

VIDEO GAMES CONSOLE

The games console industry is divided into three periods. The first period is the growth of the industry to the advent of the 32 bit era.

The next period is the developments and trends during the PlayStation era and

the third is the likely development of the industry over the next few years

BRIEF HISTORY OF THOSE PERIODS and THEIR REVENUES *(The Evolution of the Game Console Industry)*

In 1994 , the first time that consumer electronics giant Sony had bravely attempted to enter the highly competitive games console market.

Going under the catchy, self-explanatory name PlayStation, **this 32-bit, CD-based system** hit Japan in December and faced tough competition from 'The Big Two' in the form of **Sega's** fundamentally similar **Saturn**, and **Nintendo's** upcoming Ultra 64.

By May 1995, barely six months after the release of PlayStation, over 1 million Japanese gamers had become converts.

Games like Toshinden, CyberSled, Jumping Flash!, and a host of other, decidedly more obscure titles (our favourite is Chou Aniki – Kyuukyoku Muteki Ginga Saikyo Otoko – literally 'Super Older Brother – The Galaxy's Absolutely Invincible Strongest Man') helped to propel sales, impressing players with their advanced 3D visuals and diverse gameplay.

By October, worldwide PlayStation shipments had reached 9 million, and with the arrival of huge sequels such as Tekken 2, Ridge Racer Revolution and Wipeout 2097.

In a year that saw cosmologists announce that the expansion rate of the universe was actually increasing, the expansion rate of PlayStation hardware and software enjoyed an equal upturn. At the start of 1998, worldwide software shipments hit a gargantuan 200 million units and, by the end of the year, hardware production was nearing the magic 50 million mark.

April saw the launch of the next evolution of the PlayStation controller: the Analog Controller – or DualShock as it's known by most. The twin analogue sticks provided scope for superior control in future titles, while the built-in vibration function meant that you could now effectively feel the effects of the action on-screen. By August it was officially declared the standard controller for the console.

As January saw PlayStation shipments passed the 50 million mark, development work on the technology behind its successor was nearing completion.

On 2nd March, SCE (Sony Computer Entertainment) announced that the research and development on the "next-generation PlayStation" was completed. It was confirmed that the new console would feature a state-of-the-art 128-bit Central Processing Unit – the "Emotion Engine" – at its core. It seemed that the dawn of a new era in gaming was fast approaching....

Sure enough, on September 13th, SCEI confirmed that its new home computer entertainment system PlayStation 2 would be launched in 2000, and would feature DVD playback, full compatibility with PlayStation games and USB ports to cater for all manner of accessories.

On December 7, 2001 on their press release, Sony Computer Entertainment America Inc. announced stronger than expected sales during Thanksgiving week, exceeding its original product forecasts despite the current economic conditions.

Based on sales reports covering the first holiday sales weekend, the company projects that total PlayStation category sales will bring in more than **\$1 billion in retail revenue during December 2001**. Consumers visiting retail outlets interested in new products chose the industry leading, trusted PlayStation brand, purchasing more than 317,000 PlayStation 2 units and 100,000 PS one consoles during the week of November 19. PlayStation 2 sales rose more than 62 percent from the week prior, demonstrating an increased consumer interest around the platform. This sales volume remained consistent for the week of November 26 as the company sold more than 321,000 PlayStation units, with PS one experiencing another 100,000-unit week during this period.

These latest sales findings bring the life-to-date installed base of PlayStation 2 in North America to more than 6 million units since its debut 13 months ago. PS one/PlayStation consoles can be found in more than one out of every three U.S. households as the company now has sold 31 million units to consumers.

Overall in 2001 forecasted that 66 percent or \$2 out of every \$3 retail console dollars will result from sales of PlayStation products.

For 54 months straight, the PlayStation business has been the sales leader in every category in which it competes. They maintained that success by providing both the PlayStation enthusiast and new consumers with a wealth of entertainment at affordable prices."

The “Big Two” Sega and Nintendo

In 1970, Sega Enterprises Ltd. was bought by Gulf & Western, and started making **coin-up arcades and software through the 1970's and 1980's**. In the 70's Sega would make a new game every year for arcades and home consoles. When Sega entered the videogaming market, they weren't the powerhouse, they were a small company compared to others. But they had some hits like "Turbo" which came with the Colecovision driving wheel.

In 1988, Sega gave another crack at the home console market, and by this time, government pressure forced Nintendo to allow third-party developers to make games for other systems. **But still, Nintendo own 90% of the market**, and Genesis sales were slow at the start. Also because Nintendo released the Gameboy in the same year.

In 1992, Sega CD is released, making it the first ever CD based home console. But the Sega CD failed to help the Genesis because of the lack of good games.

In 1993, the talk of 32-bit systems began to appear in Japan, so Sega began making the 32X. It was a add-on to the Genesis giving it 32-bit, it was released in 1994. Sales of the 32X were high during the launch of the 32X, but it didn't last long. Mostly due to fact of limited games, and that the 32X was piece of crap. **Sega is starting to lose grip in the market**, but since the release of the 32X, Sega's been working on a totally new system.

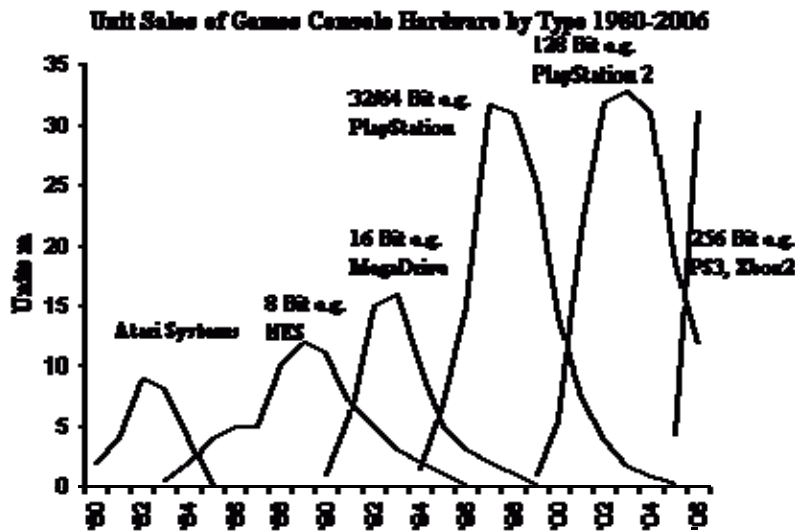
In November 22, 1994, the Sega Saturn was released, by Christmas, **500,000 Saturns** were sold in Japan. But that wasn't the same thing at the North American release in May 1995. The **Saturn was sold for \$400** American with Virtua Fighter inside.

Fall of 1995 saw Sony sticks its ugly face in the videogaming market with the release of the Playstation. But neither systems sold well, until E3 in 1996. Both companies announced they'll be dropping the price of their systems to \$200. Later that year, Sony updated the Playstation.

Next thing you know, everybodies buying a Playstation. Even though **5 million Saturns** were sold in Japan, Sega is in deep trouble. Sega was having financial trouble, almost going bankrupt at one point. In 1998, Sega launched the Dreamcast.

While Sony pulled in a revenue of \$36 billion over the period from 1995 to 2002 and Nintendo has pulled in \$32 billion, Nintendo's operating income was significantly higher than Sony's.

The global games software industry reached \$18.4bn in 2004 (excluding network games revenues). We anticipate this generation's cycle will see over 160m consoles (excluding portable game consoles) sold compared to the 140m of last generation hardware (PSOne, N64, Dreamcast)



Source: Sony, Games Investor Consulting Ltd

THE TARGET OR THE BUYERS OF THEIR PRODUCT

The average age of games players rose considerably during the period. In the UK, PC games players tended to the oldest with magazine reader surveys suggesting an average age of 27-31 (similar surveys in the US put US PC gamers at around 32-36 years old).

Playstation games players came next with an average age of around 25-20 (console user average ages begin high and tend to fall from there) with Nintendo the youngest at 18-15. A marketing refocus by Sony with greater emphasis towards club culture and "twenty-somethings" resulted in a much older initial PlayStation userbase than pervious consoles had achieved and this resulted in a broader social acceptance.

- This was, in no small part, helped by the wider appeal of games that the advent of detailed 3D graphics and CD-quality sound brought. The greater verisimilitude of games software (in particular driving and other sports games) allowed people to more easily associate with gaming experiences.
- The fact that the first generation of teenage games players in the early 1980s were then in their 20's and many are still active games players.
- The increased cost of computer and video games hardware putting gaming (certainly at the beginning of the cycle when hardware and software prices were high) out of reach of many children.

The average age of PC games players will continue a pattern of approximate 1 year growth per year whilst PlayStation games player average ages will continue to fall

towards the mid-teen level. New console launches result in the demographic cycle beginning again so PlayStation 2/ Xbox and to a lesser extent Game Cube gamers will start in the mid/late 20s.

THE BASIS OF THE COMPETITION

The basis of the competition is first and foremost the technology. Technology in terms of advancement in storage media ie. CD, Harddrives etc. , Data processing speed (bit wise), like Sega's 32 bit Saturn console (launched in 1994) and Nintendo's 64 bit N64 (launched in late 1996/7) & Sony's 32 bit PlayStation.

The price/performance level is also one of the main concern of the competition when Sega reacted by lowering the price of its console but the Playstation had built up too much momentum and, from an early stage, it was clear that Sega would struggle to match the growth of its rival's machine.

The Playstation quickly established a lead in the video games market outselling Sega and Nintendo's offerings by a vast margin. Sega re-entered the market with its 128 bit Dreamcast console but despite a strong launch in Japan in November 1998, publisher support lost momentum and Sega exited the hardware business in 2001.

THE MOST SUCCESFULL PRODUCT

The Playstation is the most successful product outselling the other 3 competitor. The PlayStation business has been the sales leader in every category in which it competes. They maintained that success by providing both the PlayStation enthusiast and new consumers with a wealth of entertainment at affordable prices.

Their marketing as mentioned earlier focus with greater emphasis towards club culture and "twenty-somethings" resulted in a much older initial PlayStation userbase than pervious consoles had achieved and this resulted in a broader social acceptance. The advent of detailed 3D graphics and CD-quality sound brought. The greater verisimilitude of games software (in particular driving and other sports games) allowed people to more easily associate with gaming experiences. And the fact that the first generation of teenage games players in the early 1980s were then in their 20's and many are still active games players.

BARRIERS WHY OTHER (specially small companies) CANNOT ENTER OF COMPETE IN THE GAME CONSOLE RACE.

The video games market (after 2001), on the other hand, has always been dominated by **(GIANTS)** proprietary standards, currently: Sony's Playstation 2, Nintendo's Game Cube and Microsoft's Xbox. The closed nature of these video game standards, coupled with the *reluctance* of the standard owners to release major hardware upgrades (to prevent

obsolescence) has and will continue, for the foreseeable future, to result in their limited shelf lives and the continued cyclical nature of the market.

WHY MICROSOFT ENTERS THE GAME CONSOLE MARKET

First, on the analysis of facts & events, Microsoft, a well known software developer for PC was well aware of the enormous revenues these game console companies were enjoying. The statistics clearly show the earnings and the wide market Microsoft can share along with its software development. It's a thriving business that Bill Gates cannot ignore and probably planned to beat its competitor.

An established billion dollar corporation like Microsoft won't have a hard time joining the bandwagon or beat the hurdles. It can easily touch the market spending 500 million dollars on advertising and promotions. Microsoft will automatically have its large shares in the market due to existing clientele and customer confidence over Microsoft Products.

Microsoft may never surpassed the triumph of Sony Playstation in the next few years but it will be a major player in the industry that Sony should always watch out.

According to published events before the launching of their first game console, Microsoft has been heavily hyping their upcoming gaming console, tentatively called the X-Box. Such hype in the industry is not unusual, however Microsoft's presence is. It is a significant departure for Microsoft which has previously concentrated on operating systems and software, leaving others to design and build the actual hardware and suffer the risk of failure.

The X-Box has some obvious design issues which makes it less than ideal as a gaming console when compared to the Playstation 2. Yet Microsoft is not a stupid company. Although they have blundered in various areas, they do not blindly enter new realms without considerable thought and their most spectacular failure left other companies holding the bag.

So why is Microsoft spending a significant amount of time, effort, money, and hype to try to make the X-Box a success, and placing themselves in a position to lose considerable quantities of money if it fails?

The X-Box's real benefit to Microsoft is as a PC replacement which they have complete control over the software which runs on it, including a revenue share of all third party software sales and the ability to limit what software is allowed to run on this platform.

What the X-Box is good for?

Although the X-Box's design makes it an inferior game console when compared to the Playstation 2, it is significantly superior as a general purpose thin Workstation or PC replacement. All the features which make it poorly suited as a video game console (more memory, the hard drive, the over engineered video system, a high performance general purpose processor, and Windows 2000 as the operating system) makes the X-Box the best PC replacement currently proposed by anyone.

Microsoft has denied that the X-Box is intended as a home PC replacement and lightweight workstation, but it is designed like one. Why else would one support such high resolution video output? Why else would the design so eagerly embrace a standard CPU? Why else would one use Windows 2000 instead of Windows CE (a much smaller and lighter Microsoft OS which is designed for, among other things, video game consoles like the Dreamcast.)?

It is hard to believe that Microsoft hasn't considered this in great detail, and is planning on using the console market as an entry point for creating a viable Post-PC computing device, especially when one considers the advantage the X-Box presents to Microsoft.

Why Microsoft wants the X-Box to succeed?

The complete control over the hardware makes life considerably easier for the OS implementers at Microsoft, but this is hardly worth the costs associated with a console. Game consoles are traditionally sold at cost or at a loss, with the revenues coming from software licenses, and the X-Box is no exception. Control over the hardware platform, although a nice side benefit, can't be a primary motivation since the hardware itself is a loss leader.

Unlike the conventional Windows world, consoles are much more constrained in terms of software approval. All software for a Playstation is licensed and approved by Sony, and Sony gets a share of the revenue for each sale. The same applies to Nintendo, Sega, and the X-Box.

In the Windows world, Microsoft does not have a veto over applications published, and does not receive a share of the revenue from third party applications. But it will on the X-Box. Although a significant advantage for any console maker (it is the primary source of revenue, which keeps providing income long after the box has been sold to the consumer), it becomes an immense resource for Microsoft if the X-Box becomes a PC replacement.

Assuming that the X-Box does end up acting as a PC replacement, does anyone believe that Microsoft would approve a version of Quicken to run on the X-Box? Unlike games, where people will buy both Unreal Tournament and Quake 3, hardly anybody purchases two separate word processors or accounting packages. Being able to, by fiat, exclude application competitors from a platform is an immense advantage for a company which makes a huge percentage of it's revenues from applications.

Undoubtedly there would be both legal and technical challenges to such a policy, but these would be unlikely to succeed in challenging Microsoft. Microsoft could easily engineer the X-Box to only run programs which have been approved by a public key signature by Microsoft. Short of modifying the box, the OS, or obtaining the private key, it is unlikely that unauthorized programs could be made to run on this system. And the legal challenges would probably last for years, making a legal victory against Microsoft moot by the time the case is settled.

Even if Microsoft did approve competing applications for deployment on the X-Box, the console model insures that they still gain a share of the revenue. *Although Microsoft would undoubtedly prefer people to run Microsoft Money instead of Quicken, they would not object so heavily if either sale resulted in revenue to Microsoft.*

*It is inconceivable that Microsoft has not thought this through. They can not intend to go head-to-head against Sony, with a marginally inferior product, a year late, and expect to do more than lose money on the endeavor. **There must be an ulterior motive.***

A Windows based, PC replacement, which Microsoft obtains revenue from all software sales and maintains a veto power over competitors is a dream come true for Microsoft.

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Why the X-Box could easily fail and Why Microsoft so greatly desires a success

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