

Massive multiplayer online role-playing games - the future of gaming

Welcome to the virtual universe of Project Entropia



Project Entropia - an online game with more than just virtual worlds. The Story behind MindArk and the Chances on the market

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EDITORIAL



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Real money in virtual worlds?

Dear readers, in this special edition of Bridge Express we take a look at the online game "Project Entropia". What is the Story of this company? What can an investor expect from it? Then we look at the game itself and try to find out the USP, while looking at the business plan and the revenue model. An Interview with CEO Jan Welter Timkrans rounds the theme off. As interesting side-news: Project Entropia has been listed in the Guinness Book of records for the highest price ever paid for a virtual property. A gamer bought an island for SEK 198, 888 and can now charge a fee from every passer-by. As we mentioned in the last edition of Bridge Express; an interesting chance to invest in a new star in a booming sector. For more information about MindArk take a look at www.mindark.com The Bridge Express Team wishes you an enjoyable read of this special edition and good investments.

A short overview of this massive multiplayer online role-playing game

The Story behind MindArk and the Project Entropia

MindArk develops and operates the three-dimensional virtual universe Project Entropia. This platform is accessible to everyone with a PC and Internet connection. MindArk provides the infrastructure of Project Entropia, a complete universe for interactive entertainment. Every user is represented by an avatar, which is a three-dimensional representation of the user's character within this virtual universe.

Institutional and private investors were also brought into ownership of the company in 1999 and 2000. These included Skandia Liv (Sweden), Banco fonder (Sweden) and Value Venture Capital AG (Switzerland). Development of Project Entropia cost nearly SEK 150 million for the five-year period up to 2003. The institutional investors decided to withdraw from the project and MindArk went into bankruptcy. The founders and employees bought it back from the bankruptcy estate.

Break Even since 2004

Revenues for 2004 were approximately SEK 18 million and the company passed the break-even point. Forecasts for 2005, based on the operating results for the first quarter, indicate revenues doubling to SEK 35 million. The company expects a growth of 100% per annum over the next 3 years.

One billion market

Project Entropia is a "massive multiplayer online role-playing game" (MMORPG) effective in a market worth one billion US Dollars 2004 with anticipated growth of 70% per annum. The universe of Project Entropia will take players on an epic journey into the future, to a place far away from Earth, beyond the borders and frontiers of known space. The central point in the human universe is now focused on a single colony on a distant planet named Calypso. Project Entropia has a unique economy with its own currency. The virtual currency is called PED, from Project Entropia Dollars. The uniqueness and strength of Project Entropia is that the currency used



in the game can be exchanged for real US Dollars and that players need not pay any fixed fees to play the game.

SWOT-Analysis

Strengths

- ✗ over Internet provides low distribution cost and high user availability
- ✗ No start-up fees increase availability to a larger audience
- ✗ No recurring monthly charges reduces churn relative to other MMORPG
- ✗ The cost of play is activity-based so each satisfied, and therefore active, customer is more profitable
- ✗ Exchangeability of the game currency adds opportunities
- ✗ Client - server solution facilitates and speeds access, even with low bandwidth
- ✗ New game concept

Weaknesses

- ✗ Very high churn
- ✗ Low brand awareness
- ✗ Relatively small marketing budget
- ✗ No distribution via retailers

Opportunities

- ✗ Number of Internet users is increasing constantly, thereby expanding the available market
- ✗ High growth in the MMORPG market
- ✗ MMORPG market relatively small in relation to the total gaming market
- ✗ Totally new product concept in the MMORPG segment with real currency exchange options
- ✗ The platform can be used for other product offerings relatively simply

Threats

- ✗ Hackers and fraudulent activities
- ✗ Using real money in Project Entropia increases interest in hack activities
- ✗ Government restrictions and possible regulatory changes

The company is headed by Jan Welter Timkrans, born in 1956, an entrepreneur with several successful start-ups behind him. Today the company employs 25 people Welter Timkrans is the biggest shareholder of the company with 45.3%, followed by C-G Bothén AB with 31.0%.

History of Project Entropia The Company

In 1995 Catco International established a separate department of ten employees led by Jan Welter Timkrans. The department worked on structuring, documentation and testing to determine the feasibility of designing a platform for a virtual three-dimensional world. After more than three years work on the project, it was transferred to a separate company named MindArk AB.

As MindArk AB was founded in 1999 the project was renamed Project Entropia. Institutional and private investors were also brought into ownership of the company in 1999 and 2000. These included Skandia Liv (Sweden), Banco fonder (Sweden) and Value Venture Capital AG (Switzerland).

Development of Project Entropia had cost nearly SEK 150 million for the five-year period up to 2003. Then, as the product became ready for commercial introduction, Skandia chose to withdraw its previous commitment, thereby forcing the



management to enter the company into bankruptcy.

The company's management decided to purchase Project Entropia from the bankruptcy administrators, Lindahls Advokatbyrå, in April 2003. In conjunction

with this, MindArk PE AB (MindArk) was founded. The purchase included all intellectual property rights and all software previously owned by MindArk AB. In addition all previous employees continued in the new company.

Over 90, 000 active accounts today - 400, 000 planned for the end of the year Actual progress dates and future projections

MindArk PE AB was founded in April 2003 and operating profit for 2004 was marginally positive. Revenues for 2004 were approximately SEK 18 million and the company passed the break-even point. Forecasts for 2005, based on the operating results for the first quarter, indicate revenues doubling to SEK 35 million.

Big plans for growth

252, 983 Accounts had been created in the virtual universe of Project Entropia up to May 2005, of these 93, 312 are active. Active players are when the accountholder returns to Project Entropia within a period of eleven months. MindArk project the number of accounts will be approximately 400, 000 accounts created by the end of 2005, provided limited marketing can be initiated in the autumn of 2005. MindArk further project an accelerated pace of expansion

to take place from autumn of 2006 when content and quality within the virtual universe is expected to be at level where

re acceptable „sickness“ has been achieved, which in turn motivates the initiation of massive marketing activities.



The next generation of interactive entertainment grows up Project Entropia - The Game, The Model and the USP

Project Entropia is expected to be the next generation of interactive entertainment. In Project Entropia, players enter a complete world with amazing three-dimensional environments using a computer and the Internet. It is a massive virtual world where millions of users can simultaneously interact with each other. Project Entropia also has a real financial system that allows the user to exchange real currency into PED (Project Entropia Dollars) and then back into a real currency again. Project Entropia is free of charge to play including no monthly fees. This means that aside from the fees for local access to the Internet while connected, client software will be available to prospective players for no payment to MindArk. The only requirement is obtaining software that will be distributed in various ways-through the Internet or on free CDs offered in computer magazines.

Players deciding to enter the world of Project Entropia as a citizen will be able to create their own visual three-dimensional persona. Project Entropia enables players to experience a life inside a vast virtual reality of their own making. It offers players social interaction with people all over the (real) world as well as real online services inside an incredible virtual environment.



Project Entropia is also meant to help players fulfil their dreams and fantasies with adventures inside an expanding science-fiction/fantasy universe. For everyone who is familiar with the term "massive multi-player online role-playing game" or MMORPG, Project Entropia will be that and much more.

As an MMORPG, the universe of Project Entropia will take players on an epic journey into the future, to a place far away from Earth, beyond the borders and fron-

tiers of known space. The central point in the human universe is now focused on a single colony on a distant planet named Calypso. The world on Calypso will undergo constant development and will initially include three vast continents with large expanding cities where living begins. The cities will offer an immense virtual playground for social interaction with other players in a thriving community. It will contain various forms of in-game institutions, real-time online services, and a variety of virtual entertainment.

Together with the others online, a player will be able to take an active role in the creation of a whole new civilization, to explore entire continents in an evolving world and claim land to establish new communities. Choosing to leave peaceful and secure cities may force a player to struggle against a wild and untamed wilderness, against hostile mutants and invading robots. Everyone must learn to use all their resources and learn many new skills, while using their wits, guts, teamwork and equipment to reclaim a lost paradise. They can also take on quests and pull the strings of the past to discover more of the story behind Project Entropia as the future unfolds in a growing web of intrigues of epic proportions.



Interview: MindArk-CEO Jan Welter Timkrans about the Game and the Future **„Lack of imagination is not the major issue of MindArk“**

To clear up some interesting points in the Story of MindArk and Project Entropia we interviewed MindArk CEO Jan Welter Timkrans about the Company, the Future and the Game. Here is what he said:

Online gaming is a huge market in Asia and the US - what is the potential?

Jan Welter Timkrans: We expect the European market to be equal to, or even surpass, the US market for online games within a few years but this is of lesser importance to us since our system functions on a global scale. However, a few adaptations are necessary in order for our product to become successful in the Asian markets, the most important is that translations will have to be made into Chinese, Japanese and Korean. This process will be initiated early in 2006.

What are the advantages of Project Entropia compared to other games?

JWT: Project Entropia is based on a real economy, the currency "Project Entropia Dollars" is exchangeable to any real world currency. This means that the balance of the game has to be managed like the economy of a real nation in order to work. Other online games with a fantasy currency do not need to emphasize this issue; therefore they all end up with a galloping inflation of their fantasy currency and, typically, skills and items. When these parameters are not in strict balance the game becomes boring after a while. Project Entropia does not have this problem, our virtual market economy is balanced and thriving, we expect the turnover within Project Entropia to be in the neighbourhood of a quarter of a billion USD this year already.

What can a player do in this game, what is the goal and what does it look like?

JWT: Project Entropia is a single universe where all participants from all around the

real world can meet, socialize and participate in adventures together. Other online games are based on several smaller "universes" catering for a few thousand participants each. This means if you start your on-line persona in one such universe you can never meet people who have created their avatar in another small universe. This also limits the potential markets to several small ones, which is, of course, not good for an economy.

How do you make money with Entropia?

JWT: Other online games are based on a monthly subscription fee. This means that the optimal case for this type of game is that users just pay their subscription fee and spend as little time playing the game as possible since this just adds to the cost for the development company of running servers, internet bandwidth support etc. For project Entropia this is completely the other way around, a participant only generates revenue for the company when she or he is actually "playing" inside our Universe. This encourages, and even forces, us to constantly develop content that will increase the enjoyment for the participants and will make them want to spend more time playing Project Entropia. In a sense we have created a system with an inherent force that will ensure an ever-expanding universe including both new content and new geographical areas.

What about the financial aspects - has the company passed the break-even point?



JWT: The company has already passed the point of breaking even. This was achieved last year. This year will generate a profit, which we intend to spend chiefly on marketing activities. The spread of Project Entropia to date has mainly been achieved by means of "word of mouth". To reach a quarter of a million users as we have done through these means must be considered to be quite unique and shows the potential of the product. Now the product has been developed to the state where we can invest in marketing activities to spread knowledge about our product to a larger audience with confidence.

I've seen there is also a stock market in the game - is it working and how does it work?

JWT: The stock market inside Project Entropia has not been put into an operational state yet. It is just there as, shall we say, an internal advertisement of things to come. Once operational it will enable players to sell stocks in their in-game virtual companies and, who knows, in the future even real world stock may be traded on this exchange. *Interview by Martin Michalky*

The players can change their play-money into real money. How do they pay in?

JWT: Players have a number of means of transferring money into Project Entropia, for example via credit cards, banks, telephone or one time "scratch cards" to name a few ways and we are constantly adding means. Every time a player deposits money into Project Entropia the total volume of money inside grows by as much.

A player who has earned money inside Project Entropia can also withdraw money whereby the total monetary volume inside Project Entropia will decrease by the same amount.

Is there any advertising in the game? If not, is it planned to increase income?

JWT: Advertising and product placement is becoming increasingly interesting as the

number of "well defined" participants in Project Entropia increases. However this activity has not been considered as of critical importance to the revenue to be generated by us, but should be seen rather as a welcome additional revenue stream. We have several alternatives in mind for the future when we become a more interesting marketplace. Only the imagination sets limits here and we feel that a lack of this is not a major issue at MindArk.

How does the money come into MindArk and what makes the game special? The Revenue Model and the uniqueness of the game

MindArk's revenue model currently has two parts-the virtual economy of PE and the normal world. The virtual economy in Project Entropia is based on real money, allowing players to exchange real currencies for the virtual currency-PED (Project Entropia Dollars). The actual exchange rate is currently set at 10 PEDs to USD 1. This money is used in the virtual economy to buy various objects for use by a player's avatar (their virtual character) in the PE virtual world. Project Entropia allows players to make, find and trade these objects as well as to go out on missions or adventures to seek the opportunity to earn money. The revenue base for MindArk is the need to repair the weapons, tools and other objects used by the players' avatars-this costs money. Inside the virtual cities, there are various types of terminal that the players use to repair their different objects. These objects retain a return value guaranteed by MindArk, although this guaranteed value is usually lower than the second hand market for the same objects in the virtual world of Entropia. Thus Project Entropia maintains a market economy. Anything can be bought or sold at auction in the game. Supply and demand are the controlling factors.

Real money out of virtual

Real revenues from the virtual economy will also come from one-time sales of various kinds. These do not have a guaranteed return value. Such products can include houses, apartments, business sites, and land (to name but a few) that will add

different values to the world of Project Entropia. Revenues will also come from special fees, such as auction fees. Players in PE earn money by doing certain work activities such as hunting, farming, or prospecting. Revenue for the ammunition purchased by the players is pooled for use as payment for treasures or as rewards to players for the activities they perform. A portion of this pooled resource also goes to 'items' placed for players to find on animals they kill. A random generator determines the size of the reward, but for the Company the revenues and reward payments should be equal.

The uniqueness

The uniqueness of Project Entropia is that the currency used in the game can be exchanged to real USD and that players need not pay any fixed fees to play.

Currency - The currency in Project Entropia is called PED. Each PED is easily exchanged for USD. The advantage with this is that players do not feel they have used their money when they exchange real USD for PED. As well, when they earn PED in the game, players can also feel they have gained real money. Further, the game in Project Entropia can become a marketplace for real goods, such as digital music.

Players in Project Entropia pay no fixed



fees or monthly charges to enter and participate in the game. Costs to the players are charged in the game for the virtual equipment they acquire as this wears out as it is used. Players must then pay 'maintenance' charges for this virtual equipment in order for it to function fully in the game. For an active player, these charges correspond to a cost of USD 0.5 to 1.5 per hour. Players experience these maintenance charges as more natural since this corresponds to real life where equipment gets worn.

It is therefore extremely important for MindArk to interest players in actually taking the time to be active in the game. This can only be done if players actually experience the game as enjoyable. The table below illustrates the logged hours played by an active player per month. The table shows that each player takes an average of one hour every day to participate in the game.

Usage of Funds: Mainly marketing, but also development to keep the cutting edge Business Plan: SEK 224m net income till 2008

MindArk has chosen an aggressive sales budget and anticipates being able to double the number of paying players annually up to 2008. During 2005 MindArk anticipates 135 000 new accounts will be created, out of these 70% will not be in use after one month. That equates to 40 500 new accounts of which 25% will be paying customers. Currently, Project Entropia has approximately 600 concurrent players in the game throughout the day. Additional revenue sources should become available when the Company increases the number of both paying and non-paying players. These could include both advertisements and direct sales. Company management believes that testing of alternative revenue sources could begin by the end of 2005. See the business

plan at the bottom of this page.

Use of Funds

MindArk plans to use most of this financing round for marketing purposes in Germany and Holland. A total of SEK 15 million has been earmarked for marketing. A further SEK 5 million will be used to set up a third development team to keep the product at the cutting edge—a high priority for the Company. A further SEK 5 million will be used for investments to handle the expected increase in player numbers.

Financial Scenario

MindArk's board of directors has approved the presented budget based on a number of assumptions and estimates. Min-

dArk estimates an annual growth in revenues of one hundred percent from 2005-2008. Furthermore it is estimated that returns of generated revenues to players will grow from five percent in 2005 to twenty percent in 2008. Estimates relating to marketing costs, computer and license costs and operating costs are based on experience of running an MMPROG Internet site. The figures for the full year 2004 and January - May 2005 presented below are the actual results and those for 2005 to 2008 are estimates. A new development team will start at the beginning of 2006.

Value and Appreciation of Value

Tamm & Partners were commissioned by MindArk to evaluate the Company as of June 10, 2005. The valuation calculation is based on the full utilization of cash flow by the Company and the fact that there are no operating assets that can be valued separately or which have a specific value. Future cash flows are based on those forecasted in the budget approved by MindArk's Board of Directors. A cash flow valuation with a 25% discount, values the Company at approximately SEK 205m.

Exit Scenario

If they succeed with their plans, MindArk will make an interesting acquisition target. The most likely exit scenario is an IPO and that MindArk will be listed on the stock market.



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