

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

GME - Q3 2013 Gamestop Corp. Earnings Conference Call

EVENT DATE/TIME: NOVEMBER 21, 2013 / 4:00PM GMT

OVERVIEW:

GME reported 3Q13 consolidated global sales of \$2.1b, consolidated global net earnings of \$68.6m and diluted EPS of \$0.58. Expects full-year 2013 EPS to be \$3.08-3.25 and 4Q13 diluted EPS to be \$1.97-2.14.



CORPORATE PARTICIPANTS

Paul Raines *GameStop Corp. - CEO*

Rob Lloyd *GameStop Corp. - CFO*

Tony Bartel *GameStop Corp. - President*

Mike Mauler *GameStop Corp. - EVP, GameStop International*

Mike Hogan *GameStop Corp. - EVP, Strategic Business & Brand Development*

CONFERENCE CALL PARTICIPANTS

Brian Nagel *Oppenheimer - Analyst*

Colin Sebastian *Robert W. Baird - Analyst*

Mike Olson *Piper Jaffray - Analyst*

Arvind Bhatia *Sterne Agee - Analyst*

Curtis Nagle *BofA Merrill Lynch - Analyst*

Anthony Chukumba *BB&T Capital Markets - Analyst*

David Magee *SunTrust Robinson Humphrey - Analyst*

PRESENTATION

Operator

Good day and welcome to GameStop Corporation's third-quarter 2013 earnings conference call. At the conclusion of the announcement, a question-and-answer session will be conducted electronically. (Operator Instructions).

I would like to remind you that this call is covered by the Safe Harbor disclosure contained in GameStop's public documents and is the property of GameStop. It is not for rebroadcast or use by any other party without the prior written consent of GameStop.

At this time, I would like to turn the call over to Paul Raines, Chief Executive Officer of GameStop Corporation.

Please go ahead, sir.

Paul Raines - GameStop Corp. - CEO

Thank you, operator, and welcome to the third-quarter earnings call for GameStop. As is our custom, we first want to recognize all the members of the GameStop family who are delivering the largest console launch in history around the world. They are the lifeblood of our Company, and we thank them for their hard work and service of our customers.

We also wanted to welcome all the new members to the family we have recently added. We are also pleased to announce that we will be closed on Thanksgiving DAY next week in the United States out of respect for our associates and their families. We will welcome customers starting at midnight for our Black Friday events.

Joining me today on our call are Rob Lloyd, Chief Financial Officer; Tony Bartel, President; Mike Mauler, Executive Vice President of International; Mike Hogan, Executive Vice President of Strategic Business; and Matt Hodges, our Vice President of Investor Relations.



What a quarter. The console videogame market returned to growth during the third quarter. And as we forecast, it is one of the most exciting categories in retail headed into the holiday season. Our comp growth of over 20% is the highest quarterly comp growth since May of 2008, and our earnings per share of \$0.58 exceeded our guidance and grew by 52.6%.

As we look at the business, a few key themes are emerging. The first is that GameStop is focused like a laser beam on the console launches. We have been working on these launches for over year. Our team has gone through intensive training on the features of the new consoles and our in-store experience reflects that knowledge level. Our supply chain has been tailored to fit the needs of our console partners and positions us well for holiday.

Tony Bartel and Mike Mauler will share some color around our strategy for success on console launches. As we like to say around the office, it's the console, stupid.

Another theme that is clear is that we will use our buy/sell/trade model to grow our share. Console launches offer a once-in-a-seven-year opportunity to reward customers with high value on their trades towards new hardware and software. We know from PowerUp rewards that if a customer buys their first console from us, it is very likely that they will continue buying software and accessories from us far into the future.

For that reason, we were aggressive this quarter on trade promotional activity to bring customers into our ecosystem with console launches. GameStop trade credits in video games and mobile devices totaled nearly \$300 million during the quarter, and most of that currency was used to buy new hardware and software.

Going forward, we believe trades will be the key to enabling consumer buying during holiday, and we are finding new ways to use them to our competitive advantage. Rob Lloyd will give you some more color on our preowned margin and how we expect it to return to normalized levels in his remarks.

On the digital and mobile front, we saw slower growth in the quarter, as our core gamers spent heavily on console software and hardware.

A final theme we are seeing is very strong growth in our omnichannel businesses. We have developed a unique hybrid of physical and digital sales, with online mobile and store channels working seamlessly to meet customers' needs. When coupled with our leading CRM programs and our Game Informer magazine, it is a powerful mix for holiday in the US and internationally. Mike Hogan will provide some color in his remarks.

Finally, a few thoughts on strategy. As many of you know, we began a strategic review of GameStop in early 2009 that identified the foundational elements of our current strategy. Those elements include best-in-class console execution and share, creation of an integrated CRM program, development of digital content sales at retail, mobile re-commerce, real estate excellence and capital discipline. As we sit on the cusp of a new console cycle, we continue to look forward and position GameStop for the next 20 years.

In the past, we have made acquisitions in the gaming space and successfully integrated them to drive new digital revenues. We have also been active in the mobile space through our GameStop stores. As part of our continuing strategic work, we have spent time in the past year studying the ways in which technology products are distributed to consumers outside the gaming space. We believe synergies exist with our model and it is clear to us that we have developed a platform of transferable core competencies for technology retailing at GameStop.

Our real estate group manages and understands thousands of ZIP Codes across America, with deep landlord relationships and leverage, particularly in secondary or whitespace markets. Our human resources function is able to create hiring and training events in any geography. Our refurbishment operations position us to be leaders in buy/sell/trade in video games, electronics and mobile devices. Our global PowerUp rewards loyalty program gives us deep data and insight around over 33 million consumers of technology products in stores and online.

Lastly, our capital process allows us to evaluate investments in specialty retail with precision and velocity.



So as part of GameStop's continuing evolution, I am pleased to announce today that we recently acquired Spring Mobile, a Salt Lake City-based exclusive dealer of AT&T Services. Spring Mobile owns and operates 152 stores in 14 states and is one of the largest authorized dealers in the AT&T network.

This acquisition provides GameStop an entry into the \$170 billion wireless market with one of the nation's fastest-growing operators. It also allows us to leverage our real estate hiring, buy/sell/trade and loyalty skill sets while adding significant executive talent in the mobile field to the GameStop team. We will provide more details on Spring Mobile in 2014.

We are also pleased to announce that we are carrying out a test of prepaid AO wireless stores in support of AT&T in several markets, and will give you color on those post-holiday.

Through our broad partnerships, we believe that our gaming brands can be supplemented with a group of technology brands that will leverage our strength in physical and digital retailing. We also see that these emerging brands give investors earnings potential that will be accretive to our core gaming brands.

I am pleased to welcome the associates of Spring Mobile and AO to the GameStop family. I will now turn the call over to Rob.

Rob Lloyd - *GameStop Corp. - CFO*

Thank you, Paul. Good morning, everyone. Let's dive right into the exciting third-quarter results. GameStop's consolidated global sales were \$2.1 billion, an increase of 19% from the prior-year quarter, with a comp increase of 20.5%. Our same-store sales significantly outperformed our forecast, beating the high end of the range by 550 basis points, and were driven by the strength of the major releases in the quarter, led by Grand Theft Auto V.

Our US comps were 23.1% and our international comps were 15.5%, led by Canada at 33.3%. New software sales increased 43.1%, including 47% in the US, compared to a 31% increase in the US market. Overall, we gained 550 basis points of new software market share in the quarter.

Our hardware sales grew 15.3% due to strength in the DS products. We outperformed the US market, leading to a hardware share gain of 690 basis points.

Preowned sales decreased 2% compared to the prior-year quarter. The US was down 3.7% and international was up 3.1%. Our preowned business lagged the overall videogame market, which is typical when a massive title launches during a non-holiday quarter.

Other sales decreased 5.2%, primarily due to comparing against the launch of two strong PC titles in the prior-year quarter. Our digital business increased 8.6% over the third quarter of last year, with over 40% growth in international. Our digital receipts or non-GAAP revenue totaled \$137.9 million, with GAAP revenues totaling \$46.5 million.

Our mobile revenues grew 14.4% from the third quarter of last year to \$49.9 million. We are on track to meet our growth targets for mobile in the year.

Consolidated global net earnings were \$68.6 million, an increase of 45.3% from last year. Diluted earnings per share for the quarter were \$0.58, up 52.6% from last year and exceeding our guidance range by \$0.03.

Overall, consolidated global gross margins for the quarter were 28.4% compared to 31.4% in the third quarter of last year. The primary reason for the decline was the shift in mix into new software. Gross margins on pre-owned declined from the same quarter of last year to 44.5% due to promotional offers made during the last few months to incent trades towards next-gen consoles. We were aggressive in our trade offers for preowned videogame products and mobile devices as we sought to provide customers with the trade currency they needed in order to make new consoles affordable and drive our share of the new console launches.

While our share gains in the past few years positioned us well for initial allocations, our goal is to grow share despite our retail competitors reentering an energized console market. Tony will share more about our successes on trades toward new consoles and the launches.

Our year-to-date preowned margin is 46.5%, and we expect to be in our normal range for the full year.

Gross margin on the other category was comparable to the prior-year quarter. Digital gross profit grew 16% to \$32.5 million. Mobile gross margins of 25.2% were also impacted by our aggressive trade programs over the past few months. In addition to driving trades towards new consoles, we were also aggressive about driving trades of mobile devices in a variety of conditions in an effort to increase awareness of our mobile device trade programs. Sellthrough of poor condition inventory impacted the margin rate for this quarter.

SG&A expenses were 21.3% of sales this quarter compared to 24.7% of sales in the third quarter of last year, as we leveraged the strong software sales in the quarter. Total SG&A expense dollars increased 2% this quarter from last year's quarter as we increased same-store sales by over 20%.

Depreciation and amortization was also down about \$3.1 million, or 7% less than the prior-year quarter. We ended the quarter with 6488 stores. We opened 9 and closed 27 in the US and opened 12 and closed 11 internationally. We still expect to reduce our store base by about 2% this year.

Inventory was up 4.3% as we head into the fourth quarter and launch new titles. As we've said in the past, the timing of new release software affects our AP leverage, which has returned to normalized levels.

We repurchased 1.8 million shares in the third quarter at an average price of \$51.37 for a total of \$94.4 million. Year-to-date, we have repurchased 5.2 million shares at an average of \$39.81 for a total of \$208.8 million. Life to date, we have repurchased 59.5 million shares at an average price of \$22.17 for a total of \$1.32 billion.

Since we implemented our aggressive and disciplined capital allocation program in January 2010, in less than 4 years, we have paid out over \$2 billion in share repurchases, dividends and debt repayments.

As we indicated in the earnings release, our Board of Directors raised our buyback authorization limit to \$500 million and authorized the fourth-quarter dividend of \$0.275 per share, to be paid on December 19.

Now we will look at the fourth-quarter outlook. For the second quarter in a row, we are pleased to be forecasting positive same-store sales, ranging from plus 2% to plus 9%. We are very excited about the console launches based on the strong sellthrough last week of Sony's PS4 and the anticipation around tonight's launch of the Xbox One.

We expect diluted earnings per share to range from \$1.97 to \$2.14. We are using weighted average fully-diluted shares outstanding of 118 million, following buybacks through the third quarter. We expect margin rates for the fourth quarter to be down 200 to 300 basis points because of increased sales of hardware.

Based on our better-than-expected third-quarter results and strong console demand, we are increasing our full-year comparable-store sales guidance from negative 3.5% to plus 1.5%, to a new range of plus 1.5% to plus 4.5%. We're also revising our previous full-year 2013 earnings-per-share guidance of \$3 to \$3.20, to a new range of \$3.08 to \$3.25, using weighted average fully-diluted shares outstanding of 119 million following buybacks through the third quarter.

Just a reminder to consider the \$0.08 per share impact of the 53rd week last year.

Now I will turn it over to Tony for his comments.

Tony Bartel - GameStop Corp. - President

Thanks, Rob. As Paul shared, we are laser focused on selling new consoles and related games and accessories this holiday season. After months of working closely with customers, platform holders and publishers, we are thrilled to be in the midst of the launch of the most innovative consumer electronics products this holiday season.

The excitement around both consoles is strong, as shown by both the sold-out launch of Sony's PS4 and the high anticipation of tonight's Xbox One launch.

We (inaudible) the console launch at our highest US market share ever for software, as we sold 52% of all 360 and PS3 software titles during the quarter. During the third quarter, we also attached software at a rate that is 2.2 times greater than that of our competition, so we are well-poised to ensure a large and profitable new console launch.

We invested heavily in our associates during the third quarter, including taking every one of them through a three-hour certification process on the two consoles. We know that they are the most prepared staff in all of retail to help consumers make a well-informed console decision and to make sure that they have all the games and related accessories to have a great gaming experience.

We had and are having midnight events in nearly all of our stores globally, and we are seeing strong consumer demand.

In addition to selling through all of our reservations and some additional allocation that we have received from Sony, we still have over 2.3 million customers on the first-to-know list, which indicates continued demand for months to come. Also, a survey of our PowerUp reward members shows that two-thirds of those surveyed expect to own a PS4 or Xbox One within the next 12 months.

According to our PowerUp reward customers, the number one concern around the console launch is affordability. So we have offered several unique trade-in programs to ensure that we are the most affordable place to buy the consoles and next-generation games.

Prior to the launch events, we hosted Sunday console days in all of our US stores to allow customers to play the new systems, talk about them with our associates and bring in their old devices for trades. Consumers responded well to this approach, as 43% of the new consoles were entirely paid off prior to launch, with over 20% of the reservation payments funded with trade credits. On average, new products are 14% funded by trade credits, so our unique buy/sell/trade model is solving the affordability question for our customers.

And with each console launching with over 20 new games, we are also the most affordable place for software as well. Working with Microsoft and our publishing partners, we are offering a \$9.99 trade-up offer to our PowerUp reward members who purchased a previous version game from us.

We are also working with Sony to allow consumers to trade up to a digital version of the next-generation game for \$9.99.

So how were the results? We have sold through all of our PS4 reservations and the additional allocation from Sony. Although we won't reveal the total amount of units for competitive reasons, our share was higher than on any previous console launch, and our sellthrough since launch was 80% higher than the total amount of PS3s that we sold in our 2006 fiscal year. Let me repeat that. Our sellthrough since launch was 80% higher than the total amount of PS3s that we sold in our 2006 fiscal year.

We are also pleased with the product flow that we are seeing through the balance of our fiscal year. As you are aware, Jack Tretton recently announced that there will be 3 million units sold in North America by the end of December, and we expect to sell a large portion of that.

We are running the same playbook with the Xbox One launch tonight, and the value of our reservations and additional allocation is 15% higher than the amount of Xbox 360s that we sold during our entire 2005 fiscal year. So we are poised for a powerful launch.

And as new product is available from the platform holders, we will be contacting the people on our first-to-know list to give them the first chance to purchase the new product.



Finally, several of our competitors have mentioned that they expect that there will be significant price discounting this holiday. While that may be true in other categories, we are confident that this will have a minimal impact on us because of the following reasons.

First, we believe the demand for the new consoles will outstrip supply for months to come, so we do not expect price discounting on the new platforms. Second, we have intentionally increased our market share and related PowerUp reward members to peak levels so we are better able to communicate our unique knowledge and value proposition and secure more allocated product. And finally, we have unique trade promotions against the new consoles and new games, making us the most affordable and profitable retailer to sell the new consoles.

So we are excited to have the most innovative consumer electronic products for the holiday season, the most knowledgeable associates and the unique deals to make the new consoles affordable, and we look forward to a strong holiday season.

With that, I will turn it over to Mike Mauler.

Mike Mauler - *GameStop Corp. - EVP, GameStop International*

Thanks, Tony. Good morning, everyone. GameStop's international businesses had a very strong third quarter. Driven by major new releases such as Grand Theft Auto V, solid digital growth and increasing preowned sales, we saw same-store sales increase 15.5% versus the prior year. This positive top-line growth combined with tight cost controls led to a 95% increase in operating earnings versus Q3 2012 to \$39 million.

I am pleased to say that this was the most profitable third quarter for the international business in our history.

A significant increase in new release reservations was a key driver of third-quarter sales, which were secured through the combination of exclusive content, unique collectors' editions and the value of our buy/sell/trade model. Providing customers with the opportunity to trade in games, used hardware and mobile devices has also made the next generation of consoles much more affordable to our customers.

During the third quarter, trade-ins increased 19% versus 2012, as customers took advantage of the opportunity to trade up to the next generation of upcoming new consoles. This increase in trades provides us with a healthy inventory position needed to support preowned sales during the holiday season.

Our investments in technology, CRM and improved vendor collaboration increased international digital receipts 42.6% in Q3 compared to the prior-year quarter. This was driven by strong growth in console DLC, the increase in sales of Steam Wallet cards in all markets and the expansion of Digital Game Informer subscription sales in Europe.

The improved collaboration with our publishing partners continues to positively impact DLC sales. The most recent example is Warner's successful new release, Batman, in October, where our international businesses drove an over at 30% attach rate on the digital season pass, with several markets surpassing a 40% attach rate.

During the third quarter, we accelerated our customer engagement investments in loyalty, e-commerce and Digital Game Informer. Our global loyalty program was rolled out to customers in Canada, Austria, Switzerland and Ireland. GameStop's powerful loyalty initiative now includes over 7 million members outside of the United States, and will continue to expand rapidly in 2014.

This growing database of passionate members provides us with the perfect resource to interact with our customers, drive revenue, increase reservations and facilitate interaction through a growing number of channels. As an example, in the third quarter, our international e-commerce business increased 51% versus prior year.

Our global loyalty program is the catalyst to engage our customers through a variety of channels, including social media, CRM emails, online forums, e-commerce, Game Informer magazine and now Digital Game Informer. With over 3 million subscriptions in the United States and a growing 430,000 subscribers internationally, Digital Game Informer is the largest digital magazine in the world and provides us with a unique opportunity to engage, inform and excite our customers worldwide.



As of two hours ago, the Xbox One launched in Australia/New Zealand, and in six hours, the next-generation Xbox will kick off in Europe, with the PS4 to come next week. With more reservations than in any previous console launch, we are very excited about the incredible opportunities over the next several years to grow the industry and our international businesses.

With the transformational investments made in recent years and best practice implementation, omnichannel technology and customer engagement, GameStop's international businesses are strategically positioned to leverage our leading market share as we launch the next generation of consoles. And now I will turn it over to Mike Hogan for his comments.

Mike Hogan - GameStop Corp. - EVP, Strategic Business & Brand Development

Thanks, Mike. I will give a quick update this morning on GameStop's omnichannel business, Game Informer and PowerUp rewards.

Omnichannel has a very significant impact on GameStop's total business, with over 60% of our customers going to GameStop on the web or mobile prior to making a purchase in our stores. In fact, for every \$1 of online sales, web and mobile are influencing more than 10 times that amount in-store.

Omnichannel sales continue to be a positive driver of total Company growth, posting 55% growth year-over-year in the third quarter. One key factor in this performance is the continued growth of the GameStop websites, which according to comScore, rank in the top 20 retail websites in terms of total traffic. And we are seeing double-digit traffic growth year-over-year.

The second key factor is the growth of our web and store business. When a product is not in stock or not available in a given store, consumers can still purchase the product from that store via GameStop.com, with free home delivery. This essentially provides enterprisewide inventory and prevents out-of-stocks. It also allows us to offer a broad variety of complementary items that are not practical to stock in all stores.

Web-in-store was introduced in late 2012 and will represent nearly 25% of our total omnichannel business for 2013. And we are experiencing explosive growth in mobile. We are seeing 67% year-over-year growth in mobile traffic.

We know omnichannel is driving total GameStop sales. 26% of GameStop.com visitors who do not buy online make a purchase in-store within 48 hours of their online visit. And 80% of surveyed customers say that they plan on visiting a store to purchase an item they saw on GameStop.com.

I want to transition briefly now to Game Informer and Power Up rewards. As you know, a significant component of our PowerUp rewards pro membership is the subscription to Game Informer magazine. And Game Informer Digital has become a key component of that customer experience.

The digital version makes possible a greatly enhanced experience for the US consumer, with embedded video and other digital features. But it has also made possible international expansion. As Mike Mauler mentioned, we now have Digital Game Informer in 12 additional countries outside the US. This would not have been possible with the physical magazine alone. And with nearly 3 million digital subscribers in the US, Game Informer Digital circulation is nearly as large as the next 24 US magazines combined. That is according to Advertising Age Magazine.

Our PowerUp rewards membership continues to grow and just recently passed the 26 million member mark in the US. This base of consumers now represents roughly one-third of all software sold in the total category in the US.

As you may recall, through our PowerUp rewards consumer panel, we are able to monitor key consumer trends, such as purchase interest of the new consoles. And as of September, as Tony mentioned, over two-thirds of PowerUp members surveyed indicated they expect to be playing on a PS4 or Xbox One within the next 12 to 18 months. This number continues to increase over time and reinforces our market model growth projections for 2014 and 2015.

I will now turn it back over to Paul.



Paul Raines - *GameStop Corp. - CEO*

Great, thank you, Mike. Before we turn the call over to Q&A, I just want to extend an invitation to all of our New York-based investors and analysts to our Xbox One launch event tonight at our Union Square store at 32 East 14th Street in Manhattan. We would love to show you what an authentic console launch experience looks like at GameStop. So please join us.

And with that, operator, we will turn the call over for question-and-answers.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Brian Nagel, Oppenheimer.

Brian Nagel - *Oppenheimer - Analyst*

Hi, good morning. So my first question, I just want to dive a little deeper into the used margin in the quarter. You gave some commentary in your prepared remarks, but just so we understand the mechanics, is -- the pressure on the used margin does that come as you are making -- as you are actually taking these trade-ins, or is it coming when you subsequently sell that product?

And then the decision to get more aggressive, I guess, on the trade-in effort, was that planned ahead of time, or was it potentially a response to maybe something you had seen in the competitive environment?

Paul Raines - *GameStop Corp. - CEO*

Let me start off with sort of the plans, and then Rob should go through some of the math on used margin rate -- and Tony may have comments for you.

We've -- one of the things that is very important to us is to have high share on these consoles. Our Company has been through several of these. We know the importance of the cycle. So going back over a year, we have wanted to maximize trying to get more allocation every day from the console makers.

For that reason, we have been focused on trade promotion for quite a while here, trying to get people into our reservation file and our first-to-know list. So I would say this has been something we have been going at awhile. And as share data becomes more apparent -- and we have to let Sony and Microsoft lead on that -- but I think investors will see how dominant GameStop truly is on these launches. And that has really been going on for a while.

A reaction -- really not much of a reaction here. You really can't react short-term. Tony, is it fair to say?

Tony Bartel - *GameStop Corp. - President*

I would clearly say that this was a calculated effort for us to go and to get market share ahead of a launch period, which is exactly what we did.

Paul Raines - *GameStop Corp. - CEO*

The world sort of forgot about consoles for a long time, but we haven't. And Rob, you want to go through sort of the math on the used margin rate?



Rob Lloyd - *GameStop Corp. - CFO*

Yes, you know the consoles were formally announced at E3 at the beginning of June, at which point GameStop started to take reservations. That is an earlier process than we have ever had before in terms of reservations toward new consoles. We have never had that much lead time.

We were, as Paul and Tony said, aggressive about our trade program. So what you start to see is the inflow of inventory with the trade offers that we were making. And then over the course of time through the third quarter, you start to see that inventory turn around and flow out in terms of sales. That impacts the margin rate.

So the margin rate in and of itself would not change based upon what flows in and is in our inventory. It is when it starts to sell through that you see that. And so it is not, again, just something that we started this quarter. It wasn't started in reaction to what we were seeing in terms of trends. We went out of the gates very aggressive in terms of driving reservations on the consoles. The trade-in program was a big part of that process. And we continued through the last five months to be aggressive on driving reservations, because we want that allocation from the console makers.

Brian Nagel - *Oppenheimer - Analyst*

Got it. So as a follow-up to that, Rob, you mentioned in your prepared comments -- I think -- correct me if I am wrong -- but you said in the fourth quarter, you should see that used margin snap back to the more normal levels. So does that then suggest that you are changing the prices at which you take trade-ins or have you worked through the inventory? Basically, how should we think about the puts and takes of that?

Rob Lloyd - *GameStop Corp. - CFO*

Well, again, as we have always said about our preowned inventory program, we have control of the buy side and the sell side pricing on that. So as far as what we do going forward, it will be a combination of both of those levers, if you will, that will have us return more to the normal range that we have always had.

Paul Raines - *GameStop Corp. - CEO*

And holiday traffic, Brian, you know plays a role in this, and we anticipate to have fairly healthy traffic given the new consoles and so forth.

Brian Nagel - *Oppenheimer - Analyst*

I just have one more question and then I will turn it over to someone else. You have taken a lot of trade-ins from the preowned -- on the preowned machines in anticipation of the launches of the new machines. How should we think about that relative -- in conjunction with kind of the weaker sales in used then?

Paul Raines - *GameStop Corp. - CEO*

Maybe you want to say we certainly have a lot of faith in the used business in a new console cycle. Maybe Mike Hogan, you want to share with the history tells us about preowned in a new cycle?

Mike Hogan - *GameStop Corp. - EVP, Strategic Business & Brand Development*

Sure. I think one of the things we have seen in the past is that with each introduction of a new console, preowned growth actually accelerates post that. And one of the reasons is because it provides you great value. These are going to be very attractively priced, so assumes attractively priced

games. And so in anticipation of that growth, we think that the opportunity to get some additional inventory is a great thing. So we think that will help feed the growth coming.

Paul Raines - *GameStop Corp. - CEO*

As the category reemerges as an innovation category, that makes the audience bigger, and it draws people into gaming who have forgotten about it and maybe were thinking about tablets or something else. Those folks, not all of them can afford a brand-new console and they will buy used to participate in the category.

Brian Nagel - *Oppenheimer - Analyst*

Thank you.

Operator

Colin Sebastian, Robert Baird.

Colin Sebastian - *Robert W. Baird - Analyst*

Great, thanks very much. A quick follow-up on the preowned margin questions. It sounds like there is a cyclical element to this. And I think I asked about this on the last call, but why wouldn't it be logical to assume that the preowned margins remain a bit lower for a period of time at least, just given the mix shift to higher-value next-gen software, where maybe that having both sides of the trade -- it doesn't give you as much flexibility?

And then secondly, Paul, back to the comments on technology retail and leveraging your assets, that brings up the point of Simply Mac, which I don't think you mentioned in the script. But I'm curious if there is any interest in acquiring the remainder of that Company.

And then more broadly, if you can talk about synergies beyond the back office between GameStop, Spring, AO and Simply Mac perhaps sharing a footprint or floor space, anything like that. Thanks.

Paul Raines - *GameStop Corp. - CEO*

Maybe, Rob, do you want to -- or you and Mike want to talk about the cyclical of the margin rate? I am not -- the one comment I would make on it, Colin, is it's all about the consumer size. It is not a fixed consumer base. People come into the category as it drives innovation, and that plays a big role. But anything you want to add to that?

Rob Lloyd - *GameStop Corp. - CFO*

Yes, Colin, what happens within the preowned margin categories, if you will, or the preowned categories is that the newer stuff tends to have a slightly lower margin rate on it than the older stuff does. You are going to see that the newer stuff is going to -- by that, I mean these consoles that are just now launching and the related software -- you are going to see that that business is going to grow over time, but predominantly it is going to be driven by what is already happening and what trades are coming in on the last-gen PS3 and Xbox 360.

So we are not giving guidance for 2014 yet, but based on history, we still expect to operate preowned within the parameters of what we always have.

Paul Raines - *GameStop Corp. - CEO*

And then as far as Simply Mac, Colin, yes, we are pleased to announce that we did complete our transaction and we own 100% of Simply Mac. And in fact, Steve Bain and the team from Simply opened up their 19th and 20th stores this week -- I think it is Missoula, Montana and Lubbock, Texas. So any investors who are based in those cities, you will have a beautiful Simply Mac store to go shop.

As far as synergies, we mentioned them. We see ourselves as having built this platform that includes real estate, talent management and training, buy/sell/trade, PowerUp rewards and capital and many others.

As far as the real estate synergies, there are multiple synergies. Marc Summey, our Senior VP of Real Estate, has identified a real long list of targets and locations where we have adjacent opportunities on the same pad, in the same mall.

If you go to Shreveport today, you will see that the GameStop and Simply Mac are very close. If you go to some of our other locations, you will see that we are leveraging our landlord relationship.

So it is very early, and yes, it is -- there is a significant real estate opportunity between the AO, Spring Mobile and Simply Mac businesses with GameStop.

Colin Sebastian - *Robert W. Baird - Analyst*

Okay, thanks.

Operator

Mike Olson, Piper Jaffray.

Mike Olson - *Piper Jaffray - Analyst*

All right. Thanks. There was some discussion earlier about the relationship between new and used sales at the beginning of a console cycle. And I think in the last cycle, you saw preowned sales increase by something like more than 20% in the first couple years of the cycle. Is there anything different about this cycle or anything you can say about what we should expect for preowned growth as we look into 2014 and 2015?

Paul Raines - *GameStop Corp. - CEO*

Yes, let's let Mike take you through some of his thoughts on that, because he has done a lot of modeling.

I would also encourage you to remember that PowerUp rewards is a bit of a game-changer on this and it has demonstrated some really different behaviors in terms of our ability to gain share of wallet. But Mike, you want to talk about that?

Mike Hogan - *GameStop Corp. - EVP, Strategic Business & Brand Development*

Sure. I think -- and I think we've talked about this before. If you go back and look at the last several -- if you look at the last several launches, we had a situation where obviously as consumers trade into the new console, they are trading in their old games. And so we do see -- I don't know if we see cyclicity in margin rates, but we certainly see cyclicity in terms of demand.

And so what we would be expecting is a fairly large quantity of consoles and games flowing in as consumers trade up to new, and we think that provides a great opportunity for us to offer a great value for new consumers, as Paul mentioned earlier, who are trading up to a 360 or to a PS3.



So although I don't think we have given out any sort of specific numbers, we certainly feel very optimistic about the opportunity to draw more consumers into the category with preowned. We think there is a great opportunity to offer great value, and we would expect to see an acceleration of growth.

Paul Raines - GameStop Corp. - CEO

And remember that we have always said the used business is an opening price point business. Because video gaming has this map pricing, we often don't think of it as an assortment of good, better, best, because there is just one price on new software.

But what GameStop created years ago is the opening price point business. And so there are consumers who will emerge who are opening price point consumers, who love the idea of console gaming, but don't have the money for a brand-new copy and a brand-new console. So that is the dynamic that will play out over the next couple of years.

Mike Olson - Piper Jaffray - Analyst

Okay. And then are you experiencing more mobile competition that could impact that business? There continues to be some new entrants in the space from time to time. Were you pressured to do more aggressive promotions there, which may have impacted mobile margins because of more competition in the space, or were you just doing them to kind of drive share gains?

Paul Raines - GameStop Corp. - CEO

I will let Tony -- Tony runs that business for us. But one comment I would make about the mobile business is we were early in that. There are a lot of new entrants into it. But we continue to be uniquely positioned in terms of our retail footprint and our refurbishment capabilities. And our play is how do we continue to leverage that and bundle it with video game promotions.

But Tony, you want to talk about mobile promotions and trades and so forth?

Tony Bartel - GameStop Corp. - President

Absolutely. I think the number one issue that we continue to face is awareness of that. So new entrants actually drive awareness of the overall business, and that is a very positive thing for GameStop. So we did not see any increased amount of discounting in that. We did -- as Rob mentioned earlier, we were very aggressive on the trade side of the business.

But we see it as a very complementary business. We see it does bring in some new customers, but a lot of the customers that do come in and buy mobile are the same customers that are coming in. Obviously, we wanted to build inventory for the large amount of holiday traffic that we expect, as we sell a lot of new consoles this holiday season. So we feel like we are well-poised for that.

Mike Olson - Piper Jaffray - Analyst

Okay, thank you.

Operator

Arvind Bhatia, Sterne Agee.



Arvind Bhatia - *Sterne Agee - Analyst*

Thank you very much. Just a couple of questions here, guys. One, I wanted to see if you could give us a sense of what you are seeing in tie ratios for the PlayStation 4 so far, and maybe compare that to what you saw early on either for the 360 or the PlayStation 3.

And then also, the 20% to 30% industry growth guidance you guys -- or not guidance -- but how you guys think about the industry for next year, is there any change in your thought process? Are you guys more comfortable with that kind of number as you now have more visibility? Then I have a follow-up.

Paul Raines - *GameStop Corp. - CEO*

Rob, do you want to take the tie ratio question?

Rob Lloyd - *GameStop Corp. - CFO*

Yes, I think it is a little bit early for us to talk about tie ratios. I think we are pleased with what we see so far. It has just been a week on the Sony side, and of course, the Xbox tonight. So I think we will have more color around that when we talk about -- or when we release our holiday results, I think.

Paul Raines - *GameStop Corp. - CEO*

One thing, Arvind, to -- and I will ask Tony to share some color with you. But one thing to look at, we have been saying for a while that these consoles will include a lot more digital content than any previous console. And that has played out with PlayStation.

If you were in our store the other night for the PS4 launch you saw that we were aggressively marketing a lot of digital content and network access but that is going to be a big part of Sony's future, that network is going to grow significantly. Tony, any color you want to add to that?

Tony Bartel - *GameStop Corp. - President*

Sure and we are working very closely with Sony to make sure that we partner with them and giving them the consumer feedback and working closely to make sure that we have a great product there. But our associates, part of their training was to make sure that when people open that product up or as people went to use it, they had a great experience.

So what we saw is that when you look at all of the PlayStation Plus subscriptions that we have sold in our lifetime as a Company, we have been selling them for years, a full one-third of all subscriptions we have sold in our lifetime were sold in the last seven days at GameStop. So that shows you the strength of attach that was over a third of the products went out with attach on that and that is growing daily as we have customers coming back in our stores on a daily basis to pick up PlayStation Plus.

Paul Raines - *GameStop Corp. - CEO*

So attaching digital content is a big part of this as well as software. Mike, the model, category model, anything you want to add to that?

Mike Hogan - *GameStop Corp. - EVP, Strategic Business & Brand Development*

Sure. So as you know, we have the category model; then we updated periodically. The last iteration we had, we were projecting between 20% and 30% console category growth in the US for next year, for 2014.

The model is built from a number of different sources, it takes in kind of a lot of different variables. What I will say is that the limited amount of data that we have here -- because it hasn't been very long -- is certainly positive and consistent with what our expectations are.

At the time we built the model, we had projected a new console cycle that is slightly smaller than the last one. We were being conservative to account for things like the effect that the Wii had in the last cycle; doesn't include things like handhelds and preowned and so on.

So our category model right now, we'll probably be updating it sometime after the first of the year. But all the data we have right now is pretty consistent with what our expectations were a few months ago.

Paul Raines - *GameStop Corp. - CEO*

Arvind, you had a follow-up?

Arvind Bhatia - *Sterne Agee - Analyst*

Just we had heard some stories where some of the recent big launches, like Call of Duty, et cetera, Battlefield, they were trending initially down, as I think it was assumed that consumers were delaying purchases for the next gen. I just wanted to see if you guys have any thoughts on how you see the full picture for the quarter. Meaning you had the \$9.99 upgrade program. When we combine existing gen and next-gen sales of some of the big properties this holiday quarter, how do you see the trend?

Paul Raines - *GameStop Corp. - CEO*

Yes, Tony will talk a little bit about what he is doing with trades. I would just say that there is a lot of noise in the business right now. We are launching Xbox One tonight. There is a lot of customers -- I talk to a lot of gamers, a lot of gamers trying to make decisions. They have so many options. So there is a little bit of noise in the system. Tony, what do you want to add to that?

Tony Bartel - *GameStop Corp. - President*

Sure. And we knew that coming in, so that is why we have the \$9.99 trade offers. And those have been very successful for us, and it is unique way for us to sell. So we will continue to do that.

I would echo Paul's thought that there is dissidence on exactly which console they are going to play it on, and I think that is going to sort itself out in the next couple of weeks, as people see the flow of consoles and see how strong the demand is for these two consoles.

Paul Raines - *GameStop Corp. - CEO*

One thing is for sure, Arvind, if you are playing your PS4 like we are, it is a spectacular device. I mean, Xbox One will be spectacular as well. But when I can read LeBron's tats and see the wrinkles in his jersey, right, as well as I can with all the social features, these devices are going to have tremendous demand and tremendous consumer innovation.

Arvind Bhatia - *Sterne Agee - Analyst*

Great, thank you, guys.



Operator

Curtis Nagle, Bank of America Merrill Lynch.

Curtis Nagle - *BofA Merrill Lynch - Analyst*

Good morning, guys, and thanks for taking my question. Just one question and then a quick follow-up. Frankly, I was pretty surprised by the amount of leverage you guys got on the quarter. Of course, sales were quite good, but just on a dollar basis, they virtually were unchanged given a very big increase in sales. And I just was wondering what the puts and takes were and kind of how we should think about leverage going into 4Q.

And then just a follow-up. I was curious why digital sales weren't stronger, just given the number of AAA titles, particularly GTA, that sold and the high attach rates that go with them. So if you could comment on that, it would be very much appreciated.

Paul Raines - *GameStop Corp. - CEO*

Why don't we start with -- Tony, why don't you take the digital question first?

Tony Bartel - *GameStop Corp. - President*

Sure. On the digital sales, you even mentioned GTA V, which was by far the largest title in the quarter. GTA V did not actually have a day and date digital component to it, which we clearly had anticipated when we last spoke that that would. And so that is really deferred, because we clearly anticipate that digital content will come out on that, and we will participate in that. So that is more deferred revenue. And I would say that was probably one of the stronger elements of the lower digital growth that took place.

But like we said, the new consoles, that we do anticipate that they will be more digital and so we feel like our digital sales will expand (multiple speakers).

Paul Raines - *GameStop Corp. - CEO*

DLC for us is all driven by the availability of day and date. And as titles come through that don't have that, it winds up impacting that growth rate. Rob, leverage?

Rob Lloyd - *GameStop Corp. - CFO*

Yes, you know, we have kind of said all along that you get a great opportunity to leverage your cost base when you are in a console launch. The same thing applies, although to a slightly lesser extent, on a title launch, when you think of something like the magnitude of a Grand Theft Auto. You know, you are not going to staff the store exactly the same as you would on a normal Wednesday, but you are going to staff to make sure the customer experience is appropriate when you're open from midnight.

But then you start to think about the flowthrough of the hundreds of people in line at a store to get a Grand Theft Auto, and then the number of people that are in line at a store to get these launches that we are going through right now. And you really have a fantastic opportunity to leverage the cost structure.

So I am glad you noticed that. We work very hard to make sure that we are positioned to get the best that we can out of the leverage when we have these opportunities.

Curtis Nagle - *BofA Merrill Lynch - Analyst*

Great, thanks so much. I appreciate the commentary.

Paul Raines - *GameStop Corp. - CEO*

Thank you, Curtis.

Operator

Anthony Chukumba, BB&T Capital Markets.

Anthony Chukumba - *BB&T Capital Markets - Analyst*

Good morning. I just wanted to probe a little bit into the Q4 guidance. Because it just struck me as very, very conservative. I mean, particularly on the comp, 2% to 9%, I mean, you are going to be selling a ton of these PlayStation 4s and Xbox Ones at \$300, \$400.

And so I guess I am just trying to dig a little bit into that, because like I said -- I definitely get the mix in terms of the margins and obviously the consoles are significantly lower margin, but I guess that just struck me as conservative, particularly from a comp perspective.

Paul Raines - *GameStop Corp. - CEO*

Yes, Rob will give you some detail. I mean, we are -- the fourth quarter, there is lots of movement, there is some title shifts, there is 53, 52 week. We did launch a Wii U last year that was a pretty successful launch. There is a few things there. Rob, maybe you want to give him some detail -- Anthony some detail on how you modeled Q4.

Rob Lloyd - *GameStop Corp. - CFO*

Yes, we are very confident, Anthony, in how we have launched the PS4 so far, what we have on tap for tonight with Xbox One. But -- we know exactly what is sitting in our stores, but the visibility into what our allocations are going to be for the rest of the quarter, that is pretty cloudy right now.

So we wanted to make sure that we had a comp range to start with that reflected the unknown surrounding that. And then we wanted to make sure that we weren't overreaching in the expectation that we put on the console makers for what they are able to deliver to the system and specifically to us.

Anthony Chukumba - *BB&T Capital Markets - Analyst*

Okay, great. That is helpful. And then just one quick follow-up, sort of related, just to clarify -- you are assuming 118 million diluted shares outstanding for Q4. So that essentially assumes that you don't repurchase any stock in Q4. Is that correct?

Rob Lloyd - *GameStop Corp. - CFO*

As is typical when we give guidance, we base it on the share count that calculates off the quarter we just completed. So that is consistent, yes.



Anthony Chukumba - *BB&T Capital Markets - Analyst*

Okay. And then I mean -- but just based on the fact you just re-upped your share repurchase program, there is no reason to think that you wouldn't buy back stock in Q4, I mean, is there?

Rob Lloyd - *GameStop Corp. - CFO*

Well, no, we are committed to the buyback program. Re-upping the authorization is obviously a symbol of that. However, as we go into a quarter, given what the price might do -- and there has been some volatility in it this year -- it is tough for us to predict exactly what we might buy in terms of share count.

So our practice has been over the course of the past three years just to base it on what we know has been completed.

Paul Raines - *GameStop Corp. - CEO*

Yes, that is a standard practice Rob and the team take. I would also point out that we have been very consistent and are very committed to the share buyback program. Rob bought back a whole bunch of shares this quarter, and we like the characteristics of our program so far.

Anthony Chukumba - *BB&T Capital Markets - Analyst*

Okay, that's very helpful. Thanks a lot.

Paul Raines - *GameStop Corp. - CEO*

Thank you, Anthony.

Operator

David Magee, SunTrust Robinson.

David Magee - *SunTrust Robinson Humphrey - Analyst*

Good morning and congrats on the good numbers, guys.

Paul Raines - *GameStop Corp. - CEO*

Hey, we got a congratulations. Thank you, Dave.

David Magee - *SunTrust Robinson Humphrey - Analyst*

Somebody had to give it to you.

Paul Raines - *GameStop Corp. - CEO*

Highest comp since May of 2008, man.

David Magee - *SunTrust Robinson Humphrey - Analyst*

You know, the interest in the new consoles is very encouraging, and I guess the discounts that we all sort of attached to it versus the last cycle launch may not have been warranted. I am curious, as you look out 6 to 9 months from now, when you get through this initial gamer-centric demand, how do you feel about the visibility of the console demand at that point in time, past the initial rush? Are you feeling better about that at this point or is it just hard to say?

Paul Raines - *GameStop Corp. - CEO*

Mike is going to give you some modeling sort of stuff. I would just tell you playing the PS4, you can't help but think about the innovation level in that device as being around for a long time. Just all the social features, Ustream, PlayStation Live, all that stuff is really compelling.

Mike -- that is just an anecdotal, qualitative kind of thing. But Mike, what you want to share about that (multiple speakers)?

Mike Hogan - *GameStop Corp. - EVP, Strategic Business & Brand Development*

Yes, I think to that point, we have actually modeled the PS4 and the Xbox One -- yes, in our model, they were modeled less than last time, but pretty close. I think one of the reasons why the total number was down had more to do with the performance of the Wii. But everything we are seeing to this point is very, very positive.

I think we made the point earlier -- what PowerUp rewards does is it allows us to go inside and see what consumers are doing. It would be -- obviously it would be a mistake to take the number of PowerUp members and literally multiply it by the percentage. But anytime you are seeing a base of 25 million, 26 million people, and you are seeing a very, very high percentage, two-thirds of them, indicating very positive purchase interest, what it says to us is that the demand is very strong and it is going to take a long time for the supply to catch up with that demand.

So I think everything we are seeing suggests very, very strong demand, not only now, but for a fairly long period of time. Keep in mind that 26 million people in the program, a lot of those people are not just core gamers. We have a very, very broad segment of the population in there.

And then I think another point that Tony mentioned earlier is value. One of the things that we think is going to be a big deal is our ability to make the systems through our trade programs affordable for millions of people who couldn't otherwise afford them.

So between the demand, the (inaudible) value and hopefully a strong lineup of new titles coming out next year, we think there is a number of things that could continue to make the console demand strong for the foreseeable future.

Paul Raines - *GameStop Corp. - CEO*

And there is a lot of data that says if we sell you that console and get you into the GameStop ecosystem that you will be back, and that is something we have been focused on quite a bit.

David Magee - *SunTrust Robinson Humphrey - Analyst*

Great, thank you and good luck this season.

Paul Raines - GameStop Corp. - CEO

Thank you, David. Okay, with that, I believe we are at our time limit and we will wrap that up. Thank you for your support of GameStop. We look forward to seeing everyone in our stores at holiday and Power to the Players.

Operator

This concludes today's program. We thank you for your participation. You may now disconnect at any time.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2013, Thomson Reuters. All Rights Reserved.