The video game industry and nintendo

The video game industry has been subject to 5 primary driving forces that have been responsible for its evolution. These are;

Technological change; technology has been constantly changing producing successive generations of powerful hardware and software. The change has also been characterized by reduced per unit cost thereby ensuring affordability.

Product innovation; larger number of developers often using distributed systems have ensured continuous and quality production of innovative applications. Analysts reckon that the games industry is the major driving force behind advances in commercial computer applications. The positive externalities resulting from the industry’s struggle to meet the expectations of an unforgiving customer base has led to its exceeding the demands for business productivity and other applications.

Promise of growth; though cyclical, the industry has been characterized by high long term growth prospects. The gaming industry has also had its application in areas hitherto thought of as purely scientific like game simulations, advertising, architecture, augmenting classroom instruction

Changes in the personal computer industry; the lower cost ad high performance of personal computers threatens the continued expansion of the industry. Home computers and laptops are increasingly replacing consoles.

Changes in consumer taste; the video games industry mainly targets the adolescent male youth as its consumer. However, recent trends show that the young adults have and women have taken to the video market (Ireland, 2006).

Key success factors for the industry

Quickly adopting new technologies; the video gaming industry is characterized by high speed innovation and delivering the innovation to the market. Developers are always ahead of the market and innovation lead time could mean success or failure.

Aggressive marketing / franchising; to ward off competition, the video game makers use extensive advertising to create knowledge of their new products.

Downstream ownership links;

Establishment of brand names

Economies of scale

Development of new products

Nintendo’s strategy

The company’s strategy has been that of focused differentiation. In the short term, the company has been pricing its products lowly and providing its console as a loss leader to its customers. Over time the company has learnt that it shouldn’t follow competitors but should rather create its own path . While the competitors were busy making new generation consoles to appeal to customers, the company was innovating products for an entirely new market. According to the CEO, Satoru Iwata, “ it is best to Zig when others Zag”. It also refined the value proposition of DS, best serving the underserved market. The combination of the right product, interface and market gave it phenomenal success. Nintendo has also successfully segmented its product to give close attention to the targeted segments. In the long term the company intends to create new franchises and diversify revenue sources as well as put more emphasis on the Chinese and Indian market.

So far, the company has been able to expand the demographic base of its market. Through partnering with other developers, it has been able to improve features while focusing on family friendly entertainment. It has also succeeded in redefining gaming as a pass time through its emphasis on simplicity and ease of use.

Nintendo can be said to be following a blue ocean strategy. a blue ocean strategy is based on the aspect of looking across the boundaries of competition (the so called Six Paths Framework) to reduce the company's planning risk by visualizing strategy, creating new demand by unlocking the three tiers of noncustomers and launch a commercially-viable blue ocean idea by aligning unprecedented utility of an offering with strategic pricing and target costing and by overcoming adoption hurdles. The adoption hurdles have typically been associated with the console-as the game can only be delivered via consoles which have to be manufactured and sold as loss leaders. The company has also engaged in Value Innovation by simultaneously pursuing low cost and differentiation as the basis for its competition. It has reconstructed the boundaries of the market by looking at the big picture, going beyond the current customer taste and preferences while making sure they get the strategic sequence right. It is an ideal example of a firm breaking out of old school competitive strategic thinking(called structuralist) and to nurture demand and squeeze profits for the company in particular and the industry In general through the use of reconstructionist (blue ocean) strategic thinking. Most importantly, Nintendo has overcome the four key hurdles that choke this out-of the box thinking. These hurdles include the motivational, resource, cognitive and political barriers that have successfully limited strategists in organizations from seeing the urge to break from status quo(cognitive), find resources to lay out the new strategic shift(resources), keeping employees committed to the new strategic shift(motivation) and overcoming the vested interests blocking the shift (political).

Selected financial measures and accompanying ratios

Ratios

2005

2006

2007

2008

current assets

1018731

993892

966534

1646834

current liabilities

205450

182275

468, 435

567222

long term liabilities

5353

4161

0

5293

owners equity

921467

974091

1, 101, 878

1229974

total assets

1132492

1, 160, 699

1, 575, 590

1, 802, 483

total liabilities

211025

186, 609

473, 714

572, 611

net sales

514988

509, 249

966534

1672423

gross margin

217376

215023

397812

700600

opertg. income

113458

91223

226024

487220

net income

87416

98378

174294

257342

Inventory

49759

30836

88, 609

104, 840

R&D exp

20513

30588

37706

37000

2005

2006

2007

2008

Revenue growth

1. 13%

-47. 31%

-42. 21%

Operating profit margin,

22. 03%

17. 91%

23. 39%

29. 13%

Gross profit margin

42. 21%

42. 22%

41. 16%

41. 89%

R&D as % of sales,

3. 98%

6. 01%

3. 90%

2. 21%

Return on Assets

7. 72%

8. 48%

11. 06%

14. 28%

Return on Equity,

9. 49%

10. 10%

15. 82%

20. 92%

Current Ratio

4. 96

5. 45

2. 06

2. 90

Inventory Turns,

10. 35

16. 51

10. 91

15. 95

Debt to Equity

22. 90%

19. 16%

42. 99%

46. 55%

From the above, it is evident that the company’s sales have been declining. However, this had nothing to do with strategy but rather was as a result of the global economic meltdown witnessed in the run up to the year 2008. It remains one of the most highly ranked companies in terms of gross margin. This is because after development, its products have low cost of manufacture and distribution. Its research and development remains low as compared to its rivals and that could also account for its falling sales. It has also utilized its assets well for the three years, raising its Return on assets ratio two fold over the four years under review. This is also the case for the return on equity that has increased by 100%. It remains one of the most liquid companies in the industry as per its current ratio well able to meet its maturing obligations. The firms gearing is balanced, topping at 47% making it enjoy the moderating effect on debt on the cost of its capital.

SWOT Analysis

Strengths

Leader in hand held gaming market

High brand reputation

Innovative

Weaknesses

Falling profits

Very high research and development costs

Weak online presence

Opportunities

Gaming is globalizing creating a mass market

Emergence of casual/ aging and female market untargeted by competition

Expanding demographics 5-95 year olds

Threats

High switching costs

Very short product life cycles

Emergence of laptops and powerful PCs

Rapidly changing industry

From the above, Nintendo's point of leverage continues to be its emphasis on innovative products which are easy to use and targeting them to the mass market. Also given the short product life cycles and long development lead times its vulnerability, the company should position its products to appeal to the mass market yet remain different from its rivals making it hard for them to copy (Porter, 1980).

Michael Porter (1985) pointed out that a firm derives competitive advantage from its ability to create value for its buyers that exceeds the cost of creating it. Value refers to what the buyers are ready to pay for while superior value comes from pricing at lower rates than the competitors for equal benefits or offering unique benefits that offset a higher price (Porter, 1985). The two types of competitive advantage differentiation and cost leadership have been put to use by Nintendo to create and sustain competitive advantage.

Kim & Mauborgne (2005) added that companies can tilt competition odds to their favor by changing:

Players – suppliers, customers etc and not just competitors

Added values – the value proposition that each player introduces to the game

The rules that give a game its form and structure

The tactics and

Scope – boundaries of the game.

Nintendo has done so by changing the players (targeting different customers), adding value (offering consoles at cheap rates) and redefining the boundaries of the competition.