

# Reasons for the closure of blockbuster



**ASSIGN  
BUSTER**

Blockbuster faced a situation not unlike other companies in the context of increased competition and changing consumer demands. How they did or didn't react, in both good and bad ways, to these changes played a role in the ultimate demise of the once ubiquitous movie outlet. Blockbuster's leadership became obsessed with capitalizing on a retail merchandising strategy as a way to increase profits from the real estate they were invested in. However, they lost sight of the fact what they really were was a conduit to provide entertainment and movies. In the end, customers defected to other companies that offered the same product, entertainment and movies, in a more convenient package at a greater perceived value. Customer's didn't associate a value to visiting a store location above the convenience of how quickly they could get the movie they wanted to see. While some parts of Blockbuster's leadership saw this and tried to adjust the company's focus, there was not a full commitment from the board of directors that allowed them to fully pivot into new distribution channels opened by technological advances.

Going back to the early days of VCRs and movie rentals in some regards it was a political factor settled by the US Supreme Court that created a safe legal framework for the home use of VCRs. The movie studios argued against the use of VCRs in fear they would erode their profits. As a result, as the home VCR market took off studios released movies at high price points (often \$79-\$99) that discouraged most consumers from buying them and drove increased demand at rental stores who paid the higher price because they would make a profit on the rentals. A political factor that had an effect on Blockbuster's eventual failure was the spread of broadband internet

access through both market forces and regulatory pressure placed on the telecommunication industry to spread broadband internet access across the nation, including traditionally underserved rural and urban areas.

Additionally, the impacts of net neutrality would eventually be felt later in Blockbuster's life as unfettered access to an open internet without data speed throttling was crucial to Netflix distribution model. <https://www.forbes.com/sites/ethangach/2013/11/07/video-rental-might-survive-streaming-even-if-blockbuster-didnt/#5db6c98e5db6>

Economic factors that had both positive and negative impacts on them were a strategic deal Blockbuster negotiated with the movie studios for revenue sharing a portion of rental sales in exchange for low cost availability of movie titles and a 28-day exclusivity on new releases. This gave them a strong upper hand as their competitors needed to spend larger amounts on purchasing titles as could only sit and watch as customers went to Blockbuster as new releases hit the market. However, a negative economic decision by Blockbuster was the reliance on late fees as a revenue stream. This created a situation where the company is financially reliant on penalizing their own customer thereby creating a motivation for some customers to defect when other viable options enter the competitive landscape.

From a social aspect, Blockbuster was a major part of the entertainment psyche and at its peak it seemed difficult to drive across a major town without passing at least one Blockbuster store. "Make it a Blockbuster Night" was more than just a slogan quickly after it debuted in 1993.

However, the social aspect of entertainment also started to shift brought on <https://assignbuster.com/reasons-for-the-closure-of-blockbuster/>

by changes in technology, specifically the spread of broadband internet access. Not only was the internet a threat to movie distribution through online streaming and piracy, it was also a threat as it became an entertainment source in and of itself.

As mentioned above there were technological change affecting Blockbuster from the growth of broadband internet access, but there were also changes in movie format that affected them. First to capitalize on technological changes in broadband internet access Blockbuster entered into a partnership with ENRON in the summer of 2000 (LA Times article) to provide Video-on-Demand directly to customer's homes. However, Blockbuster leadership was not fully behind the strategy (ENRON Tech Talk article), preferring instead to continue strengthening their retail distribution model, and the partnership was cancelled just eight months later (LA Time article) . Another technology change that affected Blockbuster was the shift from VHS cassettes to much smaller and lighter DVDs. The advent of DVDs made it possible for mail delivery of movie rental on a large scale with lower costs than mailing bulky VHS cassettes. This shift played into the favor of Netflix.

As Blockbuster attempted to pivot their business model toward online DVD rentals and in response Netflix filed a patent infringement lawsuit in 2006 for copying their online rental business model(Ars Technica). Blockbuster countersued (Daily Tech) on anti-trust grounds and both companies were locked in a legal battle for over a year at a time when both companies were in need of capital. (NETFLIXED p168-170, p211) In the end the two companies settled the suit with Blockbuster able to continue pursuing their online rental program Total Access.

One factor that did not have a significant effect on Blockbuster was environmental concerns. While there is almost always an environmental impact of most businesses there were no major concerns that played a key role in Blockbusters success and eventual failure.

The video rental business that Blockbuster competed in had multiple forces that helped shaped the market. The threat of entry was there from new competitors coming into the video rental market. While the cost of meeting Blockbuster on their own terms with a widespread retail location was a barrier to new entrant, new technologies and marketing opportunities such as mail deliver, kiosks, on-demand and streaming provided competitors the ability to enter the market without the real estate investment Blockbuster made. This lowering of the barrier kept competition alive as Blockbuster pursued largescale expansion buying up independent stores and small chains.

In terms of buying power for the consumer as new competitors entered the market the buying power of consumers rose. This was evidenced in 2006 when Blockbuster offered a \$7. 99 per month plan for one rental at a time inciting Netflix to come in even lower with \$4. 99 per month for two movies at a time. In this way, the consumer benefited as these rivals battled for precious subscribers even at the cost of lost profit margins. (Netflixed p172)

When Blockbuster first opened in 1985 they removed the barrier of cost as they embodied the threat of substitution for their competitors. By not charging a membership fee there was no economic penalty for a person to try Blockbuster even if they already had a membership at another movie

rental store. However, the cost of substituting rental with buying declined as DVDs became less expensive. This was a real threat to Blockbuster as low cost DVDs hit retail outlets. The substitution in this case was the ability of consumers to substitute purchasing DVDs instead of renting them. This makes it more than just a competing rental distribution. By making many titles available in a cost only marginally greater than the cost of rental and in a format easier to store than larger VHS tapes, studios and retailers, to a degree, created a substitution to the entire rental model. To a lesser degree piracy was always a potential substitution to rentals. As DVDs made it even easier to copy and share digital content, prior to more sophisticated DRM encryption used by studios, piracy continued to erode studio and rental company profits. This came in the form of black market DVDs and torrent sharing sites. Another threat of substitution was the internet as an entertainment source. Whether it was gaming, user created content, social media or streaming video, the introduction of broadband internet access in the late 1990s exploded in popularity in the early to mid-2000s.

As the primary creator supplier of movies, the movie studios have an upper hand in the movie rental business from setting the prices to making deals with specific companies for exclusivity for a period upon initial release. Bestbuy had a competitive advantage from deals struck with the movie studios. They entered a revenue sharing agreement passing a portion of revenue to the studios in exchange for lower cost of DVDs and 28-day exclusivity of newly released titles. This allowed them to stock more copies of titles at a lower cost and have exclusive distribution before competitors could make the titles available. Another aspect of the supplier power movie

studios held at the time was the effect on rental profits based on the quality of movies produced and released. If the previous year's theatrical releases were weak it had a direct impact on demand in the rental stores and bottom line profits. (Netflixed p. 157)

As mentioned above in relationship to Buyer's Power competitive rivalry was, and still is, present in the video rental market. While Blockbuster went out of business other entrants have moved in offering additional competition to the new incumbent, Netflix, and providing additional consume choices. There has even been a mild revival of independent brick and mortar video rental stores, many of which offer more obscure titled than can be found on mainstream streaming services (Amazon, Netflix, Hulu, Sling, DirectTV Now etc.)

Analyzing Blockbuster in relation to the STP framework; the video rental industry rose from providing a reasonable priced alternative to purchasing VHS cassettes, often prices \$79-\$89 in the early to mid-80s, to a segment of movie lovers that owned VCRs but couldn't, or wouldn't, pay the original release prices. While Blockbuster appealed to a broad range of movie and entertainment lovers they placed a strong focus on marketing toward families with certain tactics. Here are two examples. First, in an effort to promote a family friendly environment Blockbuster refused to carry adult X-rated movies even though they were a profitable portion of the product of other retailers. This helped separate it from many smaller independent rental stores that did. Secondly, Blockbuster offered discounted children's movies which appealed to many parents when picking up movies for themselves. In addition to movie lovers, Blockbuster also appealed to gamers by renting out

<https://assignbuster.com/reasons-for-the-closure-of-blockbuster/>

both games and consoles. This is consistent with them positioning themselves as an entertainment provider.

The target markets were families and many stores were placed within neighborhoods to be close to the customers and add convenience. It made sense to place stores in areas convenient to the customers but if you take that a few logical steps further what you really need to do is meet the customer where they want to be when consuming the product which is primarily at home. If being close to home is convenient, being in the customer's home is even more convenient which is what mail delivery, on demand and streaming options provide.

Relative to their customers Blockbuster positioned themselves firmly in the retail environment. They emphasized what they saw as the benefit of being able to stop in to get a movie and wanted to make Blockbuster the one stop shop for entertainment. This included not just the movies but also the snacks to go with and maybe even some movie paraphernalia (t-shirts, books, etc.) to go along with it. At the time, considering the large investment in real estate Blockbuster carried, trying to maximize sales in these locations with high mark-up retail items seemed like a solid strategy. A significant advantage that Blockbuster had, and a unique position in the market, was the ability to exclusively offer newly released movies 28 days prior to their competitors.

In relating the retail position Blockbuster chose to emphasize to the 4P framework it is important to note that the main product, entertainment, is not tied to the retail store experience that Blockbuster relied on in its



business plan. This creates an avenue for competitors to enter the same general market, movie rentals, without needing to invest in store locations.

The pricing of Blockbuster's service needed to account for the added business cost of their store locations in order to remain profitable. As their competitors entered the market and grew, by not carrying the cost of large retail networks, they were able to offer products at a lower price thereby enticing customers to defect. Take for example Red Box who was able to place kiosks in high traffic areas with little to no real estate costs with a great advantage of being able to relocate an underperforming kiosk to a new location without the cost of closing and opening a new store.

However, in terms of promotion Blockbuster had significant advantages. As the market incumbent Blockbuster enjoyed significant name recognition and spent heavily on advertising promoting new products such as Total Access. Additionally, Blockbuster had the unique advantage of offering newly released movies 28 days earlier than competitors, a fact that they capitalized on heavily in advertising. Blockbuster guaranteed new release movies would be available in stock when you stopped into the store or else it would be free the next time.

While physical locations were an advantage in offering additional merchandise, they were a drawback in terms of cost structure. Blockbuster leadership was reluctant to abandon the brick and mortar strategy and fully commit to other forms of delivery until it was too late. While they experimented with VOD offerings through a partnership with Enron, their mail delivery and streaming offerings had the potential to reinvent and

invigorate the company but changes in senior leadership led to a shift of financing away from the new ventures and back to the brick and mortar model. Ultimately this shift away from what had the potential to keep Blockbuster in business happened at a juncture that they could not successfully make a correction from in time to prevent bankruptcy.

The environment that Blockbuster was in changed faster than they were willing or able to adapt to. They were heavily invested in physical locations which motivated them to stay the course with offering more retail merchandise along with the rental business. They had a myopic view of the retail store based distribution being their key asset and function. They didn't envision themselves as a broader distributor of entertainment/movie content on a scale independent of the store locations. It wasn't the experience of going into a Blockbuster store that customers valued. It was the convenience of getting a movie they wanted to watch they wanted. When other options either became more convenient or available at a greater perceived value, Blockbuster lost their foothold in the market.

The four main competitors Blockbuster faced (mail delivery, streaming, kiosks and cheap retail DVD sales) offered a competing avenue to obtain the same product (movies at home) at a lower price and, with the exception of kiosk, without the fear of penalty for late video returns. These competitors offered the same product with even greater convenience than Blockbuster and by combining that convenience with lower price and fewer, if any, penalties they were able to erode Blockbuster's market share.

Without much to revamp the Blockbuster image and the reluctance to embrace new technology Blockbuster eventually gained a stodgy image. Netflix was the king of convenience with movies delivered to your door combined with a good on-line interface for choosing your queue and became even more so with the advent and growth of streaming. The Netflix image appealed to younger and more tech-savvy customers that shied away from Blockbuster stores.

With strong competitors gaining success with disruptive models against the market incumbent Blockbuster had a hard time meeting the challenge as they maintained, and even doubled down on, their previous model of pushing for greater retail merchandise in their stores in hopes of attracting more customers and motivating greater purchases from those in the stores. They stuck with what they knew best and tried repackaging the same recipe multiple times believing that their model would persevere in the changing market.

Could Blockbuster have been saved? I believe the answer to that is that it very likely could have been, but it would have looked like a different company and would have required a shift in focus earlier on and continued commitment from senior leadership. Specifically, the shift to an on-line rental model earlier coupled with stopping brick and mortar expansion.

Incorporating the physical locations with their on-line rentals in through the Total Access program gave Blockbuster a unique position in the market that resonated well with customers and was a position other companies could not match. For the customer, the convenience of being able to have a movie delivered to the home coupled with the option of stopping into a location to

exchange it right away instead of waiting a couple days was brilliant. It used what was eventually Blockbuster's main weakness, the retail store locations, and turned it into a strategic advantage. However, at the same time Blockbuster should have explored on-line streaming for digital content as a third line of delivery to the customer. This would add a third prong to the distribution strategy and, while it may eat into sales from its own channels, it keeps the cannibal in the family and prevents defection to other providers based on new technology. Blockbuster should have explored multiple strategies to meet the customer's need, easy access to entertainment at a value price, in a manner that kept the revenue within the company instead of ignoring or abandoning the different options that customers were clearly voting in favor of with their feet.