

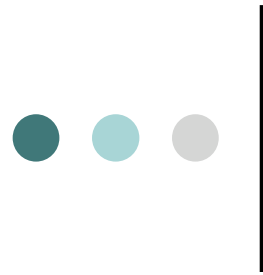


## ***Profitable Growth***

**The \$ and cents of growing a healthy studio  
OR**

***Vicarious Visions – A Series of Unfortunate Events***

***Karthik Bala, CEO  
Guha Bala, President***



# Purpose

- The game industry comprises some of the greatest creative and business talent in software and entertainment.
- However, game developers rarely sustain growth and manage healthy businesses.
- Recent years have seen the insolvency of numerous developers, and with it the death of many great creative ideas and innovative products.
- It is essential for continued growth of the industry that game developers measure and manage their studios as competitive healthy businesses as well as creative enterprises.
- We share some of the tools that helped us to grow VV ... could be helpful to you as well!

# About Vicarious Visions



- **A Leading developer of video games**
  - Developing games for console and portable markets
  - Headquartered in Albany, NY, with satellite office in Mountain View, CA, with 140 employees
  - Founded in 1994 by brothers Guha Bala and Karthik Bala
  - In January 2005, VV was acquired by Activision, Inc. – the second largest publisher of video games in the world
- **Market Success**
  - 19 million games sold worldwide
  - Generated nearly \$750 Million in retail sales!
- **Activision**
  - Founded in 1979 – one of the first video game publishers
  - Annual sales over \$1.4B US



# About Vicarious Visions

## History

- Started in high school – a hobby that became a business
- Incorporated in 1994
- Last fall, we had our 100<sup>th</sup> game title published!
  - Tony Hawk's American Sk8land for Nintendo DS.

## Multi-platform Development – handheld and console

- PlayStation 2, PlayStation 3, Xbox 360, Nintendo Revolution
- GameBoy Advance, Nintendo DS, PlayStation Portable

## Strong Entertainment Brands & Partnerships

- Shrek, Spider-Man, Star Wars, Tony Hawk, Spongebob, Finding Nemo, Doom 3 and many others.
- Dreamworks, Pixar, Disney, Lucasfilm, Sony Pictures, Marvel

## Our People

- Young, both creative and technical world class talent
- Diverse skill sets and backgrounds
  - Programmers, artists, writers, designers, musicians, producers
  - Recruited from around the world



# Humble Beginnings

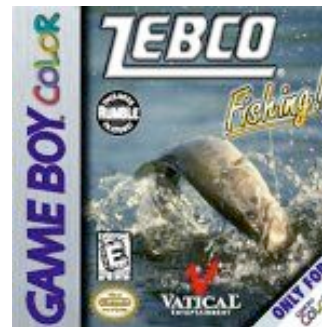
- Synnergist
  - Graphic adventure
  - High school project
  - Deliberately misspelled
- Published in 1996
  - Late - 1 year
  - Calls - none returned
  - Product - lots returned

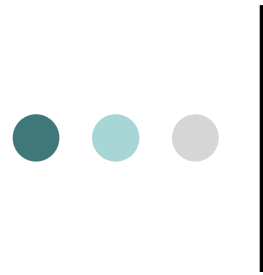


Key: To be a creative enterprise,  
we needed to run it as a vibrant  
business

# Our first break: 1999

- Small publisher
  - Regional distributor
  - Advent of Game Boy Color
- Started with Zebco Fishing GBC
  - Innovative - digital audio on GBC
  - Got the attention of Nintendo
  - First commercial success!
- Lead to multi-title GBC deal with publisher
- PSOne and N64 deals also in the works
- Sales and title growth into the horizon
- Used experience to land Spidey GBC - first high profile game
- Rosy picture!





# 2000: A bump, or a dive?

- VV on a roll
  - Rapid growth of staff
  - 15 to 40 in 1999
  - Speed prioritized over tightness of process
- Publisher hit a bump
  - Financing strategy did not pan out
  - Signed additional deals with VV - but how would they pay?
- Grim reality
  - Mid-2000 → publisher insolvent
  - 90% of our forecasted revenue
  - \$500K in uncollectible invoices
  - Credit lines tapped out - KB and GB personal guarantee - \$1M of bank debt
  - No immediate substitute business



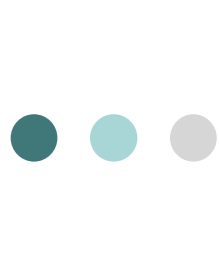
## Takeaway

# Cash the undisputed king

- Short term cash needs can cost you your business
  - Developers have limited access to capital
  - External capital in a time of crisis can come at a high cost
- Cash flow monitoring
  - Weekly and Monthly monitoring
    - Plan inflows, outflows
    - Peeled back all non-essential expenses and deferred payables where possible
    - Always paid rent and payroll on time!
  - Pressed on collections
  - Accelerated work where possible

	June		July				
	19-Jun	26-Jun	3-Jul	10-Jul	17-Jul	24-Jul	31-Jul
<b>Cash Inflows:</b>	70,000	80,000	65,000	185,000	400,000	30,000	120,000
	70,000	80,000	15,000		30,000		30,000
					40,000	30,000	30,000
					30,000		30,000
				125,000			30,000
			50,000	60,000	300,000		
<b>Line of Credit Borrowing</b>							
<b>Major Cash Outlays:</b>							
Payroll	110,375		110,899		127,430		109,730
Subcontract	18,000	18,000	31,000	10,000	105,000	4,000	19,500
Facilities		13,543		1,500			13,543
Employee Benefits		15,000		500		15,000	
Telecom & Internet		1,500	1,450			1,500	1,450
Payroll Taxes	9,000		9,000		13,000		9,000
Recruiting ( Relo& Placement)		11,000	13,000	4,000	700	1,000	2,000
Miscellaneous	2,000	2,000	27,000	2,000	2,000	2,000	2,000
<b>Total Cash Outflow:</b>	139,375	61,043	192,349	18,000	248,130	23,500	157,223
<b>Beginning Cash:</b>	226,718	157,343	176,300	48,951	215,951	367,821	374,321
<b>Ending Cash:</b>	157,343	176,300	48,951	215,951	367,821	374,321	337,098





## Takeaway

# Invest Early in Banking Relationships and Savings

- Establish banking relations early
  - Best time to get a line of credit is when you don't need it
  - Start small, and establish a borrowing and repayment history
- Caveats: bank lines are typically demand notes
  - Communicate actively with your bank
  - Make any scheduled payments on-time
- Plan a savings (untouchable reserve) account
  - Establish how much you need
  - Establish criteria for use
  - Don't touch it until these criteria are met

	safe	risky	risk neutral	very safe	
<i>Sales Cycle in months</i>		5	3	4	6
<i>Monthly Payroll</i>	\$ 362	\$ 362	\$ 362	\$ 362	
<i>Taxes available</i>	\$ -	\$ -	\$ -	\$ -	
<i>Non variable monthly expenses</i>	\$ 100	\$ 100	\$ 100	\$ 100	
<i>Bank line</i>	\$ -	\$ -	\$ -	\$ -	
<i>Customers payments</i>	\$ 118	\$ 118	\$ 118	\$ 118	
<i>Operating reserve</i>	\$ 1,720	\$ 1,032	\$ 1,376	\$ 2,064	

Takeaway

# Sales pipeline

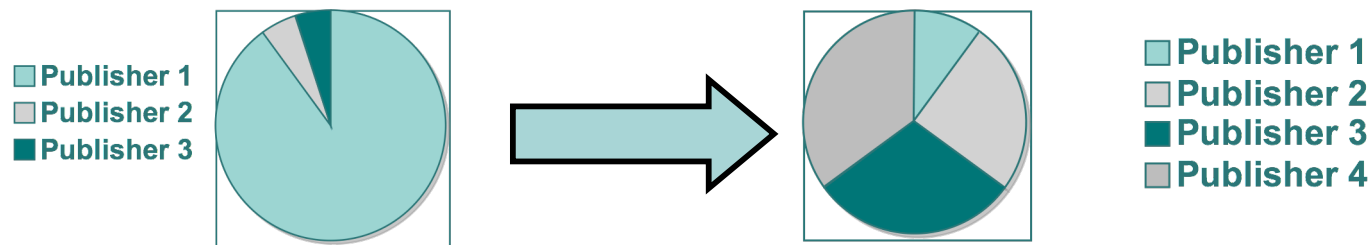
- Aggressive (but not desperate) sales
  - Projects that offered near term liquidity
  - Customers that were solvent
  - Marketed our strengths
  - Built on our consistent customer relationship efforts
- Sold projects that we could deliver!
  - Key to brand and reputation
  - Publishers wary with their first time developers
- Planned sales efforts around a probability rated pipeline

Platform	Opportunity	Certainty	Size	Impact
Console	ESPN SnoCross	95%	\$ 3,200	\$ 3,040
	Spidey 2 PSX	95%	\$ 1,200	\$ 1,140
	SnoCross DC	25%	\$ 500	\$ 125
	HydroCross Next-Gen	25%	\$ 2,000	\$ 500
	SnoCross PSX Sequel	10%	\$ 600	\$ 60
	HydroCross PSX Sequel	10%	\$ 600	\$ 60
	FreeStyle MotoCross PS2	10%	\$ 2,000	\$ 200
GBC	Wolverine GBC	50%	\$ 200	\$ 100
	Sponge Bob GBC	95%	\$ 130	\$ 183
	Mattel GBC	25%	\$ 250	\$ 56
AGB	Tony Hawk AGB	95%	\$ 400	\$ 428
	Acclaim AGB	10%	\$ 400	\$ 40
	Spiderman AGB	90%	\$ 400	\$ 360
	FreeStyle MotoCross AGB	50%	\$ 400	\$ 200
	Castlevania AGB	25%	\$ 500	\$ 125
PC	Infogrames AGB	10%	\$ 400	\$ 40
	SnoCross PC	25%	\$ 200	\$ 50
	Terminus	90%	\$ 400	\$ 360
Pipeline			\$ 13,868	\$ 7,067

## Takeaway

# Customer Diversity Increases Resilience

- Control your future: Avoid “being owned” by any single customer
  - You are owned if customer controls most of your revenues
  - Their risks are your risks, but not vice versa
  - Can’t walk away from a deal
- Customer diversity was key to go-forward plan
  - Increased our priority on multi-platform development → key to having a variety of customers
  - Marketed our work in GBC and Dreamcast
  - Replaced our single customer with several, each with a smaller share of revenue



**Key: No more than 40% with one publisher!**

2000

# So we made it through...

- Kept focus on operations, and delivered (Spidey GBC, early work on GBA)
- Sold new projects to **new** customers
- Started running several products in parallel for diversified customer base
- Paid down debt
- Promising pipeline of projects, including Tony Hawk 2 GBA
- Rosy picture!



2001

# Our First 1 Million Unit Seller

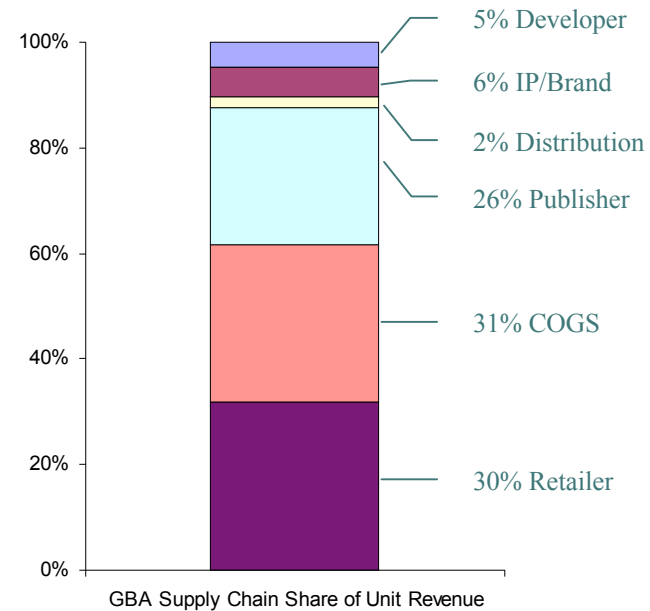
- Our first break-out hit
  - Leveraged it for brand developer → a leader on handheld
  - Build broad customer relationships
  - Strengthen the sales pipeline
  - Saved as much money as possible
- Focused our approach
  - Low cost provider **or** category leader
  - Choice not obvious for handheld/mobile developers
  - We chose category leader approach
  - Took on projects that allowed us to make high quality games
  - Turned down games that didn't

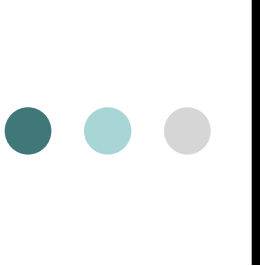


## Takeaway

# Getting better deals

- Chose between royalty earner or margin earner
- Modeled the product P&L from
  - Our various deal terms and royalty reports (cost breakdown)
  - NPD data (revenue)
- Allowed us to walk in the customers shoes
  - Identified opportunities to get more
  - Knew when to stop negotiating, and close the deal
- Did a per unit cost analysis
  - On a \$30 retail, where do the dollars go?





2002 - 2003

## Delivering is easier planned than done!

- Projects of varying shapes and sizes
  - Platforms, licenses, project lengths
  - 7 - 8 in parallel (GBC, GBA, PSOne, PS2, GCN)
- Reputation with customers → only as good as your last project
- Project tracking and management systems were basic → not suited for multi-project management
- Potential delivery crisis ahead!
- First step in delivery is **picking the right projects**
  - Became easier as our reputation developed
  - Prior tools helped with this: cash planning, savings, sales pipeline, and customer diversity
- Portfolio tool allowed us to think through risk/reward, so we didn't pile up the risk
- Most importantly helped us choose what **not** to take on



## Takeaway

# Portfolio Selection Tool

		Recruiting Risk	Design Risk	Tech Risk	Art Risk	Opp for Innovation	Notoriety	Royalty Potential	Margin Potential	Publisher Category	Total Risk	Total "Return"
GBA - Winter	<b>4 titles in house</b>											
	Shrek 2	2.0	1.0	3.0		2.0	3.0	4.0	3.5	5.0	6.0	12.5
	Crash 4	3.0	1.0	2.0		2.0	3.0	3.0	3.0	4.0	6.0	11.0
	Spyro 4	3.0	1.0	3.0		2.0	3.0	3.0	3.0	4.0	7.0	11.0
	DAFFO	3.0	2.0	3.0		3.0	2.0	2.0	3.5	5.0	8.0	10.5
GBA outsourced - Winter	<b>optional one title outsourced</b>											
	Nemo 2										0.0	0.0
GBA - Holiday 04												
	Shrek 2.5	2.0	1.0	3.0		3.0	3.0	4.0	3.5	5.0	6.0	13.5
	Sharkslayer	3.0	2.0	2.0		3.0	3.0	3.0	3.5	5.0	7.0	12.5
	Spongebob THQ										0.0	0.0
	Madden										0.0	0.0
New platforms	<b>NGage and PSP</b>											
	CNK NGage	3.0	4.0	3.0		4.0	3.0	2.0	2.0		10.0	11.0
	Riddick NGage	4.0	5.0	5.0		3.0	3.0	2.0	1.0		14.0	9.0
	Spidey PSP	4.0	4.0	4.0		4.0	4.0	4.0	2.0		12.0	14.0
	CNK PSP	4.0	3.0	3.0		4.0	3.0	3.0	2.0		10.0	12.0
	Sony PSP	5.0	5.0	5.0		5.0	5.0	5.0	1.0		15.0	16.0
Console												
	Doom 3 Xbox	3.0	4.0	3.0		5.0	5.0	5.0	4.0	5.0	10.0	19.0
	Call of Duty Xbox	2.0	3.0	1.0		3.0	4.0	2.0	5.0	5.0	6.0	14.0
	Vampyre Xbox	3.0	4.0	3.0		4.0	4.0	3.5	4.0	5.0	10.0	15.5
	XML PC	3.0	3.0	3.0		2.0	2.0	3.0	4.0	5.0	9.0	11.0
	Deus X movie PS2	4.0	5.0	5.0		4.0	4.0	4.0	2.0	4.0	14.0	14.0
	Over the Hedge	4.0	5.0	5.0		4.0	3.0	4.0	1.0	5.0	14.0	12.0
	Batman	4.0	5.0	5.0		4.0	5.0	4.0	1.0	4.0	14.0	14.0
<b>Risk</b>												
1=Pretty much any VV team could execute												
2=Well understood process, no invention required												
3=Can be mitigated with right team, mentoring												
4=Attention required from upper mgmt at beginning and end												
5=Significant attention required from upper mgmt throughout project												
<b>Reward</b>												
1=No royalties possible												
2=Royalties depend on contract												
3=Respectable royalties												
4=Very good royalties												
5=A hit :)												
<b>Units</b>												
<200K												
200-500K												
500-750K												
750K-1M												
1M+												

### Margin

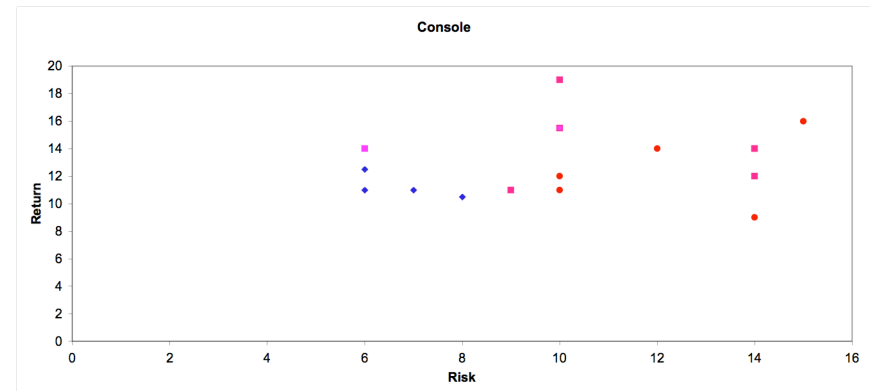
- 1=will need VV investment
- 2=squeak by with ~10%
- 3=about 20% margin
- 4=higher than average - 30%
- 5=40-50% margin

### Publisher Category

- 5= Top 5 (strong marketing, strong properties, established practices)
- 4= Top 10 (some strong properties, good marketing, mixed successes, some established processes)
- 3= Medium sized publisher (good properties, up and coming, not fully established player)
- 2= Small publisher, conservative spending (some strength, not paying very well)
- 1= Fly by Night (names omitted to protect the innocent)

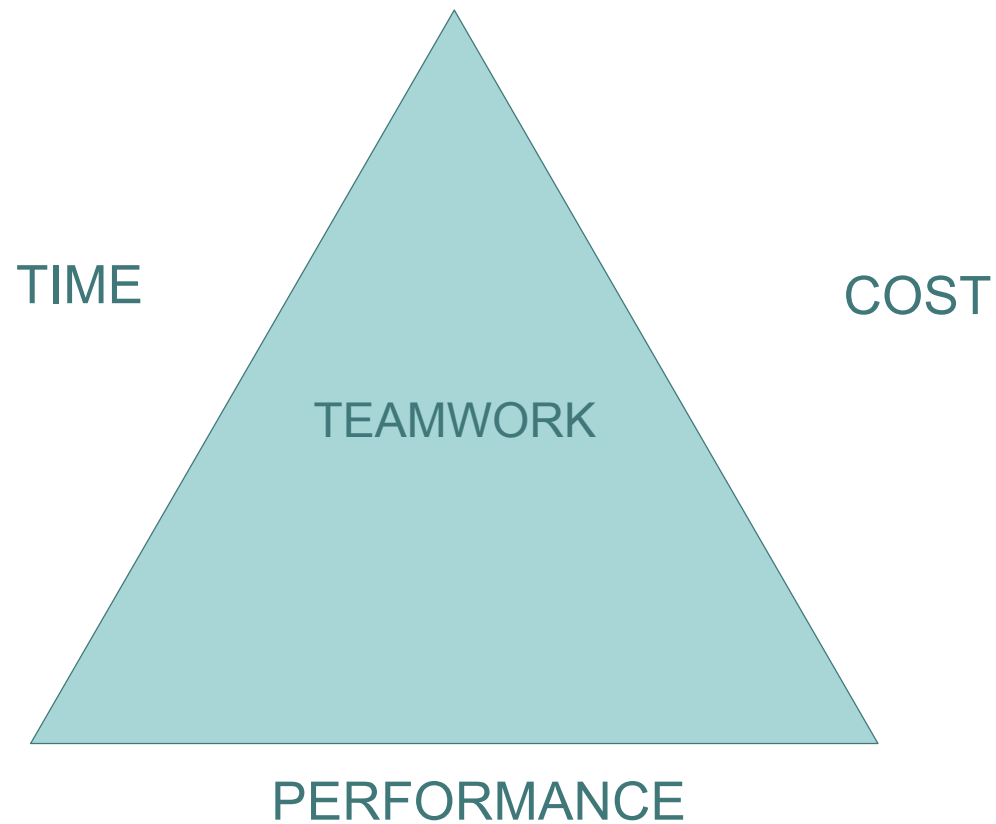
### Notoriety

- 1=No one (other than publisher/licensor) will notice
- 2= Limited press exposure in niche areas
- 3= usual amount of press/solid performance (Spidey)
- 4= above average press exposure
- 5=Game Changer (Tony Hawk, Crash)



Takeaway

# Delivering: Time Cost Performance



## Takeaway

# Tracking The Work: Financials



### THPS 3- AGB Month End February 2002

<b>Highlights:</b>			
Budget \$:	\$	26	50
Total Actual Expense - Dec 01	\$	35	71
Projected Expense	\$	2	55
Total Actual and Projected Expense	\$	38	26
<b>Preliminary Budget FTE's</b>			
Target Total FTE's		35.50	
Projected Expense FTEs:		44.41	
Total Expense FTEs YTD:		44.41	
Level of Effort YTD:		55.55	
<b>Preliminary Budget Margin</b>			
Target Margin		45%	
Previous Margin at \$7300 CPD		46%	
Actual/Forecasted Margin		20%	
Actual Margin to date- Dec 01		-1%	
Current Month FTEs:		2.11	
Current Month FTEs (Over)/Under Plan:		-	
Current Month level of Effort:		2.57	
Ytd Expense FTE's (Over) / Under Plan		(8.91)	

### Tony Hawk 3 AGB- Milestone Schedule

		SUBMISSION DATES			APPROVAL	
		Contract	Forecast	Actual	Invoice Date	Status
1	Activation					
2	Execution of Agreement	\$ ,000	2/22/05	2/22/05	2/22/05	Paid
3	GDD and TDR	\$ ,000	6/22/05	6/22/05	7/13/05	Paid
4	Technology Demo	\$ ,000	7/21/05	7/21/05	8/8/05	Paid
5	Proof of Concept	\$ ,000	8/11/05	8/11/05	9/6/05	Paid
6	First Playable	\$ ,000	9/8/05	9/8/05	10/1/05	Paid
7	Alpha	\$ ,000	10/20/05	10/20/05	10/30/05	Paid
8	Beta final (90%) MC submission	\$ ,000	11/17/05	12/25/05	12/22/05	Paid
9	Submission to Nintendo Lot Check	\$ ,000	12/15/05	1/9/06	1/3/06	Paid
10	Approved for Manufacture	\$ ,000	12/29/05	1/11/06	1/18/06	Paid
	Localizations approved	\$ ,000	12/29/05	1/16/06	2/1/06	Paid
Total		\$4 ,000				

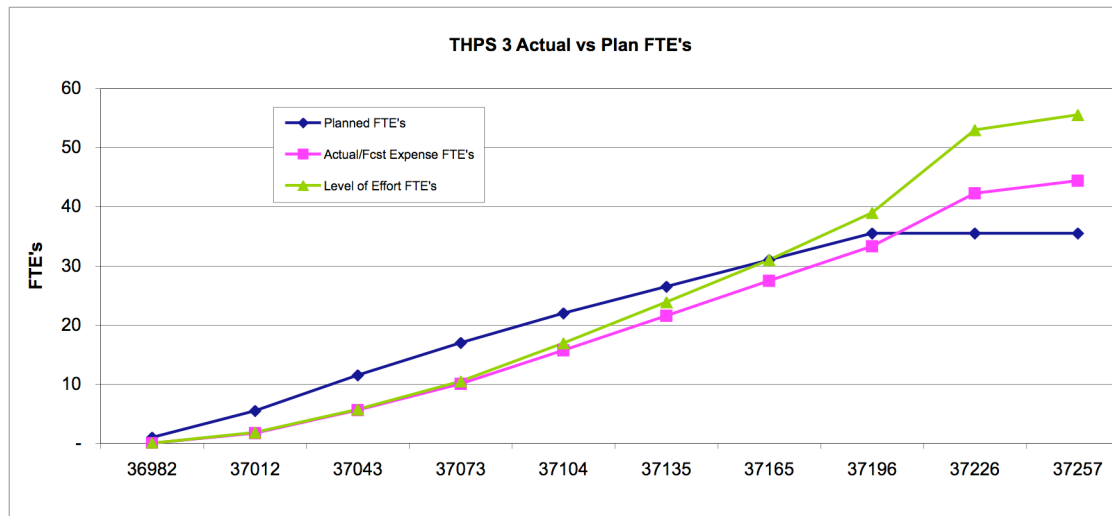
### Sub Contract Data

Total Budget:	\$	5,000
Total Forecast:	\$	5,000
Total Spent to Date:	\$	5,000

	Total	Expensed	This Yr
Music	\$ 5,000	\$ 2,000	\$ 3,000
			\$ -
			\$ -
	\$ 5,000	\$ 2,000	\$ 3,000

## Takeaway

# Tracking The Work: Labor



Plan vs. Actuals showed how good our estimates were

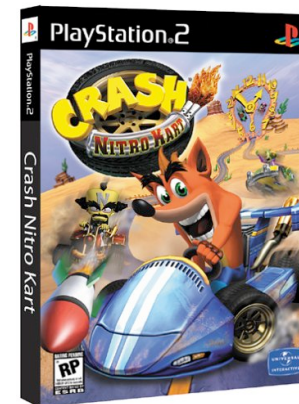
Level of effort analysis allowed us to plan better for the future

THPS 3 AGB - Actual/Forecasted Expense FTE's											
Role:		Apr-05	May-05	Jun-05	Jul-05	Aug-05	Sep-05	Oct-05	Nov-05	Dec-05	Jan-06
Artist	Rob			0.14	0.96	0.89	0.88	0.95	0.99	0.97	0.14
Guest Programmer	Alex		0.01	0.01						0.02	
Lead Artist, Project Lead	Andy		0.46	0.89	0.45	0.84	0.96	0.94	0.98	0.97	0.38
Lead Programmer	Matt		0.47	0.97	0.64	0.99	1.00	0.96	0.99	1.00	0.42
Designer	Ben									0.60	
Programmer	Alan			0.88	0.94	0.97	1.02	1.05	1.02	2.71	0.48
Programmer	Eric		0.78	0.99	0.97	1.03	0.99	1.03	1.09	1.39	0.13
GB Artist	Sean				0.49	0.96	0.99	0.98	0.77	0.91	0.22
Project Manager	Jesse									0.41	0.34
Total		0.00	1.72	3.88	4.45	5.68	5.84	5.91	5.84	8.98	2.11
Cumulative Total		0.00	1.72	5.60	10.05	15.73	21.57	27.48	33.32	42.30	44.41
Non Labor Expense (\$'s)		-	-	-	-	-	-	11.54	88	2167.09	
Cumulative non-labor Expense		-	-	-	-	-	-	12	100	2,267	2,267

2003

# Bigger projects...

- Needed cross platform tech for console
- Leveraged experience with the Crash Bandicoot franchise to secure Crash Nitro Kart
- Negotiated good deal, and a great opportunity to drive our console business
- Chose Intrinsic Alchemy as our middleware solution
  - Good partners
  - Great architecture
  - Great concept
- Looked rosy!





2003

# Stuck in the middleware

- Crash project was shifted in by 12 months (2003 not 2004 ship)
  - PS2 and X-Box skus added
  - Believed in our team and tech choice
  - We were nuts
- We had an object code license
- Critically dependent on support and not-yet-complete features
- Intrinsic Graphics ran into financial difficulties
  - Shifted to survival focus
  - Liquidated its assets
- We ***had to deliver***
  - Reputation on the line
  - Only as good as our last game -- no future in console if we failed
  - Deal terms - low margin, but great royalty -- only worked if we shipped!



2003

# Acquiring Alchemy

- We stepped in
  - We bought the assets, and engaged the team
  - Identified gaps in the product, and started building
  - Learned a lot
- Not a pretty picture, but we were able to get situation under control
  - Established bi-coastal development
  - Supported other licensees in a similar bind
- CRITICAL: **Cash Reserves!**
  - Allowed us to move quickly
  - Outpaced some much larger bidders to secure the assets
  - Speed and liquidity allowed us to cut a favorable deal
  - We shipped CNK!
- Cash reserve use met requirements
  - Use was critical to company future
  - Use didn't exhaust reserves, and left enough to fund potential additional near term issues



2004

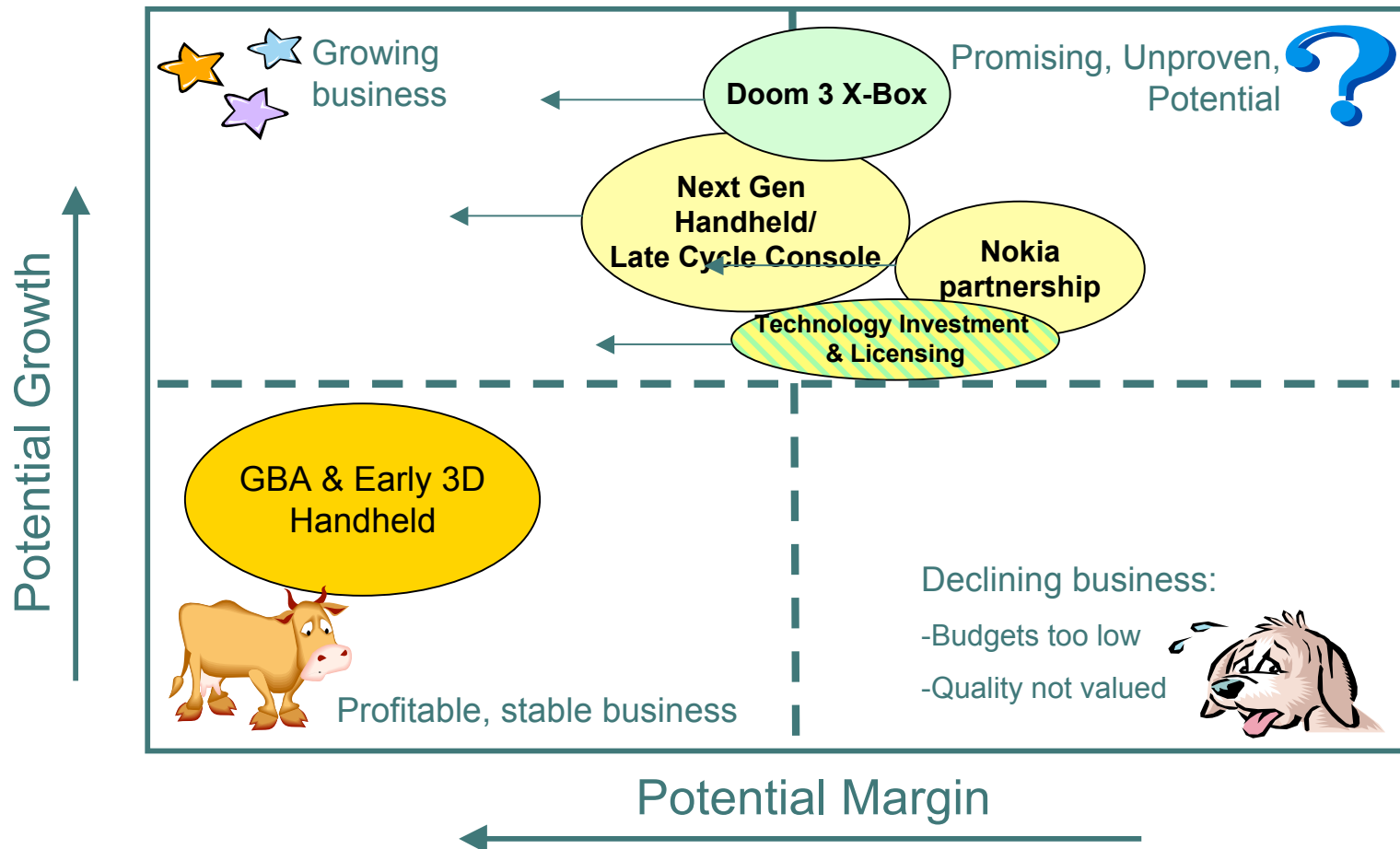
## The Hardware Transition


- Hand held and console transition fast approaching
- Needed to develop skills for new platforms and bigger development
- Established key titles for NDS and PSP launch: Spider-Man 2 with Activision
- Risky strategy → Existing business needed to fund new opportunities
- We had great customers, and a good opportunity pipeline
- Required everyone to step up!



## Takeaway

# Funding new areas, while making money

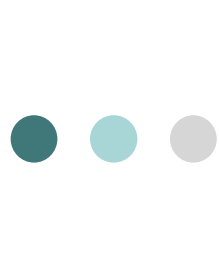




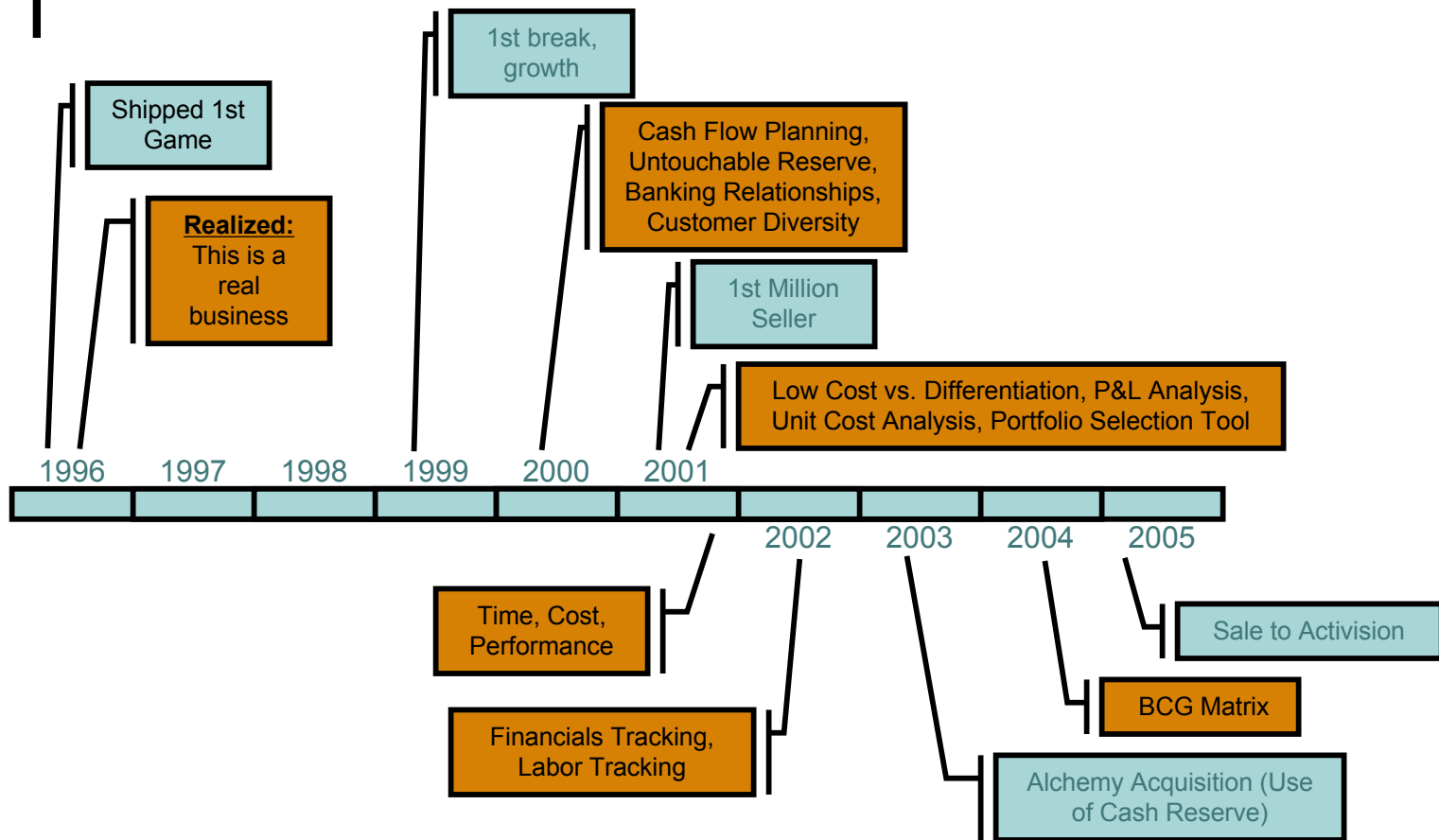
2005

# Sale to Activision

- Sold in January 2005
- Continued to grow, deliver titles
- On the right track from a quality standpoint
- New lessons to learn
  - Bigger projects
  - More innovation
  - Leveraging our capabilities through a much closer partnership with publishing



# Adding it up



Questions?