

# Sony case 1991-2003

Business



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Exploring Corporate Strategy CLASSIC CASE STUDIES Restructuring Sony  
Vivek Gupta and Konakanchi Prashanth The electronics and media giant Sony was struggling through the late 1990s and early part of the 21st century. With each disappointment, it seemed that Sony's management launched another restructuring of the company. By 2003, commentators were beginning to ask whether restructuring was part of the solution or part of the problem. How should Sony be managing its strategic renewal? G G G

As conditions change, Sony has to change accordingly, because their conventional strategy won't transcend to the Internet-enabled model. 1 Mitchell Levy, author of The Value Framework INTRODUCTION For the first quarter ending 30 June 2003, Japan-based Sony Corporation (Sony)<sup>2</sup> stunned the corporate world by reporting a decline in net profit of 98 per cent. Sony reported a net profit of ? 9.

3 million compared to ? 1. 1 billion for the same quarter in 2002. Sony's revenues fell by 6. 9 per cent to ? 1. 6 trillion for the corresponding period.

Analysts were of the opinion that Sony's expenditure on its restructuring initiatives had caused a significant dent in its profitability.

In the financial year 2002-03, Sony had spent a massive ? 100bn on restructuring (? ? 500m; ? a750m). Moreover, the company had already announced in April 2003 about its plans to spend another ? 1 trillion on a major restructuring initiative in the next three years. Analysts criticised Sony's management for spending a huge amount on frequent restructuring of its consumer electronics business, which accounted for nearly two-thirds of Sony's revenues.

In 2003, the sales of the consumer electronics division fell by 6.5 per cent.

Notably, Sony's business operations were restructured five times in the past nine years. Analysts opined that Sony's excessive focus on the maturing consumer electronics business (profit margin below 1 per cent in 2002-03), coupled with increasing competition in the consumer electronics industry was severely affecting its profitability. 1 2 ' Sony Analyzed via the Value Framework', Mitchell Levy, posted on [www.ecmgt.com](http://www.ecmgt.com), October 2002. Sony was established in 1946.

The company invented the video recorder, walkman and mini-disc recorder. It is a leading manufacturer of audio, video, communications and information technology products. Sony has also forayed into diverse fields like music, television, computer entertainment and motion pictures. The company is engaged in five main lines of business – electronics, games, music, pictures and financial services. This case was prepared by Vivek Gupta and Konakanchi Prashanth of the ICFAI Center for Management Research, Hyderabad, India.

It is intended as a basis for class discussion and not as an illustration of either good or bad management practice.

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1 Restructuring Sony Table 1 Sony's financials (1991-2003) Year ended

March 31 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001

2002 2003 \* ? 100 = approx.

A0. 75. Source: Annual Reports 1991–2003, [www.sony.net](http://www.sony.net). Sales & Operating Revenue (? bn)\* 3695.

51 3928. 67 3992. 92 3744. 8 3990. 58 4592. 56 5663.

13 6755. 49 6804. 18 6686. 66 7314. 82 7578. 26 7473.

63 Operating Income/loss (? bn) 302. 18 179. 55 126. 46 106. 96 ? 166. 64 235.

32 370. 33 520. 21 338. 06 223. 20 225. 35 134.

63 185. 44 Net Income/loss (? bn) 116. 92 120. 12 36. 26 15. 30 ? 293.

36 54. 25 139. 46 222. 07 179. 00 121.

83 16. 75 15. 31 115. 52 However, Sony's officials felt that the restructuring measures were delivering the desired results. According to them, the company had shown a significant jump in its profitability in the financial year 2002–03.

Sony reported a net income of ? 115. 52bn in the fiscal 2002–03 compared to ? 15. 31bn in 2001–02. (See Table 1 for Sony's key financials in the past 13 years. ) A statement issued by Sony said, ' The improvement in the results was partly due to the restructuring of its electronics business, especially in the components units.

' 3 At the beginning of the new millennium, Sony faced increased competition from domestic and foreign players (Korean companies like Samsung and LG) in its electronics and entertainment businesses.

The domestic rivals Matsushita and NEC were able to capture a substantial market share in the internet-ready cell phones market. Analysts felt that the US-based software giants like Microsoft and Sun Microsystems and the networking major Cisco Systems posed a serious threat to Sony's home entertainment business. BACKGROUND On 7 May 1946, Masaru Ibuka (Ibuka) and Akio Morita (Morita)<sup>4</sup> co-founded a company called Tokyo Tsushin Kogyo Kabushiki Kaisha (Tokyo Telecommunications Engineering Corporation) with an initial capital of ¥ 190, 000 in the city of Nagoya, Japan.

They gave importance to product innovation and decided to offer innovative, high-quality products to their consumers. The founders introduced many new products like the magnetic tape recorder, the 'pocketable radio', and more. By the 1960s, the company had established itself in Japan and changed its name to Sony Corporation. During the 1960s, the company focused on globalisation and entered the US and European markets.

In the 1970s, Sony also set up manufacturing units in the US and Europe. During this period, Sony developed and introduced the Walkman, which was a huge success.

It significantly boosted Sony's sales during the 1980s. By the mid-1980s, Sony's consumer products were marketed in Europe through subsidiaries in the UK, Germany and France. 3 4 'Financial Results for the Second Quarter, FY 2002', posted on [www.sony.net](http://www.sony.net).

[sony.net](http://www.sony.net), 28 October 2002. Akio Morita was a graduate in physics, while Masaru Ibuka had a degree in electronic engineering. When Morita joined the Japanese navy as a Lieutenant, he met Ibuka at the navy's Wartime

Research Committee. Exploring Corporate Strategy by Johnson, Scholes & Whittington 2 Restructuring Sony

Table 2 Sony's businesses (1994) Business Electronics Product Groups/Companies Video equipment Details Comprises 8mm, VHS, and Beta-format VTRs, laserdisc players, broadcast and industrial use video equipment, Hi-Vision-related equipment, and videotapes. Comprises CD players, Mini Disc system, headphone stereos, personal component stereos, hi-fi components, digital audio tape recorders/players, radio-cassette tape recorders, tape recorders, radios, car stereos, car navigation systems, professional-use audio equipment, audio tapes, and blank MDs.

Comprises colour TVs, Hi-Vision TVs, computer displays, professional-use monitors, satellite broadcast reception systems, projector systems, and large colour video display systems. Comprises semiconductors, electronic components, cathode ray tubes (CRTs), telephone and telecommunications equipment, computers, computer peripherals (including floppy disk systems and CD-ROM systems), home video game systems, batteries, and FA systems. Includes Columbia Records Group; Epic Records Group; TriStar Music Group; Sony Music International; Sony Classical; Sony Classical Film & Video; Sony Wonder; Sony Music Entertainment (Japan) Inc.

Includes the Columbia TriStar Motion Picture Companies; Sony Television Entertainment; Columbia TriStar Home Video; and Sony Pictures Studios and The Culver Studios. Sony Retail Entertainment includes Sony Theatres. Comprises the insurance business of Sony Life Insurance Company Limited and the finance operations of Sony Finance International.

Audio equipment Television Others Entertainment Music Group – Sony Music  
Entertainment Pictures Group – Sony Pictures Entertainment Inc. (SPEI)  
Insurance and Finance Sony Life Insurance and Sony Finance International

Source: Sony Annual Report 1995, [www.sony.net](http://www.sony.net). In 1989, Norio Ohga (Ohga) took over as the chairman and CEO of Sony from Morita. Under Ohga, Sony began to place greater emphasis on process innovations that improved efficiency and controlled product costs.

By 1994, Sony's businesses were organised into three broad divisions – Electronics, Entertainment and Insurance and Finance (see Table 2). Each business division was in turn split into product groups. The electronics business division was split into four product groups, which produced a wide variety of products.

The entertainment division, which consisted of the music group and the pictures group, made music videos and motion pictures. The finance division consisted of Sony's life insurance and finance business. The company's growth was propelled by the launch of innovative products and by its foray into the music and films business.

Restructuring of electronics business (1994) Under Ohga's leadership, Sony witnessed negligible growth in sales during 1990 and 1994. Sales and operating revenues improved by only 2 per cent during that period.

However, the net income and operating income registered a drastic fall of 87 per cent and 67 per cent respectively. Analysts felt that the stagnation in the electronics industry coupled with factors such as the recession in the Japanese economy and the appreciation of the yen against the dollar led to <https://assignbuster.com/sony-case-1991-2003/>

the deterioration in the company's performance. Exploring Corporate Strategy by Johnson, Scholes & Whittington 3 Restructuring Sony Table 3 Sales performance of the electronics business (1991–95) (in ? bn)\* Year/ Business 1991 1992 1993 1994 1995 \* ? 100 = approx. A0.

75. Source: Sony Annual Report 1995, www. ony. net. Video Equipment 928 896 828 669 691 Audio Equipment 882 948 928 841 899 Televisions 552 593 634 618 709 Others 619 793 772 817 909 It was noticed that in the electronics business (see Table 3), the revenues of the video and audio equipment businesses were coming down or were at best stagnant, while the television and ' Others' group were showing signs of improvement.

The ' Others' group, which consisted of technology intensive products such as computer products, video games, semiconductors and telecom equipment, was performing very well and had a growth rate of nearly 40 per cent.

In order to focus on the high growth businesses, Sony announced major changes in the structure of its electronics business in April 1994. Sony's management felt that the ' Group' structure, which had fuelled the company's growth in the 1980s, was proving to be redundant in the dynamic business environment of the 1990s. In the new structure, the product groups of the electronics businesses were regrouped into eight divisional companies. The eight companies were the Consumer Audio & Video Products Company, the Recording Media & Energy Company, the Broadcast Products Company, the



Business & Industrial Systems Company, the InfoCom Products Company, the Mobile Electronics Company, the Components Company, and the Semiconductor Company.

The restructuring exercise laid special focus on the products that formed the 'Others' group. Each divisional company had its own goals and was responsible for all its operations (production, sales and finance). The presidents of the divisional companies were authorised to decide upon the investments to be made up to a prescribed limit. They could also take decisions regarding the HR issues for all employees up to the level of divisional director.

In addition, they were made responsible for the financial performance of the companies headed by them. Sony's presidents were expected to perform a role similar to that of CEOs and were accountable to shareholders.

The restructuring of Sony's electronics business was aimed at improving the company's focus on high potential products and expediting the decision making process to make the company more responsive to changing market conditions. Following the restructuring, the number of layers in the decision-making process was reduced from six to a maximum of four layers.

Commenting on his responsibilities within the new structure, Ohga said, 'First of all, I would like for the divisional presidents to run their companies as if they were reporting to shareholders once a year at a shareholders' meeting. My role will be to review their strategies, examine any points I feel should be questioned and provide advice when and where necessary.'<sup>5</sup> The main goals of Sony's newly formed organisation system were explained in a

memorandum entitled ‘ The Introduction of the Company within a Company System’ (see Table 4).

Explaining the rationale for the new system, Ohga said, ‘ By revitalising its organization, Sony aims to introduce appealing products in the market in a timelier fashion while further strengthening cost-competitiveness companywide.

‘ 6 In 1995, after the implementation of the divisional company structure in the electronics business, changes were announced in Sony’s management structure. Under the new framework, Sony was to be led by a team of executives at the top management level.

The team included the Chairman & CEO, Vice Chairman, President & Chief Operating Officer (COO), Chief Officers and the presidents of divisional companies. Analysts felt that Sony’s management took this measure to reduce the company’s reliance on 5 6 ‘ From a Business Group System to a Divisional Company System’, posted on [www. sony.](http://www.sony.net)

[net](http://www.sony.net). As quoted in the 1995 annual report, posted on [www. sony.](http://www.sony.net)

[net](http://www.sony.net). Exploring Corporate Strategy by Johnson, Scholes & Whittington 4

Restructuring Sony Table 4 Five main goals of the new system

G To further enhance core businesses while developing new ones. G To introduce an organisational structure in which sales and production work closely together and respond quickly to market changes.

G To simplify the structure to clarify responsibilities and transfer authority, thus ensuring quick responses to external changes. G To reduce the levels of

hierarchy in the organisation. G To encourage the entrepreneurial spirit in order to foster a dynamic management base for the 21st century. Source: 'From a Business Group System to a Divisional Company System', posted on [www. ony.net](http://www.ony.net).

net. a single leader. In March 1995, Nobuyuki Idei (Idei) was appointed the President and Chief Operating Officer of Sony. Despite the organisational changes, the financial performance of Sony deteriorated in 1995. For the fiscal year ending March 1995, Sony reported a huge net loss of ¥ 293.

36bn. The write off of goodwill during 1994, the poor performance of the Pictures group and the strength of the yen were regarded as major reasons for this loss. During 1994, the yen was at an all-time high against the dollar, making Sony's exports uncompetitive.

Analysts also felt that Sony's consumer electronics business lacked new, innovative products. Given this poor financial performance, the top management of Sony decided to integrate the company's various domestic and global business functions such as marketing, R, finance, and HR. The functions of its numerous divisional companies were thus brought under the direct purview of headquarters.

Idei also decided to strengthen the existing eight-company structure and to lay more emphasis on R in the IT field. He felt that Sony needed to focus on developing IT-related businesses.

Accordingly, Sony's management reorganised the existing structure to create a new ten-company structure. THE TEN-COMPANY STRUCTURE (1996)

In January 1996, a new ten-company structure was announced, replacing the previous eight-company structure (see Table 5). Under the new structure, the previous Consumer Audio & Video (A&V) company was split into three new companies – the Display Company, the Home AV Company and the Personal AV Company. A new company, the Information Technology Company, was created to focus on Sony's business interests in the PC and IT industry.

The Infocom Products Company and the Mobile Electronics Company were merged to create the Personal & Mobile Communications Company. The other companies formed were the Components & Computer Peripherals Company (formerly called the Components Company), the Recording Media & Energy Company, the Broadcast Products Company, the Image & Sound Communications Company (formerly called the Business & Industrial Systems Company) and the Semiconductor Company. Table 5 Basic features of the ten-company structure G A new company structure to promote quicker, more effective operations that better reflect market changes.

G The establishment of an Executive Board to reinforce headquarters and corporate strategy and management functions. G The appointment of new companies and groups for entering into the IT and telecommunications businesses. G The consolidation of marketing functions.

G The establishment of Corporate Laboratories for new business development. G The training of promising young talent to foster future managers. Source: ' Sony Announces a New Corporate Structure', posted on [www. sony. net](http://www.sony.net), dated 16 January 1996.

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Restructuring Sony In order to devise and implement the corporate strategies of the Sony Group, an Executive Board was created. The board was chaired by Idei. The other members of the board included the Chief Human Resources Officer, the Chief Production Officer, the Chief Marketing Officer, the Chief Communications Officer, the Chief Technology Officer, the Chief Financial Officer, the Executive Deputy President & Representative Director and the Senior Managing Director.

In an attempt to consolidate the marketing operations of Sony, the marketing divisions that belonged to the previous organisational setup were spun off to create three new marketing groups – the Japan Marketing Group (JMG), the International Marketing & Operations Group (IM&O) and the Electronic Components & Devices Marketing Group (ECDMG). The JMG was responsible for all marketing activities in Japan for five companies – the Display Company, the Home AV Company, the Information Technology Company, the Personal AV Company and the Image & Sound Communications Company.

The IM&O was responsible for supporting all overseas marketing efforts for these companies.

The ECDMG oversaw the worldwide marketing operations for the Semiconductor Company and the Components & Computer Peripherals Company. Analysts felt that this consolidation was done to separate Sony's Japanese marketing operations from its worldwide operations so that the company could operate in a focused manner. To centralise all the R efforts of Sony, the previous R structure (in which each company had its own R

division) was revamped and three new corporate laboratories were established.

The laboratories were the Architecture Laboratory (responsible for carrying out R for software, network and IT-related technologies), the Product Development Laboratory (R for product development in AV businesses) and the System & LSI Laboratory (R for LSI and system design, the basic components of hardware products). In addition, a new D21 laboratory was established to conduct long-term R for future oriented technology intensive products.

Sony also gave emphasis to grooming young, talented people to take up top management positions. The company also introduced the concept of 'virtual companies' – temporary groups consisting of people from different divisions for launching hybrid products. Sony applied this idea when developing the latest generation Mini Disk players. For the financial year 1995-96, Sony registered a 15 per cent increase in revenues and became profitable again. In April 1998, a new organisation, Corporate Information Systems Solutions (CISS), was established to realign and upgrade Sony's information network systems and its global supply chain. The CISS comprised an advisory committee of individuals from management consultancy firms and Sony's CISS representatives.

The committee members advised the President on technological and strategic issues related to CISS. Representatives of the CISS were placed in all divisional companies to accelerate the implementation of corporate IT projects. During early 1998, Sony formed Sony Online Entertainment in the

US to focus on internet-related projects. In May 1998, Sony changed the composition of its board of directors and established the new position of Co-Chief Executive Officer (Co-CEO). Idei was appointed Co-CEO.

Idei reshuffled the management system to facilitate speedy decision making, improve efficiency, and provide greater role clarity to managers.

The new system separated individuals responsible for policy-making from those who were responsible for operations. Under the new system, Idei was responsible for planning and designing Sony's strategies and supervising the growth of e-business. Along with Ohga, he had to supervise the performance of the entire Sony group. President Ando was made responsible for overseeing Sony's core electronics business, while Chief Financial Officer (CFO) Tokunaka was made responsible for the company's financial strategies and network businesses.

In addition, the top management positions of Sony's global subsidiaries, which were previously called Corporate Executive Officers, were redesignated Group Executive Officers. Explaining the rationale for these changes, a Sony spokesman said, 'These changes are aimed at making Sony's management more agile'. 7 7 'Sony Names Management Team', by Yoshiko Hara, EE Times, 9 May 2000. Exploring Corporate Strategy by Johnson, Scholes & Whittington 6 Restructuring Sony Table 6 Sales performance of Sony's businesses (1995–99) (in ? bn)\* Year/Business 1995 1996 1997 1998 1999 CAGR (4 years) ? 100 = approx. A0. 75.

Source: Sony Annual Report, 1999, posted on [www.sony.net](http://www.sony.net). Electronics 3027 3283 3930 4377 4355 8. 55% Game 35 201 408 700 760 215% Music

481 506 570 660 719 10. 5% Pictures 282 317 439 643 540 17% Insurance  
113 207 228 291 339 31% Others 52 78 88 84 81 11.

7% The implications From 1995 to 1999, Sony's electronics business (on which the restructuring efforts were focused) grew at a compounded annual growth rate (CAGR) of 8. 55 per cent (see Table 6). The music business had a CAGR of 10. 5 per cent while the pictures business had a CAGR of 17 per cent.

Significant gains were, however, recorded by the games and insurance business.

The games business registered a CAGR of 215 per cent, while the insurance business registered a CAGR of 31 per cent. In the late 1990s, Sony's financial performance deteriorated. For the financial year 1998–99, its net income dropped by 19. 4 per cent. During that period, Sony was banking heavily on its PlayStation computer game machines.

It was estimated that the PlayStation (Games business) accounted for nearly 42 per cent of Sony's operating profits and 15 per cent of total sales for the quarter October–December 1998.

In the late 1990s, many companies across the world were attempting to cash in on the internet boom. At that time, Sony's management felt the need to establish a link between its electronics business (TVs, music systems, computers) and its content-related businesses (music, video games, movies and financial services) by making use of the internet. The management felt that in future, the revenues generated by internet-related businesses might



even surpass those earned through the consumer electronics business. It wanted to use the internet as a medium for selling its electronic products as well as its content (music, movies and so on).

In order to achieve this, Sony announced another reorganisation of business operations. Analysts felt that Sony was in a good position to exploit the opportunities offered by the internet since the company already had an established position in the electronics and content-related businesses. THE UNIFIED-DISPERSED MANAGEMENT MODEL In April 1999, Sony announced changes in its organisational structure. Through the new framework, the company aimed at streamlining its business operations to better exploit the opportunities offered by the internet.

Sony's key business divisions – Consumer Electronics division, Components division, Music division and the Games division – were reorganised into network businesses. This involved the reduction of ten divisional companies into three network companies, Sony Computer Entertainment (SCE) Company and the Broadcasting & Professional Systems (B) Company (see Exhibit 1).

SCE Company was responsible for the PlayStation business while the B Company supplied video and audio equipment for business, broadcast, education, industrial, medical and production related markets.

The restructuring aimed at achieving three objectives – strengthening the electronics business, privatising three Sony subsidiaries, and strengthening the management capabilities. The restructuring also aimed at enhancing shareholder value through 'Value Creation Management'. 8 8 It aimed at

creating value by dividing the group into networked autonomous business units such that the resources within the Sony Group complemented each other. Exploring Corporate Strategy by Johnson, Scholes & Whittington 7 Restructuring Sony Exhibit 1 The unified-dispersed management model

Source: ‘ Sony Announces Organization Structure for New Network Companies’, posted on [www.sony.net](http://www.sony.net).

sony. net, 29 March 1999. Strengthening the electronics business The three network companies created were the Home Network Company, the Personal IT Network Company and the Core Technology & Network Company. Each network company was governed by a network company management committee (NCMC) and a network committee board (NCB). The NCMC was responsible for developing management policies and strategies. Its members included the officers and presidents of the concerned network company.

The NCB was responsible for managing the day-to-day operations of the network company while keeping in mind the overall corporate strategy of the entire organisation. Each NCB was chaired by the concerned company’s President & CEO, Deputy President, President and Representative Director, two Executive Deputy Presidents and Representative Directors, and Corporate Senior Vice President. The new structure aimed at decentralising the worldwide operations of the company. The corporate headquarters gave the network companies the authority to function as autonomous entities in their corresponding businesses.

To facilitate more functional and operational autonomy, the corporate headquarters also transferred the required support functions and R&D labs

to each network company. To give a further boost to Sony's electronics business, the management created Digital Network Solutions (DNS) under the purview of headquarters.

The role of DNS was to create a network business model by charting strategies and developing essential technologies for exploiting the opportunities offered by the internet. The basic aim of creating DNS was to develop a network base that would provide customers with digital content (such as music and movies) and financial services.

**Privatising Sony's subsidiaries** As part of its strategy to promote functional and operational autonomy and to devote more attention to units which contributed significantly to its revenues and profits, Sony decided to convert three of its companies – Sony Music Entertainment (Japan), Sony Chemical Corporation (manufactured printed circuit boards (PCBs), recording media and automotive batteries), and Sony Precision Technology (manufactured semiconductor inspection equipment and precision measuring devices) – into wholly owned subsidiaries. Exploring Corporate Strategy by Johnson, Scholes & Whittington 8 Restructuring Sony owned subsidiaries of Sony.

In addition, Sony converted SCE, which was jointly owned by Sony and Sony Music Entertainment (Japan), into a wholly owned subsidiary of Sony. **Strengthening the management capability** To strengthen the management capability, Sony clearly demarcated the roles of headquarters and the newly created network companies.

Accordingly, distinction was made between the strategic and support functions. Sony's headquarters was split into two separate units – Group

Headquarters and Business Unit Support. The role of Group Headquarters was to oversee group operations and expedite the allocation of resources within the group.

The support functions, such as accounting, human resources and general affairs, were handled by the network companies so that they could enjoy more autonomy in their operations. Significant long-term R projects were directly supervised by the headquarters, while the immediate and short-term R projects were transferred to the concerned network companies. In order to evaluate the performance of the network companies, a value based performance measurement system<sup>9</sup> was introduced.

The implications While pursuing its restructuring efforts, Sony started developing products which were compatible with the internet.

Its electronic products, such as digital cameras, personal computers, music systems, and Walkman, were made web compatible. Through its website, [www. sony. net](http://www.sony.net), consumers could participate in popular television game shows, listen to music, and download songs and movie trailers.

Sony also ventured into e-business with the acquisition of Sky Perfect Communications. <sup>10</sup> While focusing on offering internet-enabled products, Sony also attempted to increase internet penetration by offering internet connection at lower cost and higher speed to consumers in urban areas. Sony's restructuring efforts in 1999 were well received by investors.

Following the announcement of the restructuring programme, Sony's stock prices nearly tripled. This positive trend continued even in 2000.

By March 2000, its stock prices were at a high of \$152. Having already offered its PlayStation game console on the internet, Sony successfully launched its PlayStation 2 (PS2) video game console in Japan in March 2000. The PS2 sold 980, 000 units within the first three days of its launch. However, Sony still faced problems since its other businesses, including electronics, movies, personal computers, and mobile telecommunications, were not performing well.

Analysts felt that the low internet penetration rate in Japan (estimated to be 13 per cent in 1999) was proving to be a major hurdle for Sony.

Consequently, Sony's financial performance deteriorated by the end of 1990s. For fiscal 1999 –2000, Sony's net income fell to ? 121. 83bn compared to ? 179bn in the fiscal 1998–99. This resulted in a major fall in its stock prices. By May 2000, Sony's stock prices fell by 40 per cent to \$89.

Analysts were quick to criticise Sony's efforts towards transforming itself into a web-enabled company.

They commented that the company had created more hype rather than taking a few significant steps in this regard. In response to these financial problems, Sony announced a reshuffle in its top management. Idei became the Chairman and Chief Executive Officer of Sony. Ando, who headed Sony's PC division, was 9 A system that helps in effectively determining the cost of capital. The measurement is based on economic profit, which is calculated by subtracting the cost of debt and equity from the operating profit after tax.

Sony planned to use this system of measurement to set targets and evaluate business unit performance.

<https://assignbuster.com/sony-case-1991-2003/>

The performance was to be linked, in future, with management compensation. 10 A popular satellite broadcasting company in Japan which owned Sky Perfect TV and had successfully ventured into the internet service provider (ISP) business by launching the website, www. so-net. This website enabled online shopping, interactive games, fortune telling as well as stockbroking. Exploring Corporate Strategy by Johnson, Scholes & Whittington 9 Restructuring Sony made the President, while Tokunaka, who previously headed the PlayStation unit, was made the Chief Financial Officer of Sony.

Sony also undertook a massive cost-cutting exercise. Its global manufacturing facilities were reduced from 70 in 1999 to 65 in 2001. Sony planned to further bring down the number of manufacturing facilities to 55 by the end of 2003. This move would result in the elimination of 17, 000 jobs. While implementing these measures, the company had to deal with severe resistance from employee unions and local governments (in areas where jobs would be eliminated). Despite the above measures, Sony's financial condition did not show any significant improvement in 2001.

The company was severely affected by the slowdown in the IT industry during 2000-01, which led to a decline in the demand for its computer-related products. As a result, in spite of a 9. 4 per cent increase in revenue in the fiscal 2000-01 (mainly due to the improved sales of the PlayStation games console) Sony's net income dropped significantly from ? 121. 83bn in the fiscal 1999-2000 to ? 16. 75bn in the fiscal 2000-01. Analysts commented that Sony required a new business model.

The company had immediately to take concrete measures to increase its net income.

Sony's management also felt that with the emergence of net-compatible devices like cellular phones, audio and video gadgets and laptops, PCs were losing their charm. It felt that in the emerging age of 'broadband'<sup>11</sup> the demand for the above products was likely to increase in future. Sony's management felt that in order to boost profitability and exploit the opportunities offered by the broadband era, there was a need for yet another organisational restructuring. **RESTRUCTURING EFFORTS IN 2001** Sony announced another round of organisational restructuring in March 2001.

The company aimed at transforming itself into a Personal Broadband Network Solutions company by launching a wide range of broadband products and services for its customers across the world.

Explaining the objective of the restructuring, Idei said, 'By capitalising on this business structure and by having businesses cooperate with each other, we aim to become the leading media and technology company in the broadband era.'<sup>12</sup> The restructuring involved designing a new headquarters to function as a hub for Sony's strategy, strengthening the electronics business, and facilitating network-based content distribution.

New headquarters to function as a hub for Sony's strategy Under the new structural framework (see Exhibit 2), Sony's headquarters was revamped into a Global Hub centred on five key businesses – electronics, entertainment, games, financial services and internet/ communication service. The primary role of the Global Hub (headed by the top management)

was to devise the overall management strategy of the company. Sony's management decided to integrate all the electronics business related activities under the newly created Electronic Headquarters (Electronics HQ).

In order to achieve the convergence of Audio Video Products with IT (AV/IT convergence), Sony devised a unique strategy called '4 Network Gateway'.

Under this strategy, the games and internet/communication service businesses were combined with the electronics hardware business so that innovative products could be developed and offered for the broadband market. The three businesses were under the supervision of Ando. In order to provide support services for the entire group, a management platform was created, which consisted of key support functions in diverse fields such as accounting, finance, legal, intellectual 11

An acronym for broad bandwidth, it is a high-speed, high-capacity data transmission channel that sends and receives information on coaxial cable or fibre-optic cable (which has a wider bandwidth than conventional telephone lines). This channel can carry video, voice and data simultaneously. 12 As quoted in the Annual Report 2002, [www. sony.](http://www.sony.net)

net. Exploring Corporate Strategy by Johnson, Scholes & Whittington 10

Restructuring Sony Exhibit 2 Sony organisational chart: electronics-related business (as of 1 April 2001)

Source: 'A New Group Structure for the Next Stage of Integrated, Decentralized Management', [www. sony. net](http://www.sony.net), 29 March 2001. copyrights, human resources, information systems, public relations, external affairs and design. The management platform was later split into the Engineering, <https://assignbuster.com/sony-case-1991-2003/>



Management and Customer Service (EMCS) Company and the Sales Platform (which comprised the regional sales companies and region-based internet direct marketing functions).

The management platform was headed by the Chief Administrative Officer, a newly created position.

Sony's management also converted the product-centric network companies into solution-oriented companies by regrouping them into seven companies. Group resources were allocated among the network companies on the basis of their growth potential. Exploring Corporate Strategy by Johnson, Scholes & Whittington 11 Restructuring Sony Strengthening electronics business To enhance the profitability of the electronics segment, Sony's management decided to give emphasis to product development efforts. The management felt it was also essential to enhance the quality of the electronic devices manufactured.

In order to achieve this, Sony's management devised an innovative business model called the Ubiquitous Value Network, 13 which connected the company's existing hardware, content and services through an agency of networks. Sony planned to develop a wide range of products which could be connected through this network. Network-based content distribution Like the electronics, games and internet/communication service businesses, the entertainment and financial services businesses were also developed in a network compatible manner to facilitate electronic content distribution.

In the entertainment business, music and movies were converted into a digital format and distributed over the internet (apart from being distributed

through traditional channels such as music stores and theatres). In Japan, Sony Music Entertainment launched online music through its website. This website allowed customers to download popular songs for a fee.

In the financial services business, Sony Life Insurance Japan launched the ‘Life Planner’ consultancy system which offered personalised financial services online to its customers.

Sony Life Assurance Japan also went online and started selling its insurance policies over the internet. The implications Soon after the reorganisation, Sony launched some innovative products to cater to the broadband market. For instance, in 2001, the company launched a series of internet-compatible mobile phones. However, the product was unsuccessful (owing to problems in the software used in the mobile devices) and in early 2002 Sony had to recall three batches of phones sold to Japanese companies. In consequence, Sony had to write off \$110m in the quarter ending June 2002.

In April 2003, Sony announced another major restructuring exercise (to be carried out in the next three years) in order to strengthen its corporate value (see Exhibit 3). Following this announcement, Sony was reorganised into seven business entities – four network companies and three business groups (see Exhibit 4). These business entities were given the authority to frame short-term and long-term strategies. According to analysts, the company’s financial performance did not improve in spite of the frequent restructuring by Sony’s management.

For the financial year 2001-02, Sony’s operating income fell by a significant 40.3 per cent while its revenues registered a marginal increase of 3.

6 per cent. According to a BusinessWeek report, sales of Sony's most profitable products – the PlayStation and the PS2 game consoles – were likely to fall (see Exhibit 5). Due to Sony's poor financial performance, the management planned to further reduce the number of manufacturing facilities and shift some production activities out of Japan.

Analysts also criticised Sony for being a diversified business conglomerate engaged in several businesses from semiconductors to financial services. They felt that the company should focus on a few highly profitable businesses like games, insurance, and audio-video equipment and hive off the unprofitable businesses.

Analysts felt that spending huge amounts of money on restructuring was not justified, particularly since the restructuring exercises had not yielded the expected results. In 2001, restructuring efforts had cost the company ? 100bn; and the proposed restructuring in April 2003 was expected to cost another ? 40bn. 13 The Ubiquitous Value Network is an environment in which PC and non-PC consumer electronics devices are seamlessly connected to each other and to the network, giving users access to all types of content or service, from anywhere across the globe. Exploring Corporate Strategy by Johnson, Scholes & Whittington 12 Restructuring Sony Exhibit 3 Sony organisational chart (as of 1 April 2003) Source: ' Sony Announces Executive Appointments and Organizational Reforms Effective as of April 1, 2003', www. sony. net, 31 March 2003.

Exhibit 4 Responsibilities of network companies and business groups No. 2 3  
Network company/ business group Home Network Company Broadband

Network Company IT and Mobile Solutions Network Company 4 5 6 Micro Systems Network Company Game Business Group Entertainment Business Group Responsibility To create a new home environment with networked electronic devices centred on next-generation TV Development of next-generation electronics devices and linkages to Game devices To realise a connected world with PC and mobile devices and strengthen the B2B solutions business To enhance key devices and modules as core components of attractive set products To promote Game businesses for the broadband era To develop entertainment content businesses based on pictures and music and develop a new content business model for the network era To integrate various business units providing services based on direct contact with customers (finance, retail, etc). Strengthen synergies and develop attractive new business models for customers through the application of IT. 7 Personal Solutions Business Group Source: ‘ Sony Announces Executive Appointments and Organizational Reforms Effective as of April 1, 2003’, [www.sony.com](http://www.sony.com).

et, 31 March 2003. Analysts also felt that the convergence of consumer electronics, PCs and the internet was not only opening up new opportunities for Sony but also creating more competition for its core businesses. As Sony took steps to strengthen its networking capabilities, the company faced new forms of competition in both domestic as well as foreign markets. For instance, in the US, software giants like Microsoft and Sun Microsystems (as well as a few startups) were planning to enter the home entertainment market. Exploring Corporate Strategy by Johnson, Scholes & Whittington 13 Restructuring Sony Exhibit 5 Break-up of Sony’s businesses (31 March 2002)

Business Electronics Games Insurance Films Music Others Sales (\$bn) 35. 6  
7.

4 3. 7 4. 6 4. 5 0. 6 Operating profits (\$m) 125 578 91 147 203 NA Source: ‘  
Can Sony Retain the Magic’, by Irene M.

Kunii & Cliff Edward, BusinessWeek, 11 March 2002. Even Cisco Systems, which provided network solutions, had started manufacturing consumer electronics products. A BusinessWeek report said that Sony lacked any distinctive competencies in the internet-related businesses. It was neither an aggregator of content like Yahoo! , nor a limited-product vendor with an efficient distribution network such as Dell.

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