FY2024.Q2 Earnings Announcement
Q&A (Summary)

Date: November 8, 2024 (Fri)

IMPORTANT: PLEASE READ THE FOLLOWING STATEMENT

For your reference, below please find an English summary of the question and answer session for the financial results for the second quarter ended September 30, 2024, which was conducted in Japanese.

This English summary, which is intended to replace the simultaneous translation of the question and answer session previously provided, is not intended to be a direct translation of the question and answer session. As a result, there may be some differences between this English summary and the simultaneous English interpretation provided at the question and answer session.

Questioner 1

Q: [I&SS segment] Regarding the downward revision in your full-year forecast. While the overall market is showing signs of recovery, you mentioned a downward revision in the sales plan of a major customer, so what is the outlook for the next fiscal year and beyond? You have explained that the trend of larger sensors for mobile products is a tailwind, but is there any risk related to the concentration on the major customer?

A: Although the market is recovering, we view it as very gradual and stable recovery. For this fiscal year, we downwardly revised our forecast in line with a major customer production adjustment. However, production adjustments occur for various reasons, and we carried out this adjustment as part of ordinary business practices. Therefore, we don't see any change in our outlook for the next fiscal year and beyond.
Also, the risks presented by a concentration on a major customer are not new, so we think it is important to refine our technology and have it used by a variety of customers.

Questioner 2

Q: [G&NS segment] What is the current state of your live service games? There have been two extreme results, Helldivers 2, which was a huge hit, and Concord, which was shut down. How do you see the current situation, including how to successfully manage development within your portfolio?

A: There are some aspects of new IP that cannot be understood until we try them, but there are some points that we should reflect on, such as the fact that we should have verified at an earlier stage when to implement user tests and internal evaluations. Also, due to a level of organizational fragmentation, the coordination of planning, development, and sales across the organization were not always carried out smoothly.
Looking to the future, it will be necessary to select the most appropriate windows for first-party titles and third-party titles, and conduct title launches in a way that allows us to maximize our profits and avoid cannibalization within our platforms.

Questioner 3

Q: [Music segment] There were reports that Sony acquired the music publishing rights to the works of some artists. I think that the music publishing business can be expected to generate stable income and synergy effects with your other entertainment businesses, but what role do you expect it to play within the Group?

A: Catalogs are expected to provide a stable source of recurring profits. We can create stable returns and generate upside by pursuing various opportunities for their use. By additionally acquiring what are called NIL (Name, Image and Likeness) rights, such as portrait rights and images around the IP, we can also expect to extend its use across the Group. We aim to keep a disciplined approach and continue to explore opportunities to acquire music publishing rights. Currently, particularly in the streaming market, the generation using streaming services is shifting to mature generations. Songs from evergreen music titles are being listened to a lot, and they are very important assets for us in such an environment. Also, having evergreen catalogs shows our commitment to the artists. We think it will have a positive ripple effect on our entire music business, including A&R activities.

Questioner 4

Q: [G&NS segment] Is the annual PS5 hardware unit sales forecast for this fiscal year being maintained at 18 million units? With the launch of the PS5 Pro and some people suggesting that it may be difficult to reach a wide audience due to its price tag of nearly 120,000 yen, could you also provide figures on the sales plan for PS5 Pro for this fiscal year?

A: We are maintaining our annual PS5 hardware unit sales forecast at 18 million units. For the first half of the fiscal year, sales for the first quarter were weaker than projected, and the sales for the second quarter were almost in line with our projections. Our forecast for the second half of the fiscal year is based on an assumption that we will implement a certain level of sales promotion. Also, in the first half, we were able to achieve this sell-through without price reductions, as was the case with the PS4 generation, so we think that it is reasonable to maintain our annual forecast at 18 million units. Furthermore, the number of PS5 Pro unit sales is included in our unit sales forecast. However, since PS5 Pro hardware has been targeted at high-end core users, it is not a large part of such forecast. We have received many opinions about the price, but so far, we have strong impression of the sales situation of PS5 Pro compared to the pre-order status of PS4 Pro in the same period, and we have not found that the price has a negative impact on our projections for the PS5 Pro unit sales.

Questioner 5

Q: [I&SS segment] Your production is running at full capacity, so I believe that you will adjust it to align with your revised forecast. How much time do you plan to do that? Has your forecast for inventory levels changed?

A: We are currently at full capacity, and for now we anticipate remaining at full capacity over the third quarter as well. We believe that adjustments in production levels will result in a somewhat higher level of inventory at the end of March compared to our August forecast, but for now we believe that holding back on making significant changes to our production capacity will suffice in terms of adjusting our inventories.

Q: [ET&S segment] You say that your revised forecast for the imaging business reflects a more cautious view. Did you only update your outlook on the imaging business, or did you leave your forecast unchanged as a result of revisiting your outlook for the segment as a whole? If you made upward or downward adjustments of different magnitudes depending on each business, could you share what those were?

A: The television market has worsened slightly in China, but there has not been much change when we view the worldwide market. Logistics costs have also risen slightly, but we have reflected that risk into our current forecast. Our forecast also reflects risks in the imaging business such as higher costs for expanding sales and lower volumes in the Chinese market. That said, our August forecast incorporated risks across the entire segment to some extent, which is why we have maintained our forecast.

Questioner 6

Q: [G&NS segment] I believe that, excluding the impact of foreign exchange rates, profits for the second quarter grew by around 85 billion yen. Could you tell us what the individual contributions to the increase in the profit of hardware, third-party software, and network services were? Also, I believe that hardware turned profitable in the second quarter, but what led to the improved profitability? Lastly, does your plan assume that you will use the amount by which you outperformed in the first half to allocate additional marketing and promotional costs in the second half?

A: We do not disclose figures for individual factors of profit growth, but contribution to profit growth has been made in the following descending order; hardware, third-party software, and network services. Our hardware profitability improved because we benefitted compared to the same period of the previous fiscal year ("year-on-year") in the second quarter from the transition to the new model of PS5, making for a more favorable cost structure. However, since we released the new models in the third quarter of the previous fiscal year, we do not expect this second half cost structure to change significantly year-on-year. Partly because of an improvement of average sales price, we expect hardware profitability to improve year-on-year over the full year. On the other hand, while we do not believe we are being excessive in our budgeting of marketing and promotional costs, we anticipate a certain amount of such costs in the third quarter since we plan to have the highest shipment volume in the third quarter. Therefore, in comparison to the first half, there may be a temporary appearance of a deterioration in profits in the second half.

Q: [G&NS segment] You seem to have a lot of PS5 exclusives in your lineup of third-party software titles for the second half. Is that intended to encourage the transition from PS4 to PS5? I think that there is a risk of more users opting for PCs. What do you think about the risk and opportunity?

A: We are in the latter half of the console cycle for the PS5, and the number of PS5 titles has been increasing. We have also confirmed internally that the transition of users from the PS4 to the PS5 is trending well. In addition, we see users tending to purchase more software when they switch to the PS5, which we see as a positive. In terms of losing users to PCs, we have neither confirmed that any such trend is underway, nor do we see it as a major risk, so far.

Questioner 7

Q: [GN&S segment] You upwardly revised your full-year forecast for operating income by 35 billion yen. Can we understand that the forecast has only been adjusted to reflect the outperformance of the first half and the second quarter result to the initial forecast? Also, you have cited better hardware profitability as the greatest driver of your profit growth in the second quarter. If a more favorable cost structure has widened your gross margin, I think that would drive up your second half profits as well. Is it possible that it is not reflected in your forecast?

A: The strength that we saw in the second quarter is also for the most part reflected in our second half forecast. Improved hardware profitability was a greater contributor in the first half, but in thinking about the second half, we would like you to consider the balance between what I described earlier regarding the timing of the launch of the new models and the fact that we intend to engage in a fair amount of marketing spending in the second half. I personally hope that we may see a bit of additional upside in the fourth quarter, but it is difficult at present to say what is going to happen, and I believe that our forecast is generally fair.

Q: [Music segment] You say that lots of evergreen music is being listened to, but there was also a time when you were focused on the percentage of Sony Music artists in the hit charts of new songs. You had the market for new music in mind when you decided to step up your offerings of Latin American and indie music. Is this change of your explanation due to the change of the position of your business, or are you seeing an increasing preference for old music over new music in the music industry?

A: In major countries, the markets where digital streaming platform (DSP) is already widespread, the age demographic of listeners has shifted upward. Also, social media is exposing people to older music. These are among the reasons why we are witnessing a broad trend in the whole music industry in which evergreen music is accounting for a higher percentage of music consumption and being listened to more frequently. At the same time, a lot of music from emerging markets like Latin America and India is also being consumed, so we are keeping a close watch on such areas and acquiring relevant labels. We think it is fair for you to view it as a change in the overall market makeup rather than in listener preferences.
We invested a fair amount in establishing our catalog of evergreen music, so the fact that it is being consumed more than we had anticipated represents upside for us and is a welcome trend. It is not that older music is eating into the share of the pie for emerging-market music. We want to achieve upside by focusing on both.

Questioner 8

Q: [Music segment] The fact that streaming growth started to drop off around summertime, including at your competitors, has garnered a lot of attention. Do you view the slower growth as temporary or structural?

A: The growth in our streaming is stable, tracking in line with its trend to date. Multiple DSPs raised their prices prior to the first quarter of the previous fiscal year, and this fiscal year is no longer benefiting from the impact of the increased sales due to such price revision. In our Recorded Music business, audio streaming, which accounts for the majority of our streaming revenue, saw more growth in the second quarter than in the first quarter. By contrast, the growth rate in video streaming (ad-supported streaming) has declined, weighing down overall growth. Streaming growth rate has changed not as a result of structural change but as a result of a combination of these factors. DSPs are seeing growth in paid subscriber numbers, so we expect that there will be scope for price increases in the future.

Q: [I&SS segment] Previously, your second-quarter operating income margin was well above 20%, in part because of shipments to major customers. By comparison, your operating income margin in this second quarter seems somewhat low. Given your improved yields and full utilization, could you get your margins a bit higher? I believe that the average price of wafers was up even in dollar terms, but could you explain the dynamics, including in terms of wafer costs?

A: Our operating income margin was around 11.4% in the second quarter of the previous fiscal year and 17.3% in this quarter. The same period of the previous fiscal year's low margin was due in part to our being unable to ship as much as we would have liked due to the impact of our yields. The pace of our shipments has improved quite a bit this fiscal year, and our margins have been improved as well. We are spending a fair bit on R&D to develop image sensors for high-end applications, and our depreciation and amortization expenses is also up because of capital expenditure undertaken to increase our capacity. As such, while we have grown our sales, we have not necessarily been able to widen our margins, but we want to improve them going forwards.

Questioner 9

Q: [Consolidated] You upwardly revised your forecast for consolidated operating cash flow excluding the Financial Services segment by 40 billion yen. Other than operating income, what variables should we consider when we think about upside and downside for operating cash flow going forward? I suppose examples could include inventory, the G&NS segment network services receivables or working capital.

A: The upward revision is a reflection of the upward revision to our operating income forecast for the G&NS segment. Our operating cash flow has significantly increased year-on-year, but this is due to improvement in our working capital, especially at the G&NS segment. We think inventories are tighter than in the previous fiscal year as each of our businesses is exercising solid control, but we hope to continue to update our forecast, keeping a close watch on how the year-end selling season goes for the G&NS and ET&S segments.

Other than working capital, we think that there is nothing else that warrants particular consideration in the way of upside or downside. The precision and timeliness with which we build up our inventories ahead of the year-end selling season and then bring them back to normal is expected to have an impact.
