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# 1983: The Crash



1982 was a terrific year for the burgeoning video game industry. New systems and software houses were popping up everywhere and hardware sales were phenomenally high for all the main players, including Atari, Intellivision, and the newly-arrived ColecoVision. Unfortunately, this very fast and explosive expansion was carrying also the seeds of its sudden demise and the industry's success would change within a matter of months.

Throughout 1982, Atari executives were confident they would be able to meet a 50% year-over-year increase in sales, as stated in their financial outlooks. However, during the quarterly conference call on December 7, 1982, it was finally declared that the actual growth was only around 10%. The huge miss from the original, overly optimistic estimates sent analysts and investors into a panic. On Wall Street, Warner immediately lost 32% of its market price, falling from \$51.75 to \$35.13 a share.

While results from other manufacturers like Coleco were still in line with original expectations, suddenly people at all levels—from analysts to executives to developers to gamers—realized there was something wrong throughout the whole industry. This abrupt awakening and consequent pessimism triggered a snowball effect in which people started to lose interest in playing, and more importantly in buying, new games.

How could all of this have happened? There were different reasons that combined to cause the dramatic implosion of the market that was witnessed between 1983 and 1984. Most likely, the main factors involved were:

- ❑ public perception,
- ❑ over-saturation and low-quality games,
- ❑ transitioning to a new generation, and
- ❑ home computer wars.

We will proceed in analyzing each of these individually to gain a better understanding of what was happening across the industry, and in American society, at that time. After that, we will see how individual companies were affected.

## Public Perception

Unfortunately, video games were seen with diffidence and scrutinized under a suspicious light by the general press and public alike since their very early days. In 1976, in fact, *Death Race*, an arcade game somewhat inspired by the cult sci-fi movie *Death Race 2000* (1975), was released and many people began perceiving video games as something “evil,” able to excite our worst instincts and negatively impact young people.



*Death Race*, an arcade game released in 1976 by Exidy where players had to compete by driving a car to run over stylized zombies. Most people, though, felt the objective of the game was to mercilessly run over pedestrians, like in the *Death Race 2000* movie.

Negative perception became more widespread in the early eighties when home and arcade games were at their peak. Many parents started blaming video games for the faults of their own children or, more generally, of the younger generation as a whole. One of the most vocal critics was Ms. Ronnie Lamb who was invited to famous TV talk shows where she described how bad video games were for young people by encouraging them to waste money, energy, and valuable time. As a result of her crusade, several small towns in the United States banned video game arcades or stopped opening new ones. Since then, video games have remained in the spotlight.



The front page from a 1983 issue of *Weekly World News*. The headline was dedicated to the sudden death of a teenager who suffered a heart attack while at an arcade. Obviously, video games were accused.

This attitude was not limited to the United States, though, and petitions against video games were raised in many different countries. As early as November 19, 1981, President Marcos of the Philippines banned all video games in his country, giving the population 15 days to destroy or surrender any game console to the army. The negative sentiment was shared in other countries in Southeast Asia. For example, people in Malaysia also asked for the legal ban of video games, claiming, “video games are all about killing, violence, and racism.”<sup>1</sup>

In such a heated environment, many people who were unable or unwilling to understand the new media and its unique possibilities would have been more than happy to see video games disappear and would have gladly helped push them into oblivion.

## Over-Saturation and Low-Quality Games

In 1982, it was estimated that the US home video game market could absorb up to 60 million cartridges. Unfortunately, that was the number of cartridges Atari alone published throughout the year while Activision was manufacturing between 10 to 15 million and every other company was contributing at least two million, bringing the actual total number to almost 120 million. Obviously, much of this

<sup>1</sup> Mr. Martin Khor, Consumers' Association of Penang, Malaysia, as reported in an interview published on local and international newspapers and magazines in early 1983.

huge inventory was not sold and the situation was worsened by a drastic drop in quality for the average title, including those by Atari itself.

The first dramatic example of this new trend occurred in early 1982 when Atari released its own version of the iconic arcade game *Pac-Man*, for which it had recently acquired exclusive rights for home consoles. To capitalize on the *Pac-Man* craze, the game was rushed to market and Ray Kassar finally agreed to give a small royalty to the developer, Todd Frye, as an incentive to work as quickly as possible.<sup>2</sup> The game was programmed in six weeks and released at a \$37.50 price point towards the end of March. At that time, Atari's installed user base was estimated to be still less than 10 million units. Nonetheless, Atari manufactured more than 12 million cartridges since they were sure the game would be a system seller and everyone would buy it. Unfortunately, the game was a very poor imitation of the original, bugged by slow animations and an unbearable flickering effect that made the ghost continuously disappear from the screen.

Despite all this, Atari's *Pac-Man* sold seven million units; however, that still left the company with a huge unsold inventory and, more importantly, it disillusioned most VCS owners who started losing faith in the system's actual capabilities.



*Pac-Man* for the Atari 2600. Notice how only one ghost and two power pellets are visible in this screenshot—the others were not displayed in this frame due to flickering. Despite selling seven million units thanks to *Pac-Man* fever, its poor quality tarnished Atari's reputation forever.

Unfortunately, this was only the first among a string of poor games that Atari had in the pipeline. Many soon followed, including an unlikely rendition of Rubik's Cube, ultimately hitting bottom with the infamous *E. T. the Extraterrestrial* game based on the popular movie by Steven Spielberg. In the latter case, even Ray Kassar strongly opposed the project and it was Steve Ross, the head of Warner Communications, who forced it and decided to pay Spielberg \$25 million for licensing the game. *E. T.* turned into the worst business deal ever made in video game history and permanently sealed Atari's fate.

<sup>2</sup> Todd received \$0.10 per cartridge sold.

The fateful deal was signed in July 1982. On July 23, Kassar assigned the project to Howard Scott Warshaw,<sup>3</sup> one of the best young programmers who hadn't yet defected from Atari, with the task of creating the game by September 1 to allow the required manufacturing time and ensure that the game would be on shelves before Christmas. With just a few weeks available, it was no wonder that the game turned out to be a huge disappointment with poor and confusing gameplay, but things were worsened by Ross's decision to manufacture almost five million cartridges. The game sold about 1.5 million, leaving Atari with another huge inventory of unsold cartridges that were buried in a landfill in the New Mexico desert and later destroyed.

Even though companies like Activision and Imagic kept releasing excellent and polished titles, almost all other companies started rushing out weak productions hoping for a quick buck. In a matter of months, the marketplace was cluttered with terrible or even controversial and plainly disgusting titles like *Custer's Revenge* and *Beat 'Em & Eat 'Em* by Mystique, the first software house to release pornographic games on the Atari 2600.<sup>4</sup> With such an appalling catalogue, it is easy to understand why many people started losing interest in games.

## Transitioning to a New Generation

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In the early eighties, every issue the industry faced posed new challenges that had to be solved without any historical reference or previous case studies. While the transition from dedicated systems like the Home Pong to cartridge-based systems was natural and straightforward, it wasn't as easy to decide when the next wave of consoles should come out.

As we discussed, Nolan Bushnell would have already launched a new console in the late seventies but Ray Kassar had other ideas and wanted to capitalize as much as possible on the VCS instead. Starting the transition most likely fell on Atari's shoulders. Though Atari was the industry leader, the competition was getting stronger and stronger and something needed to be done; but how could they capitalize on the existing user base? Kassar decided to have two independent systems at the same time—the best selling VCS, now renamed 2600, and the new, more powerful Atari 5200.

Paradoxically, when the 5200 finally came out in November 1982, it had to be pushed by Kassar himself who decided to overrule a petition from Atari's own engineers who were asking to cancel the launch and redesign the console. The 5200 was indeed rushed, both internally (it was basically an Atari 400 computer without any

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<sup>3</sup> Howard developed hits like *Yar's Revenge* and movie-licensed games like *Raiders of the Lost Ark*.

<sup>4</sup> Atari actually sued Mystique for tarnishing its image. In those days, after Atari lost its legal battles against Activision for producing third-party software, there was no way for hardware manufacturers to control the content of titles published on their systems.



The Atari 5200 Super System. The successor to the VCS was an Atari 400 computer in a different dress. It retailed for \$250 and, overall, only 69 games were released before the console was discontinued in March 1984.

new technology whatsoever) and externally, where cheap non-self-centering joysticks made playing arcade style games a real pain. Moreover, the 5200 didn't offer retro compatibility (neither with the 2600 nor with the Atari 400 due to different registry locations in memory) and had only a very limited launching catalogue mostly based on ports, offering no real incentive to existing users to upgrade.

On the other hand, Mattel tried a different route. Instead of producing a completely new system, they decided to do a restyling of their successful Intellivision console to make it look sleeker while also cutting production costs. Released in 1983, the



The Intellivision II was basically a simple restyling of the original and retailed in early 1983 for \$150. It was soon discounted to \$69 and then discontinued.

Intellivision II featured handy detachable controllers and new add-on peripherals<sup>5</sup> but, unfortunately, construction materials were not as reliable as before; for example, the controllers' side buttons wore out very easily, making the playing experience much more uncomfortable.

Overall, towards the end of 1982 and early 1983, there was not only a proliferation of worthless games, but also a new iteration of consoles that were disappointing for different reasons and, ultimately, delivered experiences that were far below expectations.

## Home Computer Wars

As if the preceding problems were not enough to put the video game industry on its knees, the knockout blow was delivered by consoles' "cousins"—the home computers and, more precisely, Commodore.

Having successfully delivered the VIC-20, the first color home computer for less than \$300, Commodore's marketing effectively positioned their machine as a "smart" alternative to mere game consoles. The same strategy was adopted and emphasized even more strongly in 1982 with the release of the model that changed the face of home computing: the Commodore 64, or C64 for short. Commodore started retailing its new computer at \$595, an already very low price when compared to machines with similar specs like the Apple II, but it soon started cutting its price lower and lower and offering a \$100 rebate for anyone who was willing to trade an existing computer or game console for a new C64 in 1983.

Effectively lowering prices while keeping profit margins intact was mainly possible due to Jack Tramiel's aggressive vertical integration approach, but the whole company was actively involved in the process of reducing costs as much as possible. For example, a very hard-working engineering team kept combining and reducing the number of chips required, making the final designs cheaper to manufacture. At the same time, Jack also kept constantly negotiating better prices and deals with vendors for the only peripherals that Commodore was not producing in-house (like printers and disk drives). This was happening very quickly, forcing every computer manufacturer (like Atari, Texas Instruments, Tandy, Apple, etc.) to decide quickly how to behave and react to Commodore's war.

Apple wisely decided to stay out of the fight and ignored Jack's philosophy to "sell to the masses, not to the classes." The latest iteration of the Apple II was

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<sup>5</sup> New peripherals included a music keyboard and a module to play Atari 2600 games. The Intellivision II tried to prevent unauthorized cartridges to run in an interesting way: by secretly changing the internal exec ROM. As a result of these changes, some Coleco games could not be run anymore. For a proper mechanism to forbid playing unlicensed third-party cartridges, though, players had to wait for Nintendo and its NES launch in 1985.

selling for a much higher price than the C64 while having very similar capabilities, but this strategy, supported by an effective marketing campaign, turned Apple into a company designing “high class” and “cool” products made for people who wanted to differentiate themselves from the generic crowd. While they sold many fewer units than did Commodore, they had a very high profit margin and, ultimately, this unique approach set Apple apart from the competition and worked very well.

Almost every other company instead feared losing too much of their market share and followed Commodore in cutting prices, seriously compromising their profit margins instead. None were as organized as Commodore and able to sustain such a strategy for a long time and they soon had to start selling computers below cost while relying on margins on software sales to make a profit. When Commodore also started reducing the price for its new in-house developed software titles (including both games and utilities) the war was over. In 1983, Commodore was the first computer manufacturer to report \$1 billion in sales, seizing the market and leaving all others in the dust.

## Casualties

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The effects triggered by the combination of these factors were devastating. Basically, all console manufacturers were wiped out in a matter of months and many computer companies and software houses were also forced out of business. Atari racked up a total of more than \$500 million in losses in 1983 and Warner ultimately decided to split and sell the company in 1984.

Having the most advanced console didn't save Coleco either, and the company shut down its video game department in 1985 after having lost \$258 million. But the most sudden changes happened at Mattel, where, within a two-week period during the spring of 1983, the company went from aggressively hiring game programmers to laying them off. Mattel Electronics posted a \$100 million loss in the first half of 1983, and when the total losses added up to \$300 million in early 1984, the division was closed permanently.<sup>6</sup>

Not only were hardware manufacturers harmed, but all software houses focusing on game consoles were obviously affected. Many, having just released titles that remained completely unsold with others already in the production pipeline, had to file for bankruptcy. Only the most stable and successful companies were able to survive, often in a much scaled-down structure, thanks to the huge amounts of cash they were able to save from their earlier days. Activision, for example, shifted its focus to

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<sup>6</sup> The Intellivision rights were sold to a new company, INTV Corp., that kept producing a few games while marketing a restyled version of the console until 1991.



computer games and other software products, and a few years later even changed its name to Mediagenic to emphasize its new global focus.<sup>7</sup>

On the computer side, many of the companies that tried to fight the price war with Commodore were severely affected or even forced out of business. For example, different models that made history during the early days of personal computers quickly lost their appeal and disappeared altogether, like the Texas Instruments TI99/4A. Others slowly faded into oblivion like the Tandy TRS line of computers that, besides being less competitive price-wise, was also confined to the RadioShack electronics stores and couldn't match the market penetration that a more general, non-exclusive approach granted to Commodore machines.

The 1983 crash was particularly devastating in North America (where almost all relevant companies were located), but its effects in other parts of the world, like Europe or Japan, were not as dramatic. In Europe, for example, the market had shifted from consoles to computers too, but European software houses were just beginning their operations at the time. Luckily, they had no unsold backlog catalogue to worry about and had no issues in adapting to the new trends; they started to develop games for computers instead. This approach was also fostered by a growing local computer industry, mostly located in the UK. Video games just changed platforms while remaining the most beloved entertainment activity for kids and teenagers in northern and southern Europe alike.

Games in Japan were having their own independent development too, with new computers and consoles coming out, and the industry was not particularly affected by the crash in the United States. On the contrary, the Japanese gaming scene was actually going to revive the American one in a matter of just a couple years.

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<sup>7</sup> The original Activision name was restored in December 1992 after the company was bought and completely restructured by a group of investors led by Robert Kotick.