



Sony

Playing a long game

LONDON, TOKYO AND NEW YORK

Can the PlayStation 3 revive the ailing electronics giant?

THINGS have not been going well for Sony lately. Last month senior executives at the Japanese electronics giant issued an unprecedented apology after discovering that 9.6m laptop batteries, supplied to other computer-makers, were faulty and would have to be recalled at a cost of \$436m. Sony's Blu-ray high-definition technology, launched this summer, has suffered from delays and component shortages, and is embroiled in a standards war with the rival HD-DVD format. American regulators began investigating the company last month as part of an inquiry into allegations of price-fixing in the memory-chip market. And having long been the world's most valuable electronics firm by stockmarket value, Sony's market capitalisation has fallen to less than half that of Samsung, its South Korean rival. "They really need some good news," says Paul Jackson of Forrester, a consultancy.

So a lot is riding on the PlayStation 3 (PS3), the latest incarnation of Sony's industry-leading games console, which was launched with much fanfare in Japan on November 17th. In Akihabara, Tokyo's neon-lit electronics district, stores drafted in extra workers to cope with easily the biggest product launch of the year. At the Yurakucho flagship store of Bic Camera, one of Japan's largest electronics retailers, hundreds of gamers queued through a

cold, damp night. Ken Kutaragi, who runs Sony's gaming division, was there to welcome them in the morning.

At Yodobashi Camera in the southern city of Fukuoka, half of the 400 people queuing were Chinese immigrants with orders to snap up the store's assignment for resale online in China. Across Japan, the PS3 had sold out by lunchtime. Similar scenes were expected at its American launch on November 17th. On Tuesday there were already over 100 people camping outside Sony's New York store.

Not so fast

Sony needs the PS3 to succeed for three reasons: to maintain its lucrative dominance of the games industry; to seed the market for Blu-ray and establish Sony in the emerging market for internet video downloads; and to demonstrate that the turnaround being led by Howard Stringer, who took over as chief executive in 2005, is working and that Sony's gaming, electronics and content divisions really can work together. Despite the enthusiasm of the PS3's early buyers, success in each of these areas is far from assured.

In gaming, Sony faces far stronger competition than it did when it launched the PlayStation 2 in 2000. The PS2 went on to sell over 100m units, giving Sony 70% of the market. But gaming is a cyclical busi-

ness, and success in one round does not guarantee success in the next. Microsoft has already sold over 6m of its Xbox 360 consoles, launched a year ago, and expects to have sold 10m by the end of 2006. Nintendo, Sony's other rival, will launch its new console, the Wii, on November 19th, and expects to sell 4m units by the end of the year. Manufacturing problems delayed the PS3's launch from May and meant that only 93,000 consoles were available for the Japanese launch. Sony hopes to sell 2m by the end of the year, but even if it does so, it will start the race in third place.

Availability is one weakness; pricing is another. The PS3 is available in two configurations, costing \$500 and \$600 in America, and ¥50,000 (\$425) and ¥60,000 (\$510) in Japan. That is far more than rival consoles (the Xbox 360 starts at \$300 and the Wii costs \$250) and is due to the inclusion of a Blu-ray optical drive in every PS3.

Sony will lose money on each PS3 sold for the first couple of years until higher volumes and design improvements reduce costs. But it will make money by taking a cut of every game sold. Worryingly, however, less than one game was sold per PS3 in Japan this week, which suggests that some buyers regard the PS3 as a subsidised Blu-ray player—which it is. Dedicated Blu-ray players start at around \$750. The PS3, in short, will not be the moneyspinner that the PS2 was for quite some time, and it seems unlikely to achieve the market share of its predecessors (see chart on next page).

The PS3 is also meant to ensure that Blu-ray triumphs over HD-DVD as the high-definition successor to the DVD video format. The idea is that millions of PS3s bought by gamers will seed the market for Blu-ray, providing it with critical mass and ensuring that Hollywood studios, which

are reluctant to back two rival standards, plump for Blu-ray over HD-DVD. But instead of riding the PS3 as a Trojan horse, Blu-ray has instead hobbled it by increasing its price and delaying its introduction. The battle between Blu-ray and HD-DVD may even prove irrelevant, as internet downloads become the medium of choice for high-definition video. Both Sony and Microsoft plan to sell high-definition video downloads via their consoles.

Finally, the PS3 is a litmus test for Sir Howard's turnaround effort, one of the aims of which is to get Sony's various divisions to co-operate more fully. (A spat between its electronics and content units left the field open for Apple's iPod.) The company insists that despite recent problems such as the battery recall, the turnaround is going well behind the scenes. Sony has improved margins in its electronics business and reduced headcount by 10,000 ahead of schedule. It is also on track with factory closures, asset disposals and winnowing its product line-up to focus on "champions" such as Cyber-shot digital cameras, Bravia televisions and, of course, the PS3. Sir Howard even suggested this week that the battery fiasco had helped by making it easier for him to convince doubters within Sony of the need to change.

Yet it will be some time before it is possible to tell whether the PS3 can rescue Sony. Beneath the short-term troubles, the company is playing a long game. "This is not a battle that's just about this Christmas," says Rob Wiesenthal, the finance chief of Sony's American division. Sony is betting that the PS3's advanced technology will sustain the company for a decade by extending the PlayStation franchise beyond gaming. So a few teething problems in the early days are nothing to worry about; besides, the PS2 was also criticised for being expensive, over-engineered and unreliable when it first appeared. But having achieved 70% market share last time around, Sony is certain to lose ground this time. The only question is how much. •

