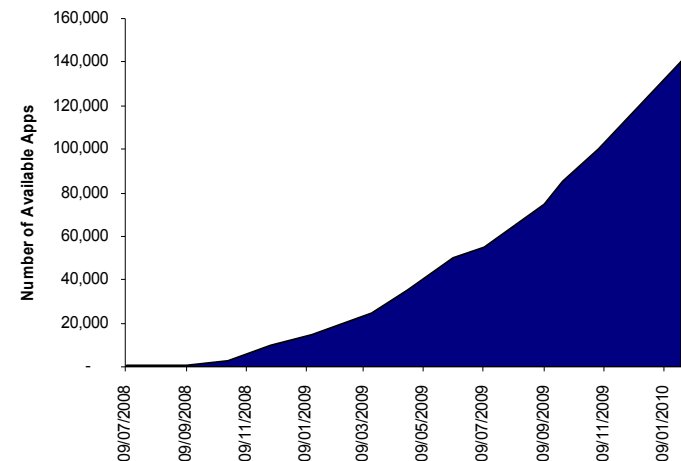
- Apple is far down the path of migrating from electronics and software to mobile communications and entertainment
- Apple's strength is providing all components of the mobile entertainment value chain in elegantly integrated consumer products and services, including hardware, software, eCommerce, applications and content
- iPad is the next stage of Apple's mobile entertainment strategy, likely to spawn many imitators. This may change the video games market in ways that are likely to be greater, but take much longer to occur, than anticipated

Aiming for a complete mobile offering



The App Store

- The App Store services iPhone, iPod Touch and iPad with >3B apps downloaded to date
- App Store should generate an increasing proportion of Apple's non-hardware revenues, with substantial unrealised profit potential
- 70/30 App Seller/Apple revenue split



And is already the mobile games app platform of choice

Apple is the dominant mobile games app platform in the US

- Apple has >7x more mobile apps than Android
- Apple has >4x new mobile apps developed per month than Android
- Apple mobile apps are paid for at twice the rate of Android apps
- 58% of Apple mobile apps are games

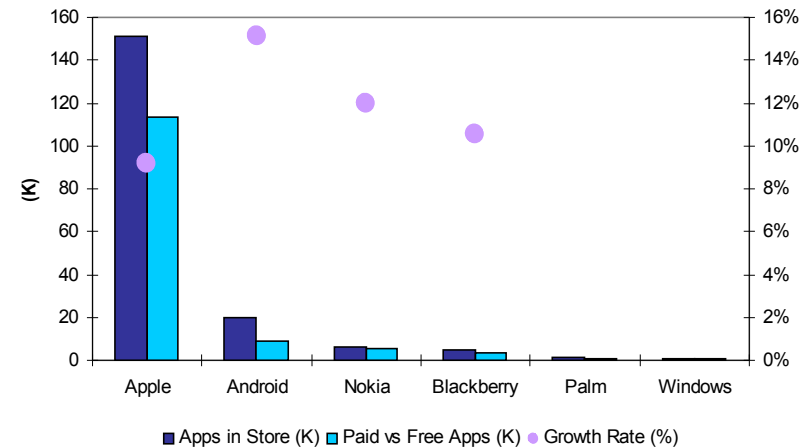
Consumers are prepared to pay for quality

- The highest volume mobile apps sell for \$0.99
- The highest grossing mobile apps sell for \$9.99

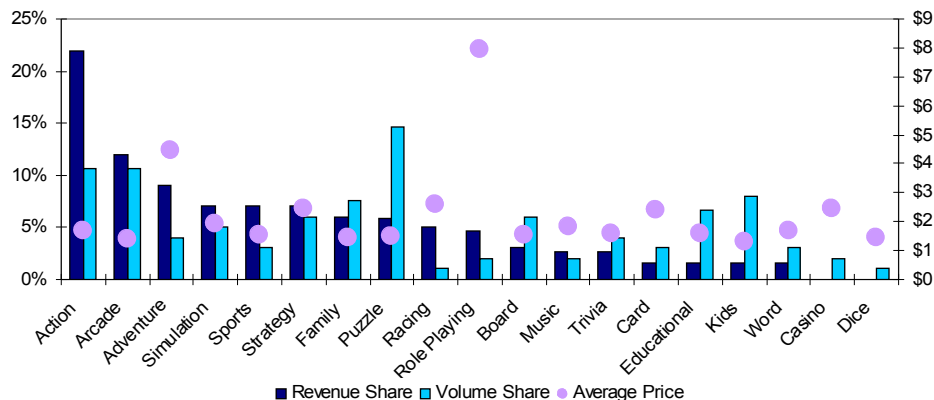
Casual/social games business models migrating to mobile

- "Freemium" models with in-game micro-transactions emerging
- For example, TapTap Revenge 3 (free app with in-app purchases of \$0.99) generated more revenue than FIFA10 (one-off app sale at \$6.99) in Jan 2010

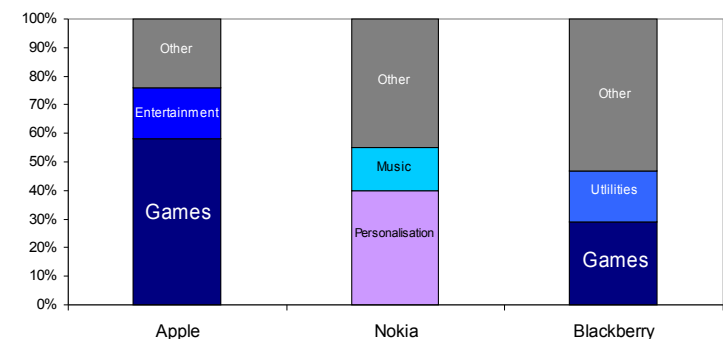
Mobile Applications (US)



Game genre share (revenue/volume) and average price (US)



Most popular app categories by platform (US)



Tencent 腾讯: MMO, casual/social online and mobile master

Tencent is the greatest game company you may not know yet

- China has 29% internet penetration, but 382M users
- China forecast to reach 56% internet penetration (754M users) by 2015
- Tencent holds dominant or leading stakes in many Chinese online/mobile markets (IM, games, eCommerce, search, mobile services)
- Tencent's Chinese games market share was 20% in 2009 with forecast 27% by 2012
- Tencent's market cap (~241Rmb B ≈ \$35B with EV ≈ 35x 2009 EBITDA) is substantially more than Activision Blizzard, Electronic Arts, GamesStop, Take2, THQ, Atari, Game Group and Ubisoft combined

Tencent's integrated model is where the market is headed

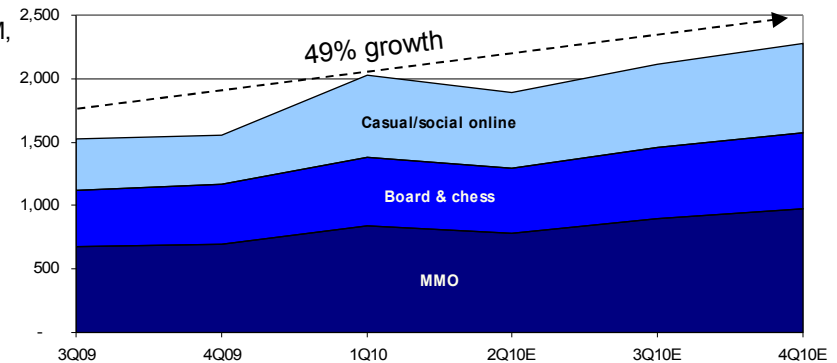
- Tencent generates ~50% operating margin
- Online/mobile games (MMO, board & chess, casual/social) generate >40% revenue
- Business model migrating from virtual items (higher Average Revenue per User) to subscriptions (short term revenue reduction, but lower volatility)
- Integrated model with upgrades/privileges across online, mobile and offline (not just games) is a significant advantage for customer acquisition, development and retention
- Enhanced capabilities to cross-promote, upsell and cross-sell

Tencent will be in your market soon, if it isn't already

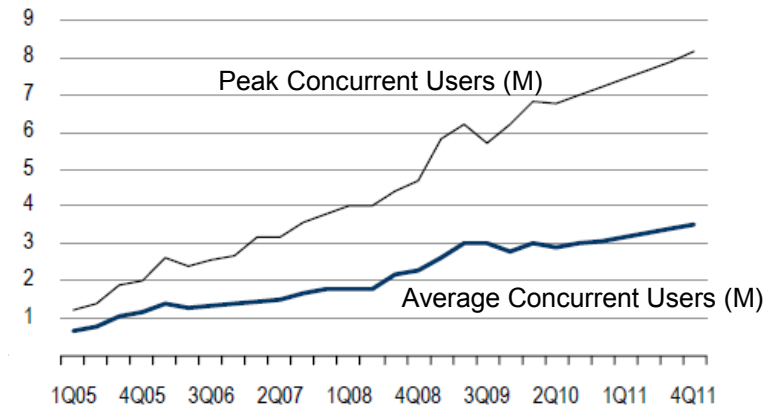
- Tencent is growing through domestic partnerships:
 - China Unicom (fixed line, 3G, operations, "QQ Wallet")
 - Hunan TV (talent, animation, online/mobile games)
 - China Merchants Bank (financial services)
- Tencent is expanding with international partnerships/investments:
 - Digital Sky Technologies (Facebook, Zynga, Mail.ru investor)
 - Vina Games (Vietnamese online games/internet)
 - MIH India Global Internet (licensed software, content & trademarks)
 - Naspers (36% Tencent investor) with global reach in high growth markets

Google, Microsoft and Amazon are learning from Tencent

Tencent Games Quarterly Revenue (Rmb M)



Tencent Concurrent Game Users



Online gambling continues to cannibalise offline

Online Gambling is high growth

- Ongoing revenue CAGR has been over 15% for the last decade
- Growing market share compared to offline (4.8% in 2008 grew to 6.3% in 2012)
- Online gambling uses the web and mobile to enable wagering, casino games, poker, lotteries, bingo and skill games
- B2C business models are based on odds stacked in the house's favour or scaled commission fee ("rake")

The line between B2C and B2B firms is blurring

- Content developers create and design games
- Platform developers develop software platforms to host games, as well as providing payment integration and statistical analysis
- Casino operators serve customers directly
- Combined B2B/B2C businesses are emerging, such as 888.com and its B2B unit Dragonfish

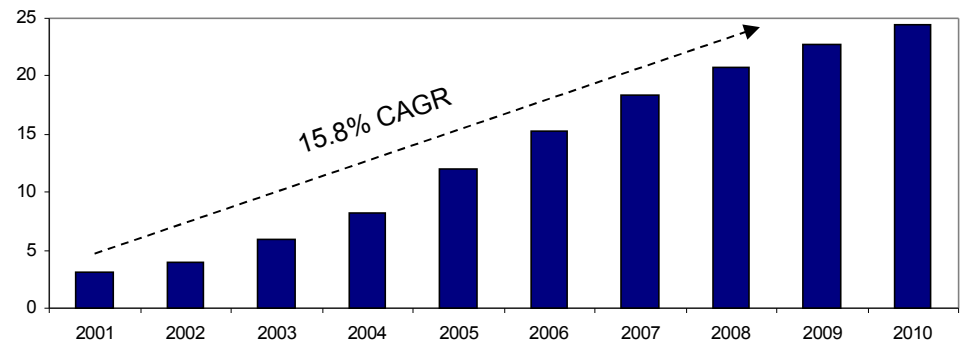
Consolidation is set to accelerate

- Europe is the largest market, supplanting the US after the Unlawful Internet Gambling Enforcement Act 2006
- The fragmented market in Europe is ripe for consolidation, with Bwin (8% market share), PartyGaming (6.3%) and William Hill Plc (4.5%) the largest firms
- Africa and South America are forecast to grow quickly from a low base

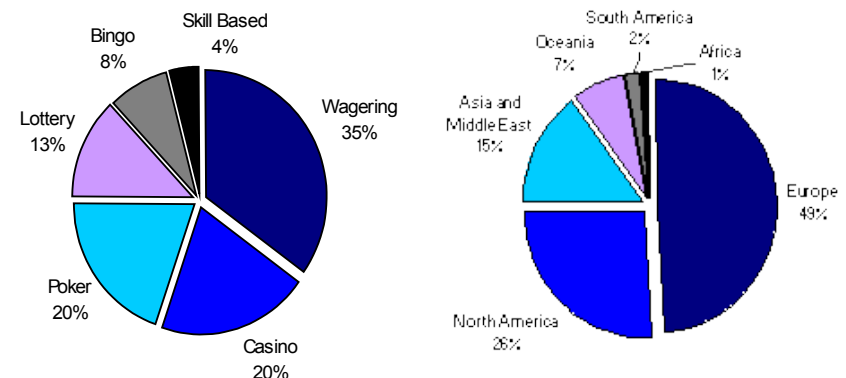
Skill based games avoid many US restrictions

- Although a small subsector within online gambling, games of skill avoid many of the legal/regulatory restrictions of most US states and international markets

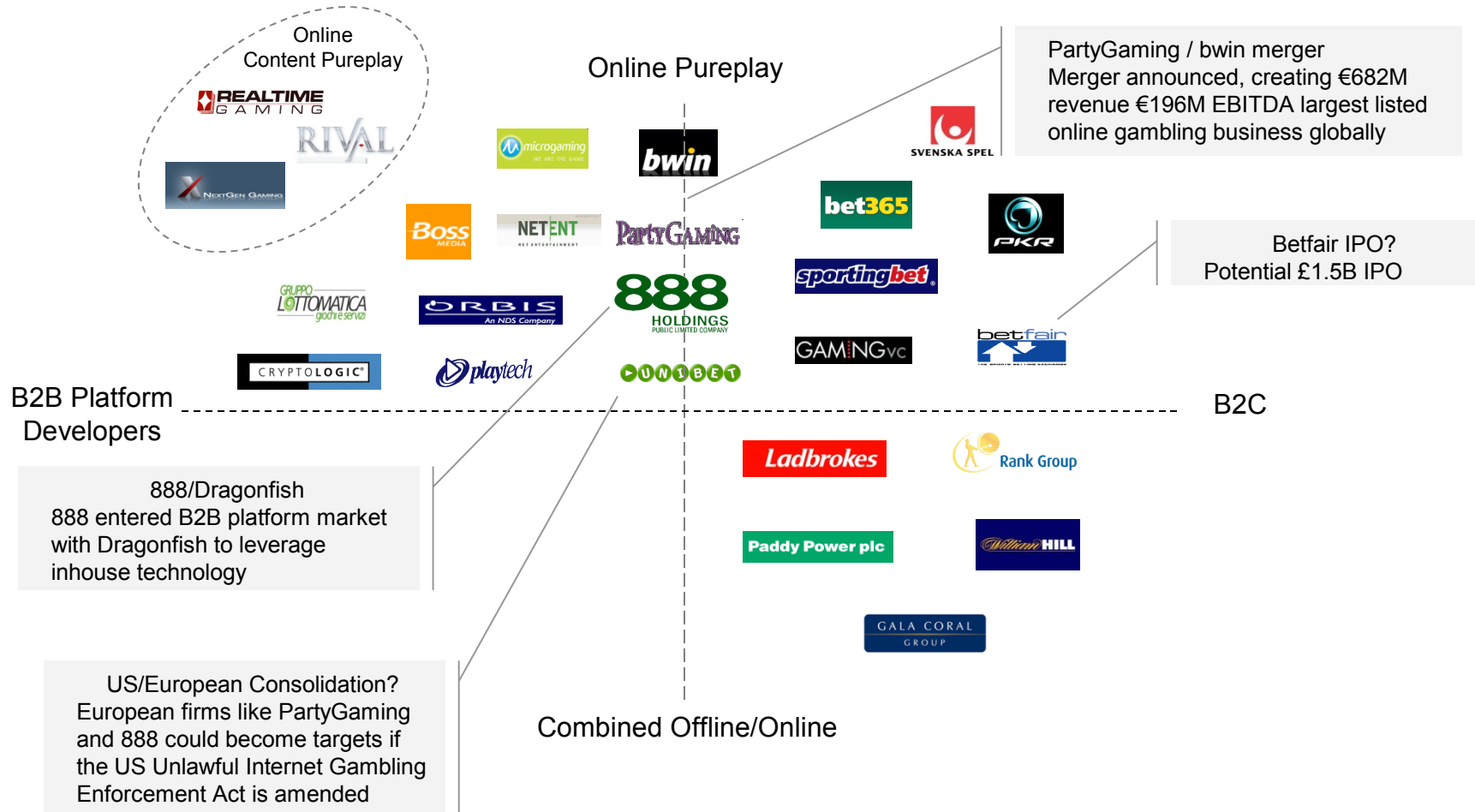
Global Online Gambling Revenue (\$B)



Market share by game type and region



Sector dynamics and growth are leading to consolidation



Skill based games avoid many regulatory challenges

Skill based games are similar to gambling

- Online betting games, but where the outcome is determined by players' skill rather than chance
- Games include arcade, puzzle, word, trivia and other skill games
- Business models are based on:
 - Scaled commission fee ("rake")
 - Entry fees for tournaments
 - Interest on players' funds invested
 - Micro-transactions
 - Players can also play non-gambling versions of most games for free
- Independence from advertising revenue reduces cyclical risk

But avoid many regulatory challenges

- Skill games are by definition not games of chance, which enables them to operate in many US States, European and Asia-Pacific markets
- Legislation has been introduced in the US to attempt to legalise online poker (20% of the gambling market globally), but the situation remains unresolved

The market continues to grow

- King.com launched in 2003, with more than 350M games played in January 2009. The website is available in nine languages, and includes skill game versions mainstream TV properties such as "American Idol" and "Deal or No Deal"
- Established, profitable business models
- Games are developed both internally and by third party developers
- The skills based market tends to target women over the age of 35, similar to the bingo market

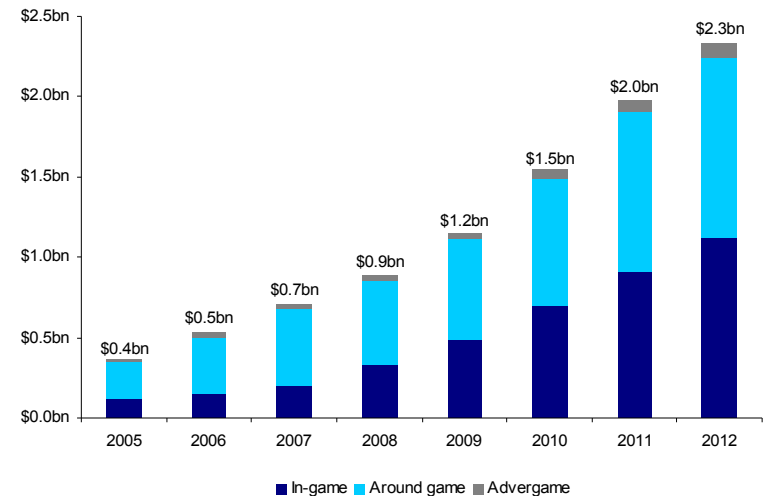


In-game advertising is early stage

In-game advertising is small but growing

- In-game advertising is seen by publishers as an additional revenue stream to traditional game sales
- In-game advertising delivers targeted advertising
 - Console: 68% male, median age 26
 - Casual/social: 50% male, median age 36
 - Mobile: 64% female, median age 31
- Global market > \$1B revenue, 12.9% CAGR forecast 2009-2014
- Multiple formats (static and dynamic):
 - In-game
 - Around-game
 - Advergames
- Online formats hold the greatest potential, whether via console (Xbox Live Arcade, Playstation Network), web or mobile, because of the ability to dynamically target and update in-game advertising
- All Microsoft Xbox 360 game advertising must use Microsoft's Massive Inc.
- Sony PS3 in-game advertising is open, with players such as IGA and Double Fusion partnering with Sony and major game publishers
- Google Ad-Sense for Games focuses on casual/social web games, with a view to expanding to console games

US Online PC games advertising revenue by category



Relatively few firms

Corporate



Independent



Online in-game advertising: static or dynamic media advertising that appears inside the game or during the game while its being loaded or played

Online around game advertising: static or rich media advertising that appears outside of the videogame but shown in conjunction with it

Online advergames: custom made games specifically created to communicate a marketing message designed around a product or service

Contact details

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