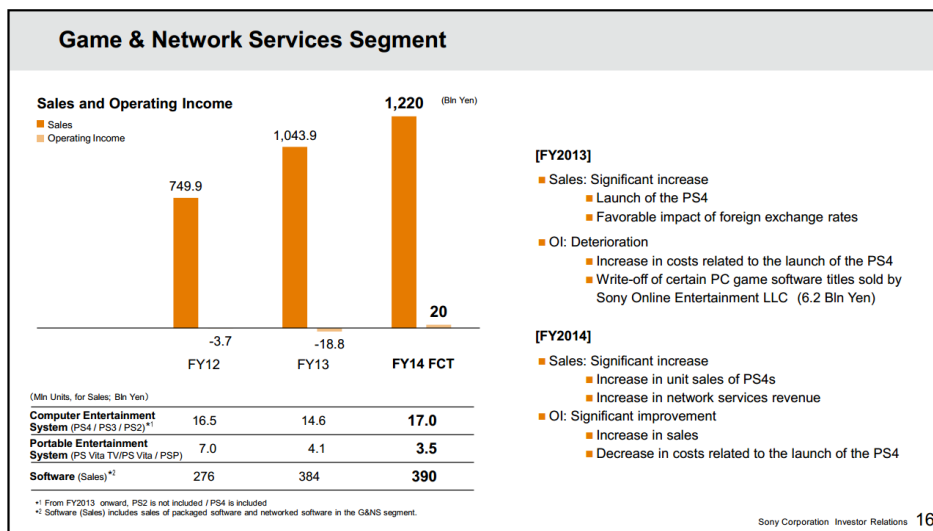


Summer 2014 Case Study



SITUATION

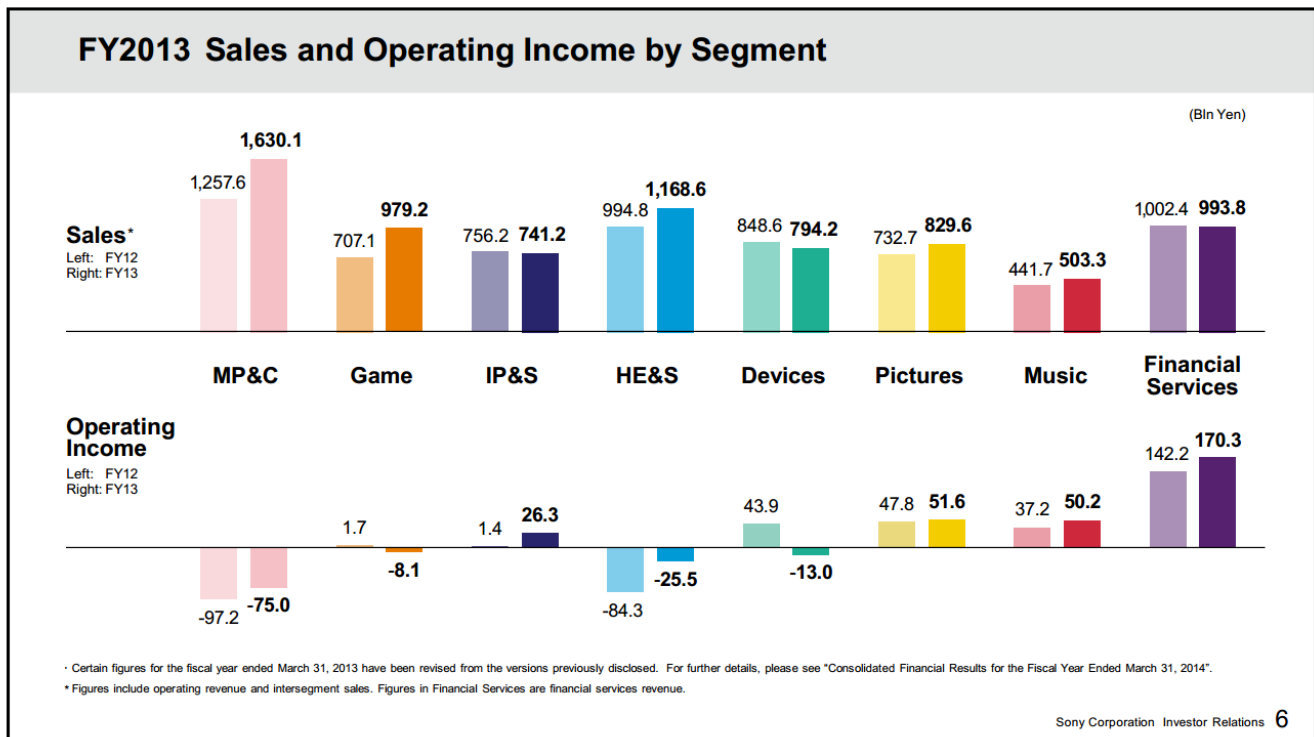
Sony Corporation is a 68-year old multinational based in Tokyo. In 2012, the tech giant employed 173,000 people, with corporate headquarters in Japan, Europe, and America. In May 2014, the company was down to 146,300, cutting 26,700 as part of CEO Kaz Hirai’s “One Sony” plan. Recently, the firm even sold former office buildings in Tokyo for \$156 million (Inagaki). This followed a similar \$1.2 billion sale in 2013. After several years of losses, Sony’s situation appears critical. In the last fiscal year, the company lost \$1.25 billion. Even the gaming division, where the Playstation console family (PS2, PS3, PS4) is projected to sell 17 million units this year, lost \$78 million (Quarterly Results). There are many causes: Sony’s jettisoning of its PC brand Vaio, the poor performance and planned spinoff of Sony’s television division, PS4 launch and marketing costs, the struggling PSVita, R&D costs for Sony’s Project Morpheus, and the fluctuation of exchange rate markets. For the current year, Sony is projecting a \$489 million loss. How sustainable is Sony’s current business model? Will the success of the PS4 lead to renewed profitability for the games division and the company as a whole? Perhaps opportunities in new markets can spark a turn-around.



The company’s core businesses are electronic entertainment (Sony Computer Entertainment, Sony Music Entertainment, and Sony Pictures Entertainment) and hardware (Sony Mobile Communications and Sony Electronics). Though it also dabbles in financial services, publishing, and medical imaging, electronics represents roughly two-thirds of the corporation’s revenue (Sony Annual Report 2011, 2013). Despite a lack of brand awareness for its financial services, these provided the largest increase in operating income across the company’s many divisions last year (Quarterly Report).

HISTORICAL PERFORMANCE

Sony created two of the strongest brands of the last three decades (Walkman and Playstation), and several of its products have become household names, including Vaio, PSP, and Sony Ericsson. The corporation is also largely responsible for the invention and commercialization of the Compact Disc (CD), Digital Video Disc (DVD), and Blu-ray Disc (BRD). Several of its proprietary formats have seen less success—UMD, minidisk, and, famously, Betamax. Sony Corp. is often at the bleeding edge of technology, recently pushing active shutter 3-D glasses, OLED, and Crystal LED. Virtual Reality is Sony's next major initiative, with the company set to launch Project Morpheus (code name) to the public in 2015. Some of its adventures in technology have become expensive boondoggles, such as the development of the CELL processor used in the Playstation 3. The CELL initiative cost Sony at least \$400 million and even assisted in the creation of rival Microsoft's Xenon processor in the Xbox 360 (Shippy and Phipps).



Since 2006, Sony has seen its stock price and general market share (across most divisions) decline. On May 8, 2012, Sony stock was trading at its lowest level since April 25, 1987 (Yasu). In January 2014, Moody's downgraded the company's stock to "junk" status (Petroff). On May 14th, 2014, UBS downgraded Sony stock to a "Sell" (flyonthewall).

The historical success of the Walkman brand has been surpassed and nearly extinguished by Apple's iPod. Sony's Playstation 3 lost more money in its first two years on the market than the Playstation 2 earned over its entire lifetime (Kennedy). Losses on the PS3, as of 2012, were somewhere in the \$3.5 billion range; rival Microsoft's Xbox 360 has earned \$1.8 billion since 2005 (Mallory). While the Playstation™ brand is generally considered healthy thanks to strong sales in Europe and Japan, it has lost market share in the United States. Exact figures aren't known (the Big 3 list "shipped to retailer" numbers as "sold"), but current estimates put the PS3 at about 83 million units worldwide, while the Xbox360 sits at 81 million and the Wii at 100.5 million ("Sales Age"). By comparison, the PS2 has sold 158 million units (Furtado). In a bit of good news for the company, the PS4 is a runaway hit, with 7.5 million sold in only seven months on the market, but

recent announcements from Microsoft threaten to shake up the console race (“Delivering More Choices...”). While a worldwide sales “victory” appears likely for the PS4, losing market leadership in the US would be damaging for the brand. IDC research manager Lewis Ward expects the Xbox One to surpass the PS4 in US market share by 2015 (Brightman).

In fact, few of Sony’s products are clear market leaders. Walkman share is in the low single digits in an mp3 market dominated by Apple. Despite being the fourth largest cell phone manufacturer, Sony Ericsson market share dropped below 2% in 2012 and has remained there since (*Yasu* and *ben-Aaron*). Sony’s Tablet S was the highest selling Android tablet in 2012, but it’s been bad news since, with stiff competition from the Kindle Fire, Samsung Galaxy, and, of course, the iPad (*Lehto*). The tablet market in general is in decline, down 3.9 percent over the last 12 months (*Whitaker*). Samsung and LG have also moved past Sony in TV sales, with Sony recording an 18.5% decline in LCD sales in 2011 (*Pham*). Steady declines have Sony’s global TV share down to 14.3%, which is good enough for third place. The general consensus is that the economic downturn of 2008 damaged high-end brands like Sony significantly more than value-proposition brands as customers reigned-in discretionary spending. Factor in deferred tax costs (\$3.2 billion in 2011), floods in Thailand affecting production, yen-to-dollar and yen-to-euro exchange rate losses, and Sony has had a rough go of it (*Phan*). The TV division has lost money for a decade (*Briel*).

Sony has also announced the closing of 65% of its brick and mortar retail stores in the US (*Neikirk*).

In 2012, Howard Stringer, Sony’s former Chairman of the Board, stepped aside as CEO in favor of Kazuo Hirai, Sony’s president and head of Playstation. Mr. Hirai vowed to turn the company around, calling his plan “One Sony” and promising to cut 10,000 jobs in fiscal year 2012 (*Lawler*). Despite promises to the contrary, the games division was affected, with Sony closing Zipper Interactive and, recently, Studio Liverpool. An in-development game at Santa Monica Studios may also have been axed as a consequence, though perhaps poor quality of alpha gameplay is to blame.

Sony Corp. has been notoriously slow to accept change, with cross-division territoriality preventing strategic shifts in the business. 2011 was a particularly devastating year for Sony. It survived the Fukushima earthquake, tsunami, and radioactive scare, a massive breach of the Playstation Network Online service that exposed 77 million users’ passwords and credit card data to hackers, and a \$6.4 billion loss. With the ramp-up to the PS4 generation of video game consoles adding hundreds of millions of dollars to Sony’s R&D costs, Mr. Hirai, who led Sony Computer Entertainment from 2006-2012, is in a tight spot. Can he create a hardware, software, and marketing strategy to crush Microsoft’s Xbox One without pushing Sony further into the red? There is a clear opportunity in the BRIC nations to expand the market for gaming and networked entertainment devices.

A 2012 article in *The New York Times*, “How the Tech Parade Passed Sony By,” suggested that Sony is in dire need of innovative ideas. Things haven’t changed much in two years. That’s your cue. Will your consulting firm dream up a winning strategy for Sony in China, or is it “game over” for Mr. Hirai (*Tabuchi*)?

A SEMESTER-LONG PROJECT

For the last fourteen years, game consoles have been banned in China. Sony’s current pricing, software, messaging, partnerships, and omni-channel approach may be inadequate in the new, blue ocean market. Threats include the imminent Xbox One and Wii U launches, the grey market, smartphones, mobile gaming, PCs, government regulation, and the limited disposable income of middle-class Chinese consumers. Moreover, Sony’s financial position is tenuous. Your marketing proposals should consider Sony’s desire to offset losses in PC, TV, and smartphone divisions. Cost-effective plans will be favored by Mr. Hirai and his executive board.

To understand the industry, you will complete three 6-7 minute micro-case presentations from the perspective of Sony’s major competitors (Nintendo, Microsoft, Oculus/Facebook). While these mini-cases deal with the industry at large,

broadening your knowledge base, our final Sony case deals with China only. Background research for Sony, Playstation, and the video game industry, including company financials, is provided, both in this document and in lecture. Students must, however, complete original research into Chinese consumer behavior and the Chinese market.

The project culminates in a 12-15 minute presentation with open-ended Q&A, accompanied by a 25-page formal analytical report (see parameters below). Substantial class time is devoted to the creation and revision of Sony Cases.

Storytelling, especially concerning Chinese consumer behavior, is encouraged in team presentations.

PROMPT

How can Sony win the new console war in China? How should it position, price, and market the PS4? Consider all known initiatives, including Project Morpheus, Playstation Now, the PSVita, and perhaps even long-term planning for the PS5 as part of your China strategy.

Consider, too, how Sony might harness its advantages, including brand loyalty/recognition, its diverse divisions and product lines, its status as a hardware manufacturer, and the largest stable of first-party developers in the industry.

Your team should have a single core proposal, strategy, or campaign. Name it something, as Hirai did with his “One Sony” initiative. You are welcome to make multiple recommendations and address any aspect of Sony Corp. that impacts video games in China, but your team should have an identifiable “big idea.”

PROJECT PARAMETERS

Every proposal you make should take into consideration Sony’s current financial outlook. Provide estimated costs and potential revenues for your marketing strategy.

Your core marketing idea should be grounded in research. It’s not unusual for Sony Reports to contain a hundred citations from dozens of sources. Unfortunately, video game journalism is especially poor, as reporting is often done by unpaid enthusiasts and bloggers. Dig deep for educated reporting and analysis.

Use the Suggested Topics section below as a starting point for brainstorming.

Include in your Sony Report a SWOT analysis (Internal: Strengths/Weaknesses, External: Opportunities/Threats) of Sony’s current situation in China, as well as a second SWOT analysis after implementation of the proposal.

Reports typically include: a cover page, a proposal page, an introductory letter, a table of contents, a list of figures, an executive summary, the body of the analytical report, an implementation time-line, a work cited page, a work consulted page, SWOT analyses, and Appendices.

Your Formal Report should be between 15 and 25 pages, not including Appendices and Indexes. Submissions should be aesthetically pleasing and are often spirally bound.

In addition to the team report, each student will create an Addendum slide-doc, proposing changes to the team’s idea based on news developing from E3 2014. This is a separate, individual assignment due after submission of your team’s Sony Report.

SUGGESTED TOPICS

HARDWARE IN CHINA: In the 8th console generation, the Playstation 4 should be Sony’s flagship product for the next five to nine years. Barring a disruptive change in the console cycle, the PS4 will likely serve as a tech base for any new peripherals

(such as advanced motion controllers or the VR headset Project Morpheus). How much and how long these products negatively affect Sony's bottom line depends largely on their BOM (Bill of Materials). Your team might make hardware recommendations for Project Morpheus, a revised PS4 slim, or any future hardware you think necessary to winning the Chinese market. If you choose this direction, your team should familiarize itself with current rumors about Project Morpheus' launch window, internal tech, and hardware specifications.

How much should the PS4 cost in China at launch? How many skus should be offered? Should Sony follow a particular pricing strategy?

If success in China requires hardware revision, what should be the system's power consumption? How large should the box be? What should come in the package? Cables, controllers, a pack-in game?

With the purchase of Oculus by Facebook, Sony faces a new and deep-pocketed competitor. What hardware decisions would allow Sony to fend off mobile gaming? Will VR gaming take off in China?

Besides hardware recommendations, your team could propose a control-input innovation. Sony is no stranger to controller-free gaming, inventing the EyeToy and the PSEye. Hardcore gamers may respond well to a generational leap in graphics tech, but consider the success of Microsoft's Kinect and the Wii remote in attracting "casuals." What future, if any, is there for the PSEye and PSMove in China? How else might Sony approach the hardcore vs. casual divide among Chinese gamers?

Sony will also launch the Playstation Vita, its successor to the PSP, in China. If you choose a hardware topic, your team might include plans for keeping the Vita afloat, as new handheld R&D may be infeasible in the short term. Moreover, your team might position the PS3, Sony's legacy system, in the market as well.

SOFTWARE IN CHINA: Most successful games have a development cycle of at least 18 months. If you believe software is key to dominance in China, which franchises should Sony push early in the PS4's lifespan? What is the right balance of genres to appeal to the Chinese demographic? Should Sony create new intellectual properties or continue existing franchises? Which of its internal developers should be assigned to games that appeal to the Chinese consumer?

Another strategy console makers follow early in the product lifecycle is to purchase exclusivity rights to AAA games from third-party developers. Besides hardware differences, exclusive games could be the most important selling point for Chinese gamers. Should Sony form strategic partnerships with Chinese developers? Which ones?

One of the largest stories in the industry is the continuing convergence of technology. Consoles are no longer simple games machines. Online services, such as Xbox Live, Playstation Network, and Steam, seek to deliver a complete entertainment solution for the living room, offering movie downloads, chat systems, video conferencing, social media apps, etc. Because of convergence, Sony's competition in China may come from unexpected sources: Apple TV, Comcast On-Demand, AT&T Universe, Netflix, Hulu, On-Live, Facebook, Renren, Taobao, and many others. What software, including changes to the PS4 Operating System (firmware), should Sony develop to improve the value proposition of the PS4 in China? Which system features are likely to draw the ire of government regulators?

While Sony is both a hardware and software company, it may not need to compete on all fronts with proprietary software. What strategic partnerships should it seek with Chinese companies?

Over the past couple years, Sony completed its purchase of EMI, making it the largest music company in the world. It also recently acquired Gaikai, giving it a streaming solution for cloud-based gaming (PSNow). Acquisition, rather than contraction, is one strategy for a struggling company. Should Sony seek to purchase second party partners or third party competitors in China?

STRATEGIC MARKETING: From crying babies to Kevin Butler, Sony has seen massive swings in the success of its television commercials in the States. What should change with the new market? Is TV a viable channel? Social media? What kind of budget should Sony have for China? Are there innovative or clever strategies Sony should consider? How might the Chinese consumer respond to data-mining efforts, omni-channel marketing, partnerships with retailers, product bundles, etc?

Marketing the PS4 in China won't occur in a vacuum. What are we likely to see from Microsoft and Nintendo over the next year? How should Sony respond?

Due to the extended console ban and protectionist government policies, the Chinese public is likely to view gaming as a dangerous, unhealthy, foreign hobby. Can you market your way past that reticence?

TARGET DEMOGRAPHICS: Understanding who buys video game systems and games in China will be crucial to any new product launch. Who is Sony's core consumer in country? Should Sony seek, like Nintendo's Wii, to expand the market to casual gamers, non-gamers, or niche audio-visual enthusiasts? Should Sony focus on the traditional video game demo (teenage males) in China? Can Sony find a viable strategy to market to women or parents or some other expanding demographic? Are there ways to reposition the aging PS3 or Vita for different demographics? What about existing PC gamers? How might Sony lure them into the living room?

COMPETITORS: In hardware, it's (currently) Microsoft and Nintendo. In software, it's Electronic Arts, Ubisoft, Activision, Valve, Nintendo, Microsoft, Capcom, Konami, Sega, Vivendi, and on and on. All the major US players will seek a presence in the new market. Understanding all the games industry at large will be vital to creating a winning strategy for Sony. Will Tencent and QQ Games be a partner or rival in China? Anticipating the strategic goals of your competitors may be just as important as the creativity of your marketing concept.

FURTHER READING

To educate yourself about the games industry, consider the following online sources:

WWW.N4G.COM
WWW.NEOGAF.COM
WWW.JOYSTIQ.COM
WWW.GIANTBOMB.COM
WWW.IGN.COM
WWW.GAMETRAILERS.COM
WWW.GAMESPOT.COM
WWW.BEYOND3D.COM
WWW.METACRITIC.COM
WWW.KOTAKU.COM

For some excellent background reading, check out the Resources section of our Oncourse site. There you'll find excerpts from Tom Chatfield's *Fun Inc.* and Jane McGonigal's *Reality is Broken*. Good luck!

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