

Main threats and opportunities to microsoft xbox management essay



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Microsoft entered video game industry with the launch of Xbox 2001 and 2005 it continued to launch the new version of Xbox 360 (Euromonitor 2009). As new comer, Microsoft runs the business successfully and becomes one of the three companies that dominant the console hardware market. However, with increased competition and more and more similarities in products between console game companies, there is an urgent need to come out with an innovation strategy to enable Microsoft surpass competitors and become the market leader.

The aim of the project report is to design an innovation strategy for Microsoft Xbox which contains business of Xbox 360, Xbox Live, software and accessory for Xbox. The sources of data come from books with topic in innovation and internet which contains database such as ABI Inform, annual report, company websites and electronic journals. The project takes two months and be divided into six sections to analyze. In the first part, main threats and opportunities of Microsoft's Xbox business will be examined, followed by its strengths and weaknesses to help to make competitive strategy in the third section. In the forth part, an innovation strategy will be designed. In the fifth part, the allocation of resources will be analyzed to support the innovation strategy. Finally, how to implement the strategy will be discussed.

Main Threats and Opportunities to Microsoft Xbox

2. 1 PEST analysis

2. 1. 1 Political:

Political factors play an important role in any business, especially regulations. For video game industry, the key challenge is that there are no strong regulations against piracy by illegal manufacturers and individual game players, especially in Asian countries as well as Eastern Europe and Latin America (Business Insight 2009: 37). This usually brings huge loss to video game companies.

2. 1. 2 Economic:

Game console industry is a booming industry, but recent financial crisis brings negative effect such as decrease in revenue and profit. As Microsoft CEO Ballmer (2009 cited by Swisher 2009): "...we are not immune to the effects of the economy. Consumers and businesses have reined in spending, which is affecting PC shipments and IT expenditures."

2. 1. 3 Social:

Nowadays see a trend that more and more women and people over 35 play games. According to Casual Games Association (cited by Business Insight 2009: 74), women take up 51% of casual players and People over 35 are the majority players compared with young people. Also people tend to play games with friends and families (Business Insight 2009: 73). Moreover, more people support a healthier lifestyle, for example, employers offer incentives for employees to have a healthier lifestyle such as doing sports (Kentent n. d.).

2. 1. 4 Technology:

Microsoft's Xbox works around the help of technology every day. Despite the fact that the innovation in the gaming industry is restricted, the speed at which the technology gets transferred is very fast. But the main problem to develop any technology is the huge cost that is required to upgrade.

Microsoft should use new technology to conduct R&D which will help the business to create new innovation products.

Porter's Five Forces Analysis

2. 2. 1 Threat of new entrants:

The barriers for new competitors entering into the game console market are very high. In fact, the console segment is controlled at both hardware and software levels by the big three-Microsoft, Nintendo and Sony (Williams 2002: 44). These giants release systems incompatible with others thus creating barriers for new comers. Other sources of the high barriers are cost and distribution. A deep pocket is necessary to compete in the gaming industry. For example, Microsoft spent about \$4 billion to launch Xbox (Euromonitor 2009).

2. 2. 2 Bargaining power of buyers:

The bargaining power of buyers is moderate. For one thing, most video game consumers are between the ages of 15-25 years. They are price-sensitive because parents play an influential role in the purchase decisions. In fact, a slight decrease in the price of the product has a greater impact on the sales level. Take 2009 for example, PS3 and Xbox's sales jumped by 104 per cent and 32 per cent respectively because of the price cut (Stevens 2009). For

another, the choices available for consumers are few, mainly from the big three. Thus, the main manufacturers have considerable bargaining power to consumers.

2. 2. 3 Supplier bargaining power:

Microsoft is one of the tree biggest console game company. Some of the specialized parts of Microsoft are developed by the suppliers, but the most fundamental and complex components are kept under Microsoft's control. Therefore, the ability for suppliers to bargain price with Microsoft is weak. Facts show that suppliers such as Nvidia, supplier of chipsets, can not refuse Microsoft's demand on Xbox design (Murphy and Morrison 2002).

2. 2. 4 Competitive rivalry within an industry:

The major rivalry of Xbox 360 is Nintendo and Sony (Business Insight 2008: 40). Nintendo is the market leader with ability to sell the products at a cheaper price and popularity with causal players (Business Insight 2008: 40). In the game console industry, the market is oligopolistic in nature. In such a market condition, there is room only for a few successful companies. Another important aspect in this industry is product differentiation. Due to high competition, price drop strategy is just used to attract new customers.

2. 2. 5 The threat to substitute products:

Console game industry where Microsoft Xbox exists is just one of game type in the game industry. Thus, for game players, they can play games through mobile phone, PC, online, DC (Nintendo) and PSP (Sony) rather than console. The threat to substitute products for Microsoft Xbox is high. It needs to bring different experience for game players with technological innovations.

The PEST analysis and Porter's five forces analysis above mainly focus on the condition of the whole industry and Xbox department respectively.

Meanwhile, in order to make a new strategy which can apply to Microsoft's gaming business, the analysis on its strengths and weakness is necessary.

Strength and Weaknesses of Microsoft Xbox

There are three primary competitors for the home console market: Sony, Microsoft and Nintendo. Therefore, when considering the strengths and weaknesses of Microsoft's Xbox 360 its technological innovation can be compared with its two main competitors. In the next part of this report, detailed comparison will be given in terms of resources and processes for technological innovation among these companies.

Technological resources are the foundations for any technological innovation. Microsoft has the tradition of emphasizing on its R & D investment: For the last decade, its average annual R&D spending as a percentage of revenue was around 17 per cent, while that of Sony was about 6.5 per cent (Wilson & Herrman 2010); for 2010 alone, Microsoft plans to spend \$9.5 billion on R & D, which is at least \$3 billion more than Sony (Berridge 2010). Sufficient cash investment including \$1 billion for Xbox 360's hardware problems fuels Xbox products' incremental innovation. These are the key strength of Microsoft over Sony and Nintendo,

Game development teams in Microsoft Game Studios are another important technological resource for the success of Xbox products. The studios are composed of in-house game developing teams and third-party partners. In-house teams from acquisitions had brought in Microsoft talented people. For

example, BigPark provided Microsoft with over 80 years of collective experience in the video game industry (Microsoft News Center 2009). In addition, Microsoft also collaborates with successful third-party partners like the developer of Halo- Bungie and its hardware partners like ATI. Furthermore, this collaboration also includes managerial expertise to help in exchange of innovative ideas (Berardini 2006).

Process management is the next step for technological innovation. As the world's largest software company, Microsoft has developed many platforms to offer solutions for project and supply chain management. Typical examples are: In order to gain efficiency for Xbox 360 launch, Microsoft used Project Management System (PMS) solution to track project schedules and establish collaboration between over 90 functional groups (Microsoft 2006). In terms of supply chain management, Business Integration and Intelligence (BII) Framework raises the on-time delivery by 20 per cent, it helps to cut inventory costs by 10 per cent and development time by 50 per cent. It also helps to increase RIO by 126 per cent and productivity by 20 per cent (Microsoft 2006). This is a reliable way to predict demand and plan production. By contrast, Nintendo has problems with its supply chain management. Wii's supply was always below customers' demand (Reisinger 2009). In addition to in-house idea generation, Microsoft adopts XNA Game Studio Express to absorb creative game ideas by providing the necessary tools to hobbyists, students, indie developers and studios (Microsoft Xbox n. d.).

Microsoft's weaknesses falls on high-rate hardware problem complaints. As one analyst commented: " Microsoft is a software company at heart, not a <https://assignbuster.com/main-threats-and-opportunities-to-microsoft-xbox-management-essay/>

hardware one” (Couch Campus 2009). According to SquareTrade’s survey of 16, 000 game consoles, Xbox 360’s failure rate at 23. 7 per cent was far higher than its rivals (PS3 10 percent, Wii 2. 7 per cent) (Thorsen, 2009). Microsoft prefers to tackle things in software terms. As for the hardware, it’s usually left to a smaller team (Couch Campus 2009). By contrast, Sony has been in the business of producing consumer electronics for years and is better at solving hardware problems. Therefore, Microsoft has to focus incremental innovation on hardware quality improvement.

From this brief comparison, it’s fair to conclude that Microsoft has much strength. At the same time, it inevitably has some weaknesses comparing to Sony and Nintendo. Therefore, our recommendation for Microsoft is to make good use of its resources while not forget to work on its weakness and improve to develop in the highly-competitive gaming industry.

The analysis above shows that, in order to overcome Microsoft’s weaknesses and optimize its advantages, an effective competitive strategy is essential.

Technological Innovation in Microsoft’s Competitive Strategy

Microsoft game sector should pursue the competitive strategy of differentiation. The strategy of “ cost leadership” is not suitable for Microsoft. Nintendo retains the advantage of low price because it lacks various components such as DVD playback and incorporated hard drive which is some of the main features of Xbox (Furness, 2008).

Differentiation strategy refers to the strategy of developing unique products and service valuable for the buyers, thus making the buyers willing to accept

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higher price (Dess and Davis, 1984). The differentiation of Microsoft game sector should embody in its target market and product delivered. For uniqueness of its market, Microsoft should develop games which deliver interactive entertainment. For its product, the games should adopt the concept of interaction, entertainment and healthy life-style.

4. 1 Market:

Nintendo Wii's target market was kids (1) but has expanded it into the older people segment as well (Sabbagh 2006) while Sony play station 3's target market is men of the ages 15-30 (Moats, 2008). Regarding to Microsoft console game, it should target all segments of people (Afan 2010). Video games are no longer being regarded as a mean of self-entertainment but the way of interaction with family and friends as well (Business Insight 2009). In the US, the percentage of interaction game players was creeping up by 8% from 2006 to 2008, while in Europe, the percentage of parents interacting with their children below 16 with video games is 81%, with Finland exceeding 90% and UK reaching about 83%.

4. 2 Product:

The concept Microsoft should adopt in developing its products is products advocating interaction, entertainment and healthy life-style. People now are pursuing a healthy life-style, which can be achieved through sports (Robson 2001). However, the current video game is detrimental to players' physical health since it makes the players sit in front of the screen (Stromberg n. d.). Nintendo produces the motion-sensitive system but with physical controller (Terdiman 2009). As Spielberg said (cited in Terdiman 2009), most people are too intimidated to play games with controllers. For the rest 60% of <https://assignbuster.com/main-threats-and-opportunities-to-microsoft-xbox-management-essay/>

household without console games, the only way to make them accept them is to make controllers invisible. Therefore, Microsoft should develop products with hands-free controller system providing healthy entertainment.

4. 3 Sustainable differentiation strategy

According to Grant (2000), the sustainable competitive advantage of firms is the major factor of inter-firm profit differentiation, requiring the barrier of imitation to competitors (Porter 1985). In the process of shaping it, the inimitable bulk of resource and capabilities play an important role, which is resource-based view (Porter 1985). As mentioned above, the combination of Microsoft's deep pocket, favorable brand reputation, technological innovation, strong in-house game development teams with successful third-party partners creates the sustainable competitive advantage. The role of technological innovation in forming competitive advantage is discussed in detail in the following part.

4. 4 Role of technological innovation

Technological innovation generates the uniqueness which is necessary for differentiation strategy, making the products superior to those of competitors (Murray 1988). The technological innovation in Microsoft games will contribute to the success of differentiation strategy. However, the differentiation strategy relying on the high-tech products cannot maintain sustainable growth (Murray 1988). A sustainable differentiation preventing competitors' to imitate is needed, which can be achieved through creating products that are difficult to imitate and should achieve imperfect mobility (Johnson, Scholes and Whittington 2005) via technological innovation.

Imitation barriers can be created through situation development (Johnson, Scholes and Whittington 2005), which can be further achieved by technological innovation in different business units combined together. For Microsoft game sector, the technological innovation such as Microsoft platform for opening innovation (Microsoft 2007) and other Microsoft software like Microsoft® Office OneNote® 2007 are the central repository (Barrett 2009) which contributes to the creation of imitable strategic advantage.

Imperfect mobility can be achieved through switching cost (Johnson, Scholes and Whittington 2005). Microsoft can raise the switching cost through the technological innovation in accessories.

For example, Xbox 360 black wireless controller is \$64.44, creating high switching cost of Microsoft Xbox360 (1).

Innovation Strategy for Microsoft Xbox

To support the differentiation strategy, an innovation strategy in which technological innovations play an important role is imperative. According to Dodgson et al (2008: 104), innovation strategy can be distinguished as proactive strategies, active strategies, reactive strategies and passive strategies. The innovation strategy we choose is active strategy which mainly contains incremental innovations and combines some radical innovations. For one thing, traditionally, Microsoft uses active strategy (Dodgson et al 2008: 105). For another, acting as technology leader needs more radical innovations which will cost a lot of time and resources that Microsoft Xbox may not sustain.

Traditional software and hardware in console game which are restricted to TV and sitting playing method are not qualified enough to realize the goal in differentiation strategy which aims to advocate interaction, entertainment and healthy life-style. Therefore, some radical innovations are necessary to break these restrictions. For example, Natal, an undergoing project of Microsoft, turns the game players themselves into controllers with a camera tracking users' movement and voices reorganization (Paul 2009). This new technology breaks the traditional playing method and encourages game players to use the whole body to play games, which gives them a healthier life. If it combines sports games, it will put entertainment into physical exercise, which improves the health and entertainment concept.

In addition to radical innovations, in our innovation strategy, incremental innovations play a leading role because they are easier to achieve. They mainly help Microsoft to improve its products in both hardware and software. Innovations in hardware can be complementary to the radical innovations or the upgraded version of existing products, for example, making the console Xbox portable, enlarging the capacity of the memory stick, more hardware accessories, etc. And innovation in software should focus on the new product concept and the customer group to encourage interaction between group players.

Both internal and external resources can be used for these innovations.

Radical innovations should rely on in-house intelligence because radical innovations such as Natal will bring significant change in the competition and they should be kept secret before launch. Moreover, internal development of radical innovations and some incremental innovations for Xbox can take <https://assignbuster.com/main-threats-and-opportunities-to-microsoft-xbox-management-essay/>

advantage of Microsoft itself which has dominant position in software development. While external resources can not only save cost but also offer external innovations. They can come from universities, customers themselves and other companies, especially start-ups which focus on technology development.

The innovations described above can be developed through strategic integration which involves customers and suppliers and technological integration (Dodgson et al 2008: 64). The involvement of customers and suppliers helps to understand customer demand and generate ideas for innovations. Microsoft can integrate suppliers' technology and listen to customer needs like how group players want to play with each other. Technological integration may in forms of new technology that combines different knowledge base or involves elements of innovation process. Therefore, Microsoft can consider this way to drive innovation. For example, OnLive, the technology of " cloud game computer", can work on Xbox 360 (Keighley 2009). Microsoft can combine its knowledge base into new technology. Another approach is open innovation. Open innovation that encourages external intelligence can help Microsoft reduce risk and combine external innovations into internal product development. For example, some casual games can be developed by talented game players themselves and shared through Xbox Live or Xbox community. Another consideration is collaboration with SMEs, universities and NGOs to scale up solutions.

The last step of the innovation strategy is to commercialize innovations.

According to Tidd et al (2005: 154), the effective commercialization of an innovation depends largely on complementary assets, namely competencies
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in production, marketing and after-sales support. Take Natal as an example. When it is developed, it needs a series of complementary assets to support its launch. Firstly, in light of the high failure rate of Xbox 360 as mentioned above, the company should set up a department of quality control in the manufacturing plants to censor the production process and improve product quality. Secondly, the marketing strategy can target group players. Advertising can be done through networking such as Facebook which has partnership with Microsoft (Xbox 2010). Experience center for Natal can be set up when Natal is launched to attract more Xbox players. Finally, after-sales service is also important. For example, women and older people may resist complex technology or game operation. Services such as easy instruction in website and manual in products and guide in experience center can help reduce understanding difficulties for them. Other services such as maintenances for hardware failure are also necessary to solve quality problems.

Allocation of Resources

The innovation strategy cannot be implemented without appropriate allocation of resources to support it. In order to develop a R&D budget for the next 3 years we take the previous two years as the base year. Since R&D expenses of 1H2008 and 1H2009 were 678 and 929 million dollars in entertainment and Device Division of Microsoft respectively (Bishop 2009) Xbox is one of the tree businesses of EDD, R&D expenses for Xbox in 2008 and 2009 were approximately 452 and 619. 2 million dollars respectively. Since, Natal is going to be launched in 2010 (Xbox 2010), therefore R&D expense should be increased in order to support the Natal project, but the

expense should be decreased in 2011 because there is no urgent need to launch new technology. 2012 will see increase in R&D budge to continue to develop more innovations. The investment of R&D will go to tree resources for innovation, namely human resources for R&D expertise, technological intelligence from collaboration with technology leaders, customers, suppliers and R&D staff of Microsoft and finally R&D facilitates such as R&D center.

R&D expense

2010

2011

2012

Budge (million dollars)

712

640.8

717.7

Growth rate

15%

-10%

12%

When resources for innovation are decided and then allocated, time frame should be considered. Here, three factors are considered in allocation of resources in different time frame. First of all, different level of risk and uncertainty of innovations require different amount of resources in different time frame. Theoretically, innovations which contain high level of technological uncertainty or market risk should be allocated with less resources and on long term basis, for example, the innovation to realize interaction virtually between Xbox players is a long term goal. While many incremental innovations which are easier to achieve should be allocated with more resources and on a shorter span of time in order to gain their reward quickly, for instance, the development of games for group players in shorter span of time. Secondly, the allocation of resources should be consistent with the company's business strategy. The success of Nintendo's Wii with its emotion controllers has stimulated Sony and Microsoft to develop emotion controllers of their own (Harding 2009). Microsoft's reaction is the project Natal. And after the expected launch of Project Natal as mentioned above, the following one or two years will be the optimization and commercialization of Project Natal with more funding to it. For example, more games that can work with Natal should be developed since most of games on the market today may not work with Natal, which shows urgency for Microsoft in the short term. Thirdly, the last consideration is the response of competitors. Sony and Nintendo haven't followed Microsoft to develop Natal. Instead, Nintendo improved its controller into Motion Plus add-on and Sony went with Sony Station Move (Nintendo News 2010). It indicates that there will be a battle of hardware and software among these three console game

developers. Therefore, the majority of resources for R&D are needed in short term to improve products and gain competitiveness.

Further, different types of R&D projects will be set up to support the innovation strategy. According to Tidd et al (2005: 221), three types of R&D projects are worth financing, namely knowledge building, strategic positioning and business investment. Knowledge building needs scientific experts to judge which kinds of technology will generate future opportunities and develop it through exploratory research. They are full of uncertainties and risk but necessary since they may nurture radical innovations that change the industry standard. Strategy positioning project can drive new business through applied R&D with careful market research which helps to reduce risk. For Microsoft, new business opportunities probably exist in new customer group and the changing lifestyle which pursues health. Therefore, programs that belong to strategy positioning project should capture these opportunities with adequate innovations. Business investment is the project to develop and commercialize radical or incremental innovations which shows possibility and less risk. For instance, when project Natal is launched, business investment project will be in charge of the further development, production and marketing of project Natal.

Finally, decisions should be made about the funder of R&D. Theoretically, it will be better that the corporate could fund R&D projects like knowledge building since they are highly uncertain and the corporate has broaden technology capabilities to judge which field of technology to step into, while division is in charge of projects like strategic positioning and business

investment because they need to be consistent with division's strategy and <https://assignbuster.com/main-threats-and-opportunities-to-microsoft-xbox-management-essay/>

they are less risky for the division. For example, Microsoft has already scanned the future technologies that it needs to develop, namely, cloud computing and software plus services, natural user interfaces, natural language processing etc (Microsoft Corporation 2009). For Microsoft with five divisions, division is suitable to fund strategic positioning and business investment since it has specific industry knowledge and interface with customers and suppliers, which helps it to target R&D projects.

The new innovation strategy is useless without effective implementation. Therefore, in the next part of this project report, how to implement the new strategy successfully in a cost-effective way will be demonstrated.

Implementation

In order to implement the innovation strategy successfully, top managers need to understand the pressures for and against strategy changes within the Entertainment and Devices Division. By carrying out the new innovation strategy implementation, top managers need to strengthen the forces supporting a decision, and reduce the impact of opposition to it^{1/4}^Kurt 2007^{1/4}%.

7. 1 Force field analysis

7. 1. 1 Forces for the innovation strategy:

According to Teece (1986), technological innovation is the core reason for Microsoft's thrive, so forces for the innovation strategy would be huge. The top management of Microsoft and the gaming department would be one of the most powerful forces which support the new strategy in respect of that the new innovation strategy, which values incremental innovations in one

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hand, encourages radical innovations in the other hand; and the decision to promote Natal would endow absolute competitive advantages to the Xbox department. Besides this, the Natal camera which “ uses special sensors and software to track body movements” ¹/₄MSFT Annual Report 2009¹/₄ is more advanced and sensitive than an accelerometer and the company is “ trying to get as close as possible to (an) ‘ impulse buy’ price ” (Cnet News 2009) Sales and marketing departments would feel much easier to promote new products rather than old games and consoles which are already mature and less attractive. What’s more, the strategic integration of internal and external human resources and R&D would be very helpful to realize resource optimization because this means the company could maximize the volume of innovations by absorbing both internal and external ideas in a cost-effective way.

7. 1. 2 Forces against the innovation strategy

Under the condition both Nintendo and Sony have given up the idea of developing a product such as Natal because of its huge costs and uncertain future (Nintendo News 2010), the financial department of Microsoft, considering the risk of long-term benefits, would face a lot of pressure of long-term investment on Natal’s R&D, marketing and advertising, especially when Microsoft committed to control costs in 2010 ¹/₄MSFT Annual Report 2009¹/₄%. Moreover, as Microsoft made adjustments to its cost structure through strategic job eliminations (MSFT Annual Report 2009)¹/₄CE engineers and other staff who are not involved in the new strategy implementation could fall in to panic that they are not important to the company anymore. Besides this, some of employees would

probably be afraid of technical changes because it means, in order to maintain the whole department's competitive advantage, they have to accept extra training and learn more about the new technology. What's more, although according to prediction, the natal cameras' strengths would give Microsoft " a huge advantage in the battle for consumers' dollars" (Lange 2010), during the promotion period of Natal, the marketing department may have problems with effective product promotion as many customers are not familiar with the new hardware and may hesitate to purchase the natal camera and related accessories. Moreover, many customers may doubt the future of Natal so some of them would not purchase it immediately because, as a radical innovation, there are currently few games that can be played through Natal and the game's quality and game play still remain to be seen as well. The strategy of setting up a quality control department in the manufacturing plants would push the company to confront the human resources problems as well as financial problems.

According to the Force Field analysis above, in order to implement the new innovation strategy successfully, managers need to be aware of the culture of the gaming department to ensure that the subculture is applied to the culture of the whole company. This encourages technological innovation because such kind of culture is a strong power that can encourage employees to accept new technological ideas and innovations (Gelder 2007). Besides this, the investment plan should be made in detail according to both long-term and short-term goals and the investment on employee training should be increased. More professional engineers ought to be

employed considering the condition that both radical and incremental innovations require high technology and detailed design. Moreover, the company needs to enhance the cooperation with game suppliers so that more games applying to Natal can be produced. Last but not least, more communication between different departments and within the gaming department is crucial so that everyone knows what is happening-staff can align their behavior to the new strategy while the marketing department can make a promotional plan according to the R&D achievements and to the whole financial conditions.

All in all, top managers need to do everything necessary to make sure the forces for the new innovation strategy can outweigh the forces against the strategy, and the stronger the supportive forces are, the easier the implementation of the new innovation strategy.

Conclusion

To conclude, the above analysis has studied the feasibility and implementation for Microsoft Xbox to adopt a differentiation strategy in terms of market and product differentiation. It's true that the gaming industry is getting mature and consumers' needs are changing fast. It's also true that Microsoft has strong bargaining power to both suppliers and consumers. If Microsoft combines this power with sufficient financial and human resources, this strategy can be feasible. To implement this strategy, an active technological innovation by utilizing in-house intelligence and external resources is the key. However, proper allocation of the resources is a big challenge. To overcome this challenge, strong I