



Nintendo Switch: Shifting from Market-Competing to Market-Creating Strategy

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Introduction

“... Fighting with brute force is not our way of doing business. Yet again, it is our intention to go into a new blue ocean...”

Satoru Iwata, Former CEO, Nintendo, 2014¹

In 2016, after abysmal sales of the Wii U gaming console, critics argued that Kyoto-based Nintendo should exit the hardware market and cease making videogame consoles – as critics had also argued before the introduction of the bestselling Nintendo Wii. Apple and Samsung owned the mobile space, while Sony and Microsoft dominated high-powered videogame consoles; Nintendo couldn't possibly compete, they said.

Readying for the release of its newest console, codenamed the NX, Nintendo faced troubling times. Sales had fallen so far that executives at director-level and above had slashed their pay. As if morale wasn't already low enough, CEO Satoru Iwata, who had overseen the release of the Nintendo DS and Wii, died of cancer at an early age.

Nintendo used a blue ocean approach when developing the bestselling DS and Wii. Faced with the rise of massively disruptive smartphones and tablets, the firm pivoted to competition with the Wii U console and technology innovation with the 3D DS. Would their upcoming new console, the Nintendo Switch, be another blue ocean success or red ocean flop?

History

Playing cards and card games were introduced to Japan in 1549 by missionary Francis Xavier who failed to spread religion but succeeded in spreading card games and gambling. Fed up with both, Japan closed contact with the west and banned playing cards in 1633. Local artisans created alternative card styles but they were deemed to encourage gambling, and therefore outlawed.

It was in November 1889 that Japanese entrepreneur Fusajiro Yamauchi introduced a new type of card game, *Hanafuda* or flower card game, in a store named Nintendo Koppai. The cards were different enough from gambling cards that the government legalized them and Yamauchi's Nintendo thrived, opening stores in other cities and growing to be the dominant game maker in Japan.² Nintendo grew though remained solely in the playing card space, creating minor variations of cards for decades.

1 Whitehead, Thomas. "Satoru Iwata Announces a "Quality of Life" Platform Business of "Non-Wearable" Technology." Nintendo Life. January 30, 2014. Accessed February 18, 2019. http://www.nintendolife.com/news/2014/01/satoru_iwata_announces_a_quality_of_life_platform_business_of_non_wearable_technology

2 Reports suggest the Japanese underground, the *Yakuza*, did eventually create gambling games with the cards but this was a clear misuse. Where other cards were designed for gambling, flower cards were not.



After a 1959 licensing agreement to produce cards with Disney characters proved wildly popular, Nintendo went public, listing on the Osaka stock exchange in 1962. However, the firm initially struggled as a public company until they found a niche developing then novel electronic toys, a high-margin category. Building on the success of the Nintendo Beam Gun, a toy that shot light, the firm partnered with the first video game console, the Magnavox Odyssey, to create a light gun in 1972. The gun would “shoot” on the screen.³

Nintendo decided their first homemade game would feature a hero, villain, and damsel in distress. The villain would be a large ape named Donkey Kong. The damsel was given the name Pauline. But the hero, their protagonist, proved to be a more difficult creative challenge.

New to creating IP, the team sat in their then newly leased but almost empty US office space thinking about a name and characterization for a videogame character who never gives up, persisting screen after screen against all odds. While brainstorming, their landlord, Mario Segale, arrived and aggressively inquired about the late rent in front of his team, refusing to let the matter rest. Nintendo had their character, Super Mario, the guy who never gives up.

Mario went on to become arguably the best-known videogame character in the world. “Mario himself became not only the face of Nintendo, but also the face of the video game industry as a whole,” writes the National Museum of Play.

Nintendo’s first console, introduced in 1983, was called the Family Computer Home Video Game Console (Famicom), or Nintendo Entertainment System (NES) outside Japan.⁴ The initial plan was to license characters for videogames from others, like they’d licensed Disney characters for their playing cards, but they quickly realized their budget was inadequate. Instead, the firm was forced to create its own characters.

The NES was a blockbuster, combining imagination and innovation with high-quality games and rescuing the entire video game industry, that struggled after the downfall of then dominant market incumbent Atari.⁵ Worldwide, the system would go on to dominate home videogame systems, selling just under 62 million units.⁶

Nintendo moved on, innovating an experimental system featuring a low computing power handheld long-lasting battery-operated black-and-white gaming system, the *Game-Boy*, released in 1989 and priced at just \$90.⁷ The Game-Boy sold 188 million units; thirty years later it remains the bestselling videogame system in history.

Next came the *Super Nintendo Entertainment System* (SNES), released in Japan Nov. 21, 1990.⁸

The SNES went on to sell 49 million units worldwide. The early game console market had many

3 Hongo, Jun. "Nintendo Brought Arcade Games into Homes 30 Years Ago." The Japan Times. Accessed February 18, 2019. <https://www.japantimes.co.jp/news/2013/07/15/reference/nintendo-brought-arcade-games-into-homes-30-years-ago/>

4 The system morphed in name and purpose during the early years. It was the Family Computer Home Video Game Console, then the Family Computer (for a time it was marketed as a general-purpose computer), then the shortened name Famicom then, finally, evolved into the Nintendo Entertainment System or NES.

5 The NES was initially named the Family Computer, or Famicom, but was renamed retroactively for the US release. The NES was released in North America Oct. 18, 1985, in Europe Sept. 1, 1986, in Australia 1987, and in Brazil in 1993.

6 Nintendo released a miniaturized version of the NES, that looks like the original but fits into the palm of a hand, worldwide in 2017. Whereas games for the early system required cartridges, the new one has 30 top selling games from the era already installed. Originally released as a novelty device, Nintendo had to increase production when the \$60 toy was reselling for as much as \$1,800 during the 2017 holiday season.

7 The Game-Boy came from an internal competition at Nintendo to develop a portable system. The Game-Boy team decided to purposefully use older technology to achieve a low price point and long battery life.

8 North America followed Aug. 23, 1991, and the rest of the world in 1992-1993.



competitors, the most noteworthy being *Sega*, but Nintendo did well with a combination of reasonably-priced hardware and imaginative software.

In 1993, then CEO Yamauchi financially rescued independent game studio *HAL Laboratory*, which created Nintendo games, on the condition they appoint game developer Satoru Iwata as CEO. Yamauchi believed that Iwata would be better able to manage the creative yet commercially challenged game studio. Iwata went on to create *Pokémon* and *Super Smash Bros.*, two mega-hits that ran exclusively on Nintendo game systems.

Nintendo Struggles with Competition

During the prior era, Nintendo had competition but, by combining high-quality games (software) with their gaming systems (hardware), dominated or came in a close second. But that changed on December 3, 1994, when Sony released the \$300 *PlayStation* console. Packed with high-powered chips for realistic graphics and sound, gamers loved the device. The PlayStation was wildly popular, selling over 102 million units during its lifespan.

Nintendo responded by offering the \$200 *Nintendo 64*, featuring a 64-bit microprocessor.⁹ Yet despite its lower price, a brand name that resonated with gamers, and marketing materials that touted its processing power, only 33 million units were sold worldwide.

In November 2001, Microsoft entered the market with the *Xbox*, a high-powered computing game console that sold 10 million units.¹⁰ In March 2002, Sony followed up with *PlayStation 2*, which featured even more powerful graphics, high-quality sound, and a built-in DVD player (then a new and expensive gadget). A decade later (December 2012), Sony had sold 155 million PlayStation 2 systems.

Nintendo countered with the *GameCube*, which became an unmitigated flop, with worldwide sales reaching a paltry 13 million, not significantly more than Microsoft's product that had few games and no characters to offer, in contrast to Nintendo's vast library.¹¹

In 2000, at Yamauchi's request, Iwata joined Nintendo in the corporate planning division, taking over as CEO in 2002. Iwata believed game consoles had evolved to focus too much on technology demanded by die-hard gamers, who demanded complex and oftentimes violent games to run at high speed with realistic graphics and high-definition sound. Young men were especially attracted to violent, adrenaline-fueled, sport-simulation gaming experiences that demanded lightning-fast reflexes. Besides increasing the price of the computer hardware, game makers also had to create high-resolution graphics and sound, encapsulating it all within software to make gameplay realistic, wrapped around a cohesive story. Games were becoming prohibitively expensive to

9 Nintendo advertisements from this era did not explain how the 64-bit chip improved the user experience. Bullets on the box read focused on technology: * 64 bits of pure power * Realistic 3D graphics * Revolutionary controller with joystick * It's an unbelievable gaming experience!

10 Microsoft was initially unenthusiastic about entering the videogame market but saw the consoles as a "trojan horse" to take over the living room, dominating television, music, and video. They believed there was no alternative except to offer their own console.

11 Microsoft chose to partner with, fund, or outright purchase game studios to build a game library for the XBox.

produce, increasing the price that the cost game studios charged which further reduced their mass appeal.¹²

Iwata personally loved games but not necessarily the new offerings. He realized there were many more people like him, alienated by violent, difficult-to-learn games: “On my business card, I am a corporate president. In my mind, I am a game developer. But in my heart, I am a gamer.” said Iwata.

Towards a Blue Ocean

Nintendo DS

“I vaguely remember some time in ... second or third grade when I decided I wanted a Nintendo DS. So I saved my money ... and one day I sat down with my mom and picked out a very specific DS colour. I picked this pink because I was trying to remember what colour my friend had... But I needed a game with my pink DS... So somehow, it came down to Nintendogs. I mean—I knew nothing about video games. I wanted some because my two best friends had DS’s.”

Emily Rae (edited for clarity)¹³

Iwata’s first offering was an entirely reworked portable game system to replace the aging Game Boy. With a tiny screen that supported only low-resolution graphics and sound, the *Nintendo DS* was decidedly not for core gamers, with their demanding standards for technical features. It was aimed towards the vast majority of people who cared passionately about fun and variety of games, not the technical features. Because the screen was small and there was no support for high-resolution sound, DS games cost far less to develop than console games.¹⁴ Low development costs encouraged experimentation and innovation, pushing studios to think more about fun than technological sophistication, and creating a wide variety of interesting and low-cost games that increased the appeal of the console.¹⁵

Recognizing that game systems were purchased and played primarily by boys (note the name of the prior system, Game Boy), Nintendo opted to release the system in both blue and pink plastic, doubling the size of their customer base by signalling to former noncustomer girls that they too would enjoy videogames. Released on November 21, 2004, the DS was a smash hit. Nintendo sold 154 million units.

“Inside Nintendo, we call our strategy ‘Blue Ocean.’ This is in contrast to a ‘Red Ocean.’ Seeing a Blue Ocean is the notion of creating a market where there initially was none -- going out where nobody has yet gone. Red Ocean is what our competitors do – heated competition where sales

12 The number of bytes (amount of memory) in a game correlates to production cost of the game and both cost and game size must be plotted on a logarithmic scale (a y-axis that increases by 10x each increment) to visualize the data correctly. These ever-larger file sizes, with ever-larger costs, are due to high-resolution graphics and sound that are expensive to produce. <https://venturebeat.com/2018/01/23/the-cost-of-games/>

13 <https://www.quora.com/What-was-your-very-first-video-game>. Answer by Emily Rae, Jul. 1, 2017.

14 Nintendo DS games typically cost hundreds of thousands of dollars to create whereas PS3 and Xbox 360 games more often have budgets in the \$20-30 million and blockbuster games have development budgets in excess of \$100 million. http://vgsales.wikia.com/wiki/Video_game_costs

15 Like all game system developers, Nintendo charges a licensing fee to publish a game on their systems, earning revenue from each game sold. The exact amount is secret it is assumed to be about 33% of the retail price. Licensing fees are the reason some game consoles are sold at or below cost.



are finite and the product is fairly predictable. We're making games that are expanding our base of consumers in Japan and America. Yes, those who've always played games are still playing, but we've got people who've never played to start loving it with titles like Nintendogs, Animal Crossing and Brain Games. These games are Blue Ocean in action," said former Nintendo Vice President of Marketing and Corporate Affairs Perrin Kaplan.¹⁶

Nintendo Wii: Casual Games

"Many people in this industry tend to categorize our customers into two groups — one is the core gamer and the other is casual gamers...We want to create a kind of cycle where casual gamers are gradually growing up to become passionate players. In order to maintain that kind of cycle, we needed to break down the wall."

Satoru Iwata, CEO¹⁷

Seeing the success of the DS – the appeal to people who had not bought video game systems before – Iwata, a lifelong video game fanatic, tasked his team to study what makes for a good game. Whereas Sony and Microsoft, with their expensive consoles, were running focus groups on gamers, Nintendo studied non-gamers. Most famously, Nintendo went to retirement homes to watch how people spent their time. Their primary motive was not to sell videogame consoles to nursing homes (although they did eventually accomplish this) but rather to watch how the residents played games. They observed elderly retirees playing card games that had simple rules that could become mind-numbingly complex depending on the skill of the players.

Nintendo reasoned that a console could be built on a similar principle; games that anybody could approach, that were easy to start with but increased in complexity with a player's skill – *casual games*. Traditional gamers might find these games fun, but so would a far larger group – non-gamers – people who opted out of playing videogames, like the nursing-home residents, and were worlds apart from die-hard young males who purchased consoles and games.

Focusing on the pain-points of console gaming for non-gamers – elements that turned non-gamers off – Nintendo realized the traditional game controllers were confusing and difficult to learn.¹⁸ Traditional controllers featured a wide array of buttons that had to be pushed at high speed in various configurations and did not appeal to a person willing to give a game console 60-seconds. Games became so complex that entire “eSport” programs were built around them, with college scholarships, tournaments in stadiums, and corporate sponsors.¹⁹ Further, traditional gamers were not welcoming of

“Nintendo reasoned that a console could be built on a similar principle; games that anybody could approach, that were easy to start with but increased in complexity with a player's skill – *casual games*.”

16 Rosmarin, Rachel. "Nintendo's New Look." Forbes. July 13, 2012. Accessed February 18, 2019. https://www.forbes.com/2006/02/07/xbox-ps3-revolution-cx_rr_0207nintendo.html#17dbf98d6781

17 Scimeca, Dennis. "10 Important Reasons Satoru Iwata Will Live Forever in the Hearts of Gamers." The Daily Dot. March 08, 2017. Accessed February 18, 2019. <https://www.dailymotion.com/parsec/satoru-iwata-legacy/>

18 "Playing a Different Game." The Economist. October 26, 2006. Accessed February 18, 2019. <https://www.economist.com/business/2006/10/26/playing-a-different-game>

19 Dollinger, Arielle. "Video Games Are a Waste of Time? Not for Those With E-sports Scholarships." The New York Times. November 02, 2018. Accessed February 18, 2019. <https://www.nytimes.com/2018/11/02/education/learning/video-games-esports-scholarships.html>



newcomers. For example, they adopted disparaging terms for non-gamers unfamiliar with controllers, “noob,” short for newbie.²⁰ Noob’s, the noncustomers of gaming, significantly outnumbered the traditional gamers the industry historically focused on. Noobs – the bane of traditional gamers – were who Nintendo aimed their offering towards.

To solve the pain-point Nintendo innovated a new controller that used motion rather than buttons, a magic wand, called a *Wiimote*, which followed hand motions on-screen.²¹ While Nintendo dialled-up the ease of controlling the system with their new controller, they reduced graphics and sound far below Sony and Microsoft, opting for good-enough. Similar to the DS, the lower graphics made the games far less expensive to develop than Sony or Microsoft consoles²². This created a large library of reasonably-priced games.²³ Nintendo eliminated high-resolution videodisk playback altogether. Their system was assigned the moniker Nintendo Revolution.²⁴

“... [T]here’s this new controller. It is out of this world, literally! You can now move your hand, arm, wrist or body to control the game. If you were playing a fishing game, before you would just press buttons on a controller held in both hands in front of you. With this, you can move your arm back and forth and cast your bait. It senses depth. As someone who doesn’t spend hours per day gaming, I was thrilled with the experience,” said VP of Marketing and Corporate Affairs, Perrin Kaplan.

On April 6, 2006, the name of the not-yet-released Nintendo Revolution was changed to the *Wii*. Gamers scoffed. “Do you have any *Wii* in stock?” they imagined a customer asking. “Of course we do: Urine GameStop!”

was a typical joke.²⁵ But business analysts explained that the *Wii* was something different: “Remember, too, that you’re not the audience for this console,” the influential blog Endgadget wrote to its base of die-hard gamers. “The hardcore market is only a subsegment of the entire population of people who Nintendo *hopes* will become gamers, if approached in the right way with the right product.”²⁶

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Analysts expected the *Wii* to become a niche item competing against Sony’s PS3 and Microsoft’s Xbox 360, but they were wrong. It did not compete. There were no ads suggesting buyers

20 “Noob.” Dictionary.com. Accessed February 18, 2019. <https://www.dictionary.com/browse/noob>

21 Remember that Nintendo’s first video game entrant was a light-gun, similar to the hand controller, for the earliest videogame systems. Nintendo was familiar with the concept of using movement to control electronics. The technology behind the motion-sensing controller, called an accelerometer, was taken from airbag technologies that sensed three-dimensional movement in real time to determine if an airbag must deploy. The *Wiimote* accelerometer is an ADXL330 produced by Analog Devices and measuring just 4mm x 4mm x 1.45mm.

22 A high-quality *Wii* game could be developed for \$5 million; far less than high-quality PS3 or Xbox 360 games.

23 High-end, expensive and oftentimes violent games are usually created via an “engine” – a piece of software allowing the game to be programmed once then deployed to multiple systems without significant additional programming. There are two popular engines for high-end games, the Unreal Engine 3 by Epic Games and CryENGINE in Germany. Both engines supported deploying games to PC’s, PlayStation, and Xbox but neither supported the *Wii*.

30 Rosmarin, Rachel. “Nintendo’s New Look.” Forbes. July 13, 2012. Accessed February 18, 2019. https://www.forbes.com/2006/02/07/xbox-ps3-revolution-cx_rr_0207nintendo.html#17dbf98d6781

25 Cole, Vladimir. “Nintendo “Revolution” Now Called “Wii” [update 6].” Engadget. July 14, 2016. Accessed February 18, 2019. <https://www.engadget.com/2006/04/27/nintendo-revolution-now-called-wii/>

26 *Ibid.*



purchase a Wii *instead of* a Sony or Microsoft console. Instead, the Wii created a brand-new market space and offered incomparable value. In other words, it was not a substitute for other consoles. No matter whether you owned a Sony or Microsoft console, you could still enjoy a Wii. People who would never consider buying a traditional console but wanted to have fun would buy a Wii.²⁷

Released on November 19th, 2006, at a retail price of \$249, the Wii went on to outsell Sony and Microsoft combined through 2009. Unlike Sony or Microsoft, who sold consoles at a steep loss to buy market share, Nintendo made a profit on every console sold from day one.²⁸

"When the (high definition graphics) console wars started, Nintendo stuck with a system that, when it came to graphics, wasn't too far from the original Xbox. It didn't make sense at the time, and some of us didn't think Nintendo stood a chance. Turns out the market agreed that fun was more important than graphics," wrote gaming industry analyst Jacob Lopez.²⁹

The fastest selling game console in history, Nintendo eventually sold 101 million Wii's.

Into the Red: In Response to Disruptive Technology, Nintendo Decides to Compete

With Wii's flying off store shelves faster than they could be stocked, on January 9th, 2007, Apple's Steve Jobs made what at the time sounded like an entirely unrelated announcement:

"The most advanced phones are called smartphones. And the problem is that they're not so smart and they're not so easy to use... What we wanna do is make a leapfrog product that is way smarter than any mobile device has ever been, and super-easy to use. That is what the iPhone is, OK? So, we're gonna reinvent the phone."

The first iPhone, which people loved, only supported programs (apps) created by Apple. That changed soon after. Frustrated by their inability to install third-party apps, hackers began "jailbreaking" the phones, sidestepping Apple's security to enable users to install third-party programs, just as they could on any computer. After months of fighting the hackers, on July 10, 2008, Apple opened the App Store, allowing developers to sell and install software on their popular phones. Games quickly became one of the most popular smartphone app categories.

Smartphones were great for gaming, especially casual games. First the iPhone, then Google's Android, provided an ideal user experience. Rather than remain tethered to a television, smartphones allowed users to game everywhere and anywhere. By connecting wirelessly to the internet, they enabled people to easily play against one another. Smartphones were good for phone calls, email, text messages, and web browsing; with their relatively powerful computing power they were great for games.

27 Sterlicchi, John. "Nintendo's Wii Console Captures New Game Market." The Guardian. October 10, 2007. Accessed February 18, 2019. <https://www.theguardian.com/business/2007/oct/10/usnews.internationalnews>

28 O'Brien, Jeffrey M. "Wii Will Rock You (Fortune, 2007)." Fortune. June 4, 2007. Accessed February 18, 2019. <http://fortune.com/2007/06/04/nintendo-wii-will-rock-you/>

29 Feltham, Jamie. "HTC Is Taking Applications for 6DOF Dev Kits." VentureBeat. November 03, 2018. Accessed February 18, 2019. <https://venturebeat.com/2018/11/04/htc-is-taking-applications-for-6dof-dev-kits/>

Casual games, the category innovated by Nintendo with the Wii, became especially popular for people sneaking in short bursts of game time while commuting, waiting in line, or even working.³⁰ But Nintendo's DS system, with its small screens and no utility value beyond gaming, was now obsolete. Since users had an array of approachable games they could control just by moving their phones, the appeal of the Wii to control with movement wore off. High-powered consoles for traditional gamers continued to sell as smartphones became popular, but the elements of the Wii that differentiated it were lost against the new smartphones.

The situation grew worse with the introduction of tablets – essentially large phones with bigger screens – that were even better for gaming and so intuitive that babies could use them. Whereas developers could program DS games for hundreds of thousands of dollars, they could create phone games for hundreds of dollars. For example, Vietnamese programmer Dong Nguyen, working alone, spent three days creating a phone game called *Flappy Bird* which went on to earn \$50,000 per day.

“... some of us didn’t think Nintendo stood a chance. Turns out the market agreed that *fun was more important than graphics.*”

– Gaming Industry Analyst Jacob Lopez.

Nintendo went from boom to bust, squeezed by mobile platforms for casual games and high-end consoles for traditional gamers. In late July 2011, the situation was dire enough that Iwata slashed his own salary, about \$770,000, by half. Other executives, including legendary designer Miyamoto, took pay cuts of 20% to 30%.³¹ They also slashed the price of the Nintendo 3DS, a three-dimensional version of the DS that relied on gimmicky technology that was not well received, from \$250 to \$170.³²

To work their way back, Nintendo decided they had to compete by offering some type of tablet.

The Wii's successor, called the *Wii U*, was released on November 18th, 2012. The system featured a 6.2-inch (15.7cm) touchscreen tablet, *GamePad*, that connected wirelessly to the game console. In contrast, the state-of-the-art iPhone 5 featured a 4-inch screen. The iPad Mini, released ten days before the Wii U, featured a 7.9-inch screen. The standard iPad sported a 9.7-inch screen. Whereas the iPhone and iPad contained full-blown computers, the Wii U required the GamePad to be within 25ft (8m) of the base system that contained the Wii U's computer. Reviews ranged from bad to worse:

- “freakishly long feature list”
- It will “underwhelm tablet owners who are used to higher quality displays”³³
- “feels a little cheap and flimsy”
- “makes small elements a little blurry”

³⁰ This introduced serious issues, including workplace fatalities caused by distracted gamers, that the authors acknowledge but which are beyond the scope of this case study.

³¹ Kohler, Chris. "Nintendo Chief Takes 50% Pay Cut After 3DS Markdown." *Wired*. December 22, 2017. Accessed February 18, 2019. <https://www.wired.com/2011/07/nintendo-satoru-iwata-pay-cut/>

³² From this time to 2018 top selling DS games did not utilize the 3D technology.

³³ Vargus, Nic. "Nintendo Wii U Review (2012)." *IGN Boards*. November 21, 2012. Accessed February 18, 2019. <https://www.ign.com/articles/2012/11/21/wii-u-review>

- “It’s a disaster of a touchscreen”
- “Every game implements the GamePad differently, and most don’t do it very well.”³⁴

Whereas Wii reviews focused on how the system was easy and fun, Wii U reviewers focused on the GamePad as a piece of technology, comparing it negatively to tablet-based gaming.

In November 2013, Sony and Microsoft released new consoles one week apart. Locked in a computing power arms race focused on technological advances for ever-faster and realistic gaming, both offered blazingly fast gameplay, ultra-high-definition graphics and sound, games that were often violent, and online gameplay with real-time chat.³⁵

As of October 2018, Sony had sold 86 million PlayStation 4 units and Microsoft 39 million Xbox One units. Nintendo sold an abysmal 13.5 million Wii U units before the system was discontinued in 2017.

Searching for a New Blue Ocean

“It’s time for Nintendo to leave consoles in the past. I’ve rewritten this opening paragraph multiple times trying to figure out the right way to say that. I’ve written that there are few surprising things in the gaming industry these days, save for Nintendo, which remains a wild card of poor marketing decisions, and that Nintendo’s mistakes have proven that it’s software, not hardware, that people are interested in. Sometimes, though, it’s best just to come out and get to the point: Nintendo needs to close the curtains on its hardware business and transition to being a pure software developer.”

Eric Abent, *Slash Gear*, September 5th, 2016

Recalling the gloomy days of the GameCube, analysts again urged Nintendo to focus on software, creating games that run on mobile phones and tablets. Mobile gaming had grown to a \$106 billion market by 2016.³⁶ Analysts noted that despite the mobile game market size – Sony and Microsoft still sold an enormous number of consoles and games: \$35 billion together.³⁷

34 Pierce, David. "Nintendo Wii U Review." *The Verge*. November 18, 2012. Accessed February 18, 2019. <https://www.theverge.com/2012/11/18/3658130/nintendo-wii-u-review>

35 Sony and Microsoft chatrooms are infamously hostile. Countless videos have been published of people, including young children, yelling profanities at one another over game chat systems. In 2017 a gamer arranged for a third party to call the police and pretend to be on the verge of a murder spree, with the intent of sending police to the home of a gamer he had lost an online match too. Gamers call this activity “swatting,” after the name of the heavily armed police who respond to these calls, “SWAT” units. However, the target gamer had given a fake address. When police arrived at the address, a random house, the 28-year-old resident was predictably confused and waved them away. Believing he was a deranged killer reaching for a weapon the SWAT team shot and killed the man. The gamers involved, Shane Gaskill, 19, and Casey Viner, 18, had wagered \$1.50 in an online tournament that led to the incident. As of 2018 both men Gaskill and Viner face felony prosecutions; Barriss has been sentenced to 20 years in prison. Stevens, Matt, and Andrew R. Chow. "Man Pleads Guilty to 'Swatting' Hoax That Resulted in a Fatal Shooting." *The New York Times*. November 14, 2018. <https://www.nytimes.com/2018/11/13/us/barris-swatting-wichita.html>

36 Takahashi, Dean. "Newzoo: Games Market Expected to Hit \$180.1 Billion in Revenues in 2021." *VentureBeat*. May 02, 2018. Accessed February 18, 2019. <https://venturebeat.com/2018/04/30/newzoo-global-games-expected-to-hit-180-1-billion-in-revenues-2021/>. By 2018 the mobile game market is \$138 billion and is projected to reach \$180 billion by 2021.

37 Takahashi, Dean. "Sony Dominates Console Market with 57% Share Worldwide." *VentureBeat*. March 16, 2017. Accessed February 18, 2019. <https://venturebeat.com/2017/03/16/sony-dominates-console-market-with-57-share-worldwide/>

Mobile gaming did not disrupt console sales in the core gamer market; the failure of the Wii U was because when Nintendo attempted to counter the mobile-gaming disruption of the casual gamer market, it locked itself into a technology-based battle on hardware that it had little chance of winning. In response, Nintendo moved into the mobile space, partnering to release one game and developing several other games on its own.

Pokémon Go

Game studio Niantic, originally part of Google, released a mobile game called *Ingress* that required players to walk to physical places rather than sitting still to play. Once they reached the same real-world place players would battle one another in real time, on their phones, for domination. *Ingress* was moderately successful, attracting a small but loyal fan base. One of those fans was Tsunekazu Ishihara, president of the *Pokémon* Company that produced the popular *Pokémon* television show and related media. Ishihara approached Nintendo's Iwata about developing a similar game featuring *Pokémon* characters.³⁸

Ishihara and Iwata partnered with Google to create a prototype of the idea, an April Fool's joke for Google Maps where users could run and catch *Pokémon* around the world (the Niantic team included the people who developed Google Earth that evolved into Google Maps). The concept proved popular and the two partnered with and funded Niantic, which already had location information and technology infrastructure from *Ingress*, to spin-out the company from Google and

“... mobile gaming did not disrupt console sales; the failure of the Wii U is because Nintendo did not offer a console that buyers wanted.”

develop their game.³⁹ Like *Ingress*, players must walk to physical locations. *Pokémon* are superimposed on top of the real-world, via a live video stream from a phone using a technology known as

augmented reality. Walking allows players to capture and grow *Pokémon*, which they fight against one another at larger locations or “gyms.” *Pokémon Go* was released on July 6, 2016.

Pokémon Go was a smash success, rapidly becoming the most popular smartphone game on both Android and iOS with over 20 million daily active users. Only leading messaging and social media apps had higher daily active user figures.⁴⁰ In the US, over 34 million people downloaded the game and after a month 90% were still playing.⁴¹ The game was so popular that the computer servers it relied on routinely crashed from overuse. While *Pokémon Go* was predictably popular with young millennials, Gen-X and baby boomers accounted for almost half the players. Usage was split 60/40 between male/female gamers.⁴² Two years later, the game was still popular, with

38 Nintendo owns 32% of the *Pokémon* franchise.

39 This arrangement involved Nintendo purchasing an unknown percentage of Niantic.

40 Dogtiev, Artyom. "Pokémon GO Revenue and Usage Statistics (2017)." Business of Apps. May 4, 2018. Accessed February 18, 2019. <http://www.businessofapps.com/data/pokemon-go-statistics/#1>

41 "Pokémon Go: 34m Downloads, 31m Current Players, and 10m Paying Users since U.S. Launch." YouGov. Accessed February 18, 2019. <https://today.yougov.com/topics/entertainment/articles-reports/2016/08/12/pokemon-go-34m-downloads-31m-current-players-and-1>

42 Perez, Sarah. "Pokémon Go's Paying User Base Has Reached a Plateau." TechCrunch. July 29, 2016. Accessed February 18, 2019. <https://techcrunch.com/2016/07/29/pokemon-gos-paying-user-base-has-reached-a-plateau/?ncid=rss>



147 million active users in May 2018 and \$104 million in revenue.⁴³ As the weather cools down, the game – which is played primarily outside – tends to wane in popularity. However, even in the winter of 2018, there were still five million daily active users, 65 million monthly active users, and revenues of \$2 million per day from advertising and in-game purchases.⁴⁴ A unique feature was the ability for businesses to draw in players. Businesses can, for a small fee, lure more Pokémons to their storefronts, where players will congregate and, with the right incentives, make purchases. The game literally walked customers to advertisers. By the end of 2018, Pokémon Go had exceeded \$2 billion in revenue, a milestone shared with only four other phone games.⁴⁵

Nintendo Produced Mobile Games

On December 15, 2016, Nintendo released a Mario title for use on mobile platforms, *Super Mario Run*, the first Mario game run on non-Nintendo computing hardware. The game itself was similar to others in the crowded genre known as a “side-scroller” where players manipulate a character to intersect with or avoid obstacles. Despite an arguably lack of originality in gameplay, *Super Mario Run* proved incredibly popular, with 50 million downloads in the first week and 200 million by the end of 2017.⁴⁶

Nintendo also released *Fire Emblem Heroes* in February 2017 and *Animal Crossing: Pocket Camp* in the fall of 2017. *Fire Emblem* is a strategy role playing game and *Animal Crossing* a camping simulator.

All Nintendo mobile games had a common business model – known as a “freemium”, where apps are free to download and try but users must pay for additional features or functions.⁴⁷ In the case of *Super Mario Run*, early levels were free but a relatively steep \$10 fee was required to unlock additional levels.⁴⁸ The other games were also downloadable for free but offered smaller in-game purchases, at lower cost, rather than one large purchase to unlock an entire game.

Nintendo did not break down downloads or revenue figures for the latter two. Despite a large number of downloads, *Super Mario Run* had “not yet reached an acceptable profit point” while *Fire Emblem Heroes* was doing well financially.⁴⁹ “Our objective is to offer a service that allows even consumers who do not normally play games on a regular basis to have a little fun each and

43 Tassi, Paul. "'Pokémon GO' Is More Popular Than It's Been At Any Point Since Launch In 2016." Forbes. June 27, 2018. Accessed February 18, 2019. <https://www.forbes.com/sites/insertcoin/2018/06/27/pokemon-go-is-more-popular-than-its-been-at-any-point-since-launch-in-2016/#6f09d78cf26>

44 Smith, Craig. "115 Amazing Pokémon Go Statistics." DMR. January 21, 2019. Accessed February 18, 2019. <https://expandedramblings.com/index.php/pokemon-go-statistics/>

45 Tassi, Paul. "'Pokémon GO' Has Just Crossed \$2 Billion In Revenue Since Launch, Almost An Industry Best." Forbes. September 25, 2018. Accessed February 18, 2019. <https://www.forbes.com/sites/insertcoin/2018/09/25/pokemon-go-has-just-crossed-2-billion-in-revenue-since-launch-almost-an-industry-best/#1074c85a3257>

46 Webster, Andrew. "Super Mario Run's 200 Million Downloads Didn't Result in 'acceptable Profit' for Nintendo." The Verge. October 31, 2017. Accessed February 18, 2019. <https://www.theverge.com/2017/10/31/16580976/super-mario-run-nintendo-downloads-profit>

47 Perez, Cody. "How to Enjoy Super Mario Run for Free." GameRevolution. August 17, 2017. Accessed February 18, 2019. <https://www.gamerevolution.com/guides/345493-enjoy-super-mario-run-free>

48 Nintendo is continually adding levels to the game while releasing prior levels, that cost money, for free. Once the player pays to unlock the game all future levels are unlocked.

49 Webster, Andrew. "Super Mario Run's 200 Million Downloads Didn't Result in 'acceptable Profit' for Nintendo." The Verge. October 31, 2017. Accessed February 18, 2019. <https://www.theverge.com/2017/10/31/16580976/super-mario-run-nintendo-downloads-profit>



every day," Nintendo announced. As of July 2018, *Fire Emblem Heroes* had grossed \$400 million, *Super Mario* \$64 million, and *Animal Crossing* \$42 million.⁵⁰

Back to Blue Ocean Consoles: Nintendo Switch

Sony and Microsoft continued the red ocean console war, each outdoing the other in terms of high-end technology for increased computing power.⁵¹ Nintendo could not and did not want to compete – either with Sony, Microsoft, Apple, or anyone else. The Kyoto firm needed to reboot, to value innovate something different.

Complicating that effort, Iwata died in 2015 at the early age of 55, leaving a leadership vacuum. Senior Nintendo executive Tatsumi Kimishima stepped in as transitional CEO. A banker who after 27 years had left Sanwa Bank to join first The Pokémon Company, then Nintendo, he was a strong finance manager but not especially creative.⁵² His prior involvement in senior leadership had been before Iwata and resulted in the disastrous Game Cube.

Nevertheless, Nintendo defied all odds (and countless critics) when it released Iwata's last project, the *Nintendo Switch*, on March 3, 2017. Nintendo describes the core Switch value proposition as an "Anytime – Anywhere – With Anyone" play concept.⁵³ The Switch could be used as a traditional console and also a portable system – a new 'hybrid' product category. As a portable system, it featured a 6.2 inch (15.75cm) bright and responsive touchscreen, with two motion sensitive controllers that attach on each side. As a console, the controllers are removed and the console placed in a dock to control a television. The same games run in both portable and console mode, though the graphics were smoother when the system is attached to a television.⁵⁴

Whereas the Wii U handled video calls, contained a web browser, and did virtually anything a tablet could do (albeit poorly), the Switch eliminated all non-game functions: it did not play movies, stream video or allow web surfing. Despite that the system has the technical capability to handle media, and an internet connection no less powerful than tablets, the company deliberately eliminated all non-game functionality. There are no phone calls, no Netflix, no Kindle reading app, no email or web browsing.⁵⁵

Previously, when the Wii U was released, Nintendo allowed and encouraged game developers to create third-party game titles. The system was subsequently flooded with a large selection of low-quality titles that confused and annoyed customers; "this game is an unfortunate mess..." reads a not atypical review of a Wii U game.⁵⁶ Pivoting to the Switch, the company forced unknown game

50 McAloon, Alissa. "With \$400M Revenue, *Fire Emblem Heroes* Reigns as Nintendo's Big Mobile Earner." Gamasutra Article. Accessed February 18, 2019.

https://www.gamasutra.com/view/news/323556/With_400M_revenue_Fire_Emblem_Heroes_reigns_as_Nintendos_big_mobile_earner.php

51 Sony and Microsoft have been competing over largely undifferentiated offerings for, as of fall 2018, 17 years. Neither company has signalled a substantive change in strategy.

52 Despite strong sales, Kimishima, who was in his late 60's, would step aside within three years, ceding the CEO's position to a significantly younger Shuntaro Furukawa.

53 Nintendo Co., Ltd. Six Months Financial Results Briefing for Fiscal Year Ending March 2018.
https://www.nintendo.co.jp/ir/pdf/2017/171031_2e.pdf

54 Nintendo purposefully slows high-resolution graphics rendering in portable mode to extend battery life.

55 There is a *hidden* web browser in the Switch that hackers show can be accessed with light hacking. The exclusion of the web browser as a supported feature is purposeful: Nintendo intended the Switch to be used solely as a gaming device.

56 "Worst Wii U Games." Top Ten Types of Roller Coasters - TheTopTens®. Accessed February 18, 2019.
<https://www.thetoptens.com/worst-wii-u-games/>

developers to submit games that were finished (or nearly so) before considering whether they would be authorized, a system more like that used by Apple for iOS (iPhone and iPad) apps.⁵⁷ Leading game studios were encouraged to create games for the Switch before it was released, but were forbidden to discuss the device with the gaming media, rather than hyping it as Nintendo had done in the past.⁵⁸

Technology disruption is commonplace, but the scope of what Nintendo faced was unusual. A decade earlier, its noncustomers had included a blue ocean of people who thought of videogames as console games for boys and young men: testosterone-filled, violent and complicated. When it came to the development of the Switch, these noncustomers had been made aware of casual games either by the Wii or via mobile technology. Nintendo was not going to create high-powered gaming consoles to compete with Sony or Microsoft, nor offer a smartphone or full-blown tablet.

Instead, Nintendo reconstructed market boundaries, capturing the best of high-powered game consoles and smartphone games. First, it raised the depth and complexity of its casual games. This captured players who craved games with deeper themes than mobile games but were uncomfortable with the complexity, violence and sport-simulation games common on Sony and Microsoft's consoles. *Legend of Zelda: Breath of the Wild* allows players to roam around an enormous freeform world, interacting with countless characters while going on quests, or simply seeing what the Nintendo creative team had dreamed up. *Splatoon* is a shooting game where players play one another online except they shoot paint, not armaments. Their latest edition of Mario, *Super Mario Odyssey*, had the original two-dimensional included for nostalgic parents. *Arms* allows players to fight one another on-screen with their fists, which they must pump and move in real life, providing an upper body workout.

Second, while raising the level of gameplay from the casual game movement Nintendo also created a framework to enable multiplayer games on one device. Mobile devices had networked games that played over the internet, but the Switch – with its two controllers (and two more that could be added) – excelled at enabling multiple players to use one Switch. A hybrid system that worked as both a portable device and a docked system was the inspiration for the name – Switch – because first-time players could easily switch between the two dominant game platforms with one device that worked seamlessly as a portable and as a docked station. *Mario Kart* allowed up to four players to compete against one another with one Switch.

As of Q2 2018, Nintendo had sold just under 20 million Switch consoles, making it the fastest selling game console in history after the Wii.⁵⁹ Analysts struggled to answer the question “what is the Switch competing against?” It’s not a handheld, not a console, not a phone or tablet, and definitely not a general-purpose computer. Eventually, they concluded “Nintendo is mostly

⁵⁷ Nintendo Developer Website. <https://developer.nintendo.com/>

⁵⁸ Priestman, Chris. "What's It like Developing for the Switch? 9 Indie Studios Weigh in." Gamasutra Article. March 10, 2017. Accessed February 18, 2019. http://www.gamasutra.com/view/news/293404/Whats_it_like_developing_for_the_Switch_9_indie_studios_weigh_in.php

⁵⁹ Kuchera, Ben. "The Nintendo Switch Has Sold Close to 20M Units, but What Does That Mean?" Polygon. July 31, 2018. Accessed February 18, 2019. <https://www.polygon.com/2018/7/31/17634450/nintendo-switch-console-hardware-sales>



competing against itself ... Nintendo created a new market category, and is reaping the rewards."⁶⁰ Once again it made the competition irrelevant.

Epilogue

"Nintendo is mostly competing against itself ... Nintendo created a new market category, and is reaping the rewards."

than traditional console games. Additionally, Nintendo released a series of toys called the *Labo*, pieces of cardboard that use the Switch console and controller to create entirely new physical/digital world hybrid systems. For example, players can create a piano from cardboard then play it with the notes and sound showing up on the console. Or they can create a fishing rod used to fish inside a virtual lake that appears on the console. A cardboard gas pedal controls the cars in *Mario Kart*. There are also Amiibo toy figurines that when placed next to certain consoles enable new functionality. While the idea isn't new, it's done well thanks to Nintendo's strong IP, with over 20 million figurines and over 15 million trading cards sold.⁶¹

However, as demonstrated by the boom-and-bust nature of prior systems, somebody else will inevitably copy what makes the Switch special, sending Nintendo back to the drawing board. Successful blue ocean innovations are eventually copied, some with more success than others. These me-too copies usually take decades to have an impact, but the business cycle of videogames is hyper-accelerated, not unlike the games themselves.

Nintendo continues to innovate. The company is releasing new games that follow the same strategic path; more complex than casual games yet less violent and easier to get started

⁶⁰ *Ibid.*

⁶¹ Calvert, Darren. "While Other Toys-To-Life Products Struggle, Sales Of Amiibo Continue To Grow." *Nintendo Life*. April 26, 2018. Accessed February 18, 2019.

http://www.nintendolife.com/news/2018/04/while_other_toys-to-life_products_struggle_sales_of_amiibo_continue_to_grow



Questions

Can you see a pattern behind the ups and downs of Nintendo's 129-year-long corporate history? What kind of strategic behaviour consistently led it into the trap of red ocean competition? And what kind of strategic behaviour enabled it to break away from the pack and create blue oceans?

Gaming is a tech-intensive industry. Was technology innovation the defining factor for Nintendo's success? If not, what was the key factor behind Nintendo's business success? What role did technology play in Nintendo's new market creation?

According to the case, smartphones and tablets massively disrupted the traditional gaming industry. What were Nintendo's responses? What worked and what didn't? Can you use relevant blue ocean frameworks to explain how Nintendo's Pokémon Go eventually created a new blue ocean out of the disrupted market?

From a corporate perspective, with public corporations' mandate to balance earnings stability and growth, what can we learn from Nintendo's portfolio management practices over the last 20 years? Plot Nintendo's business offerings on Kim & Mauborgne's Pioneer-Migrator-Settler Map and compare the results across different time periods. What key insights do you gain?

Do the majority of people buy videogames based on technology per se or based on value? If on value, then why do Nintendo's competitors focus so heavily on marketing their technology?