MARKET OVERVIEW

The world of video games took great strides during 2007. Nick Parker provides an insider's view.

The interactive gaming industry is entering the most dynamic growth period in its history. It is one of the few media sectors still increasing sales and the industry is undergoing rapid consolidation. With all three new generation consoles now launched and online gaming starting to capture the imagination of the masses, this market has finally achieved acceptability as a mainstream medium.

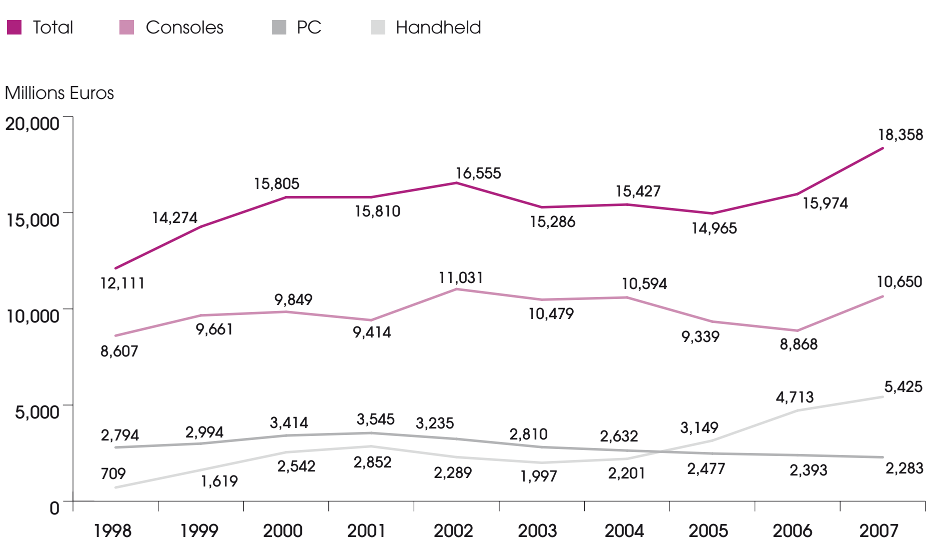
GAMES SOFTWARE, THE INDUSTRY POWERHOUSE

The market for games software is the most important measure of the total games market, as it is the largest product group and demonstrates the desire for gaming the most clearly. In 2007, its worldwide value grew by over 15 per cent, to reach annual sales of €18.4 billion. This compares to a flat compound annual growth rate (CAGR) between 2000 and 2006.

The primary drivers were: the DS Lite hand-held device and the Wii console, both from Nintendo; the Microsoft Xbox 360 – after a slow start to the year; and the most recent arrival, the Sony PlayStation 3 (PS3), which launched in Europe in March 2007 – though elsewhere at the end of 2006.

The Sony PS2, now seven years old, generated software sales of €3.6 billion of the global total software market value. This equates to 20 per cent of the market, putting it in second place behind the Nintendo DS Lite due to its significant hardware installed base.

TABLE ONE: **GLOBAL SOFTWARE VALUE MARKET SIZE**



Source: Screen Digest

NICK PARKER CONSULTANT

Nick Parker is the founder and CEO of Parker Consulting Ltd, the foremost specialist games strategic business consultancy in Europe.

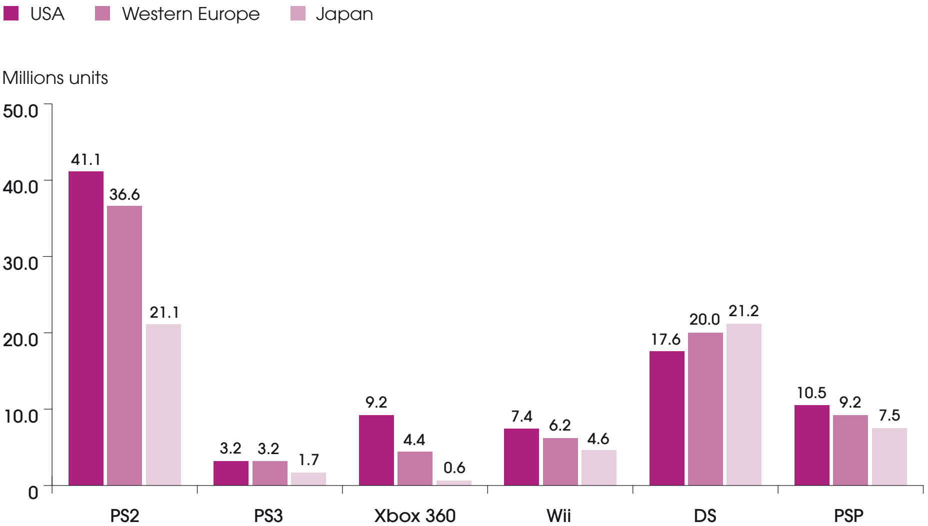
Not forgetting the pc software performance, the bread and butter of the market which keeps many publishers afloat during transition periods with consoles, which generated €2.3 billion (12 per cent of total software sales). PC was a top four best-performing platform in value terms and generated a considerable volume of software, a growing share of which was for massive multiplayer games (MMOGS).

GLOBAL TRENDS

The chart below demonstrates the potential sales which consoles can achieve, with the PS2 selling over 100 million units on a global basis. It is unlikely that any one console out of the three newer releases – PS3, Xbox 360 and Wii – will reach that figure. Why? Because, in this generation, each device is competing against the other and 'household saturation point' is a factor. But the three together are sure to create a combined market greater than those of previous generations.

Simple, casual online games – such as Bejeweled or Tetris and MMOGs like World of Warcraft – are the dominant gaming experience in most of the Far East but account for less than 10 per cent of gaming revenues in the West. However, these internet-driven games are growing significantly, introducing new payment models and attracting a less hardcore market.

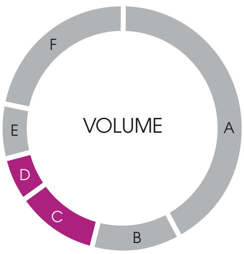
TABLE TWO: **LIFETIME HARDWARE SALES FOR THE YEAR ENDED DECEMBER 2007**



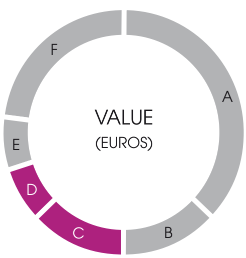
Source: Screen Digest

▶ MARKET OVERVIEW CONTINUED

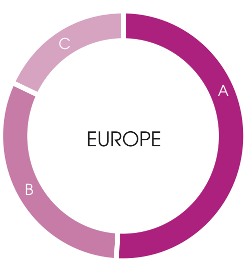
TABLE THREE:
SOFTWARE MARKET SHARES (2007)



A USA 42%
B Japan 12%
C United Kingdom 11%
D France 6%
E Germany 7%
F Other 22%



A USA 37%
B Japan 13%
C United Kingdom 13%
D France 7%
E Germany 7%
F Other 23%



A Consoles 51%
B Hand-held 31%
C PC 18%

Source: Screen Digest

EUROPEAN FOCUS

Western Europe is now the largest games market in the world, with software revenues of more than €7.5 billion in 2007. Within Europe, the UK leads and is the third strongest market on a global basis after the US and Japan.

Europe has the most evenly-divided share of platform sales in the world, as gaming on pcs remains a viable option. In 2007, pc sales of €1.4 billion accounted for 18 per cent of total European software sales, much higher than in the US or Japan.

It was also the first year when all three of the next generation consoles were available on the European market, following the PS3 launch at the end of March. Hand-held software, led by Nintendo, is on a par with Japan in terms of software revenues.

DIVERSE EUROPEAN MARKET CULTURES

The unusual aspects of gaming preferences in Europe are the difference in consumer cultures and retail structures across the continent. For example, in the UK, children behave in a more independent, irreverent way than children of the same age group in Germany, where parental influence is stronger and pc gaming is more popular.

These differences mean that local software genres and styles have to be respected and games which work well in one country are not necessarily successful in another. Indeed, some console devices, due to their gamer demographic, work better in some countries and not in others.

Take the Xbox 360, which appeals more to the adult male player and sells well in certain markets like the UK, Australia and the US. But the more casual, family markets in southern Europe present it with a challenge to gain market share. Nintendo has always performed well in France, for example, where the gamer demographic is more female, family-based and casual than in other parts of the world.

In general value terms, Germany, France, Spain and Italy are next in Europe after the UK, but they have different strengths. Germany is the biggest pc gaming market in Europe. Spain sells more Sony PSP hand-held devices than any other European market except the UK and France is second to the UK on all other consoles.

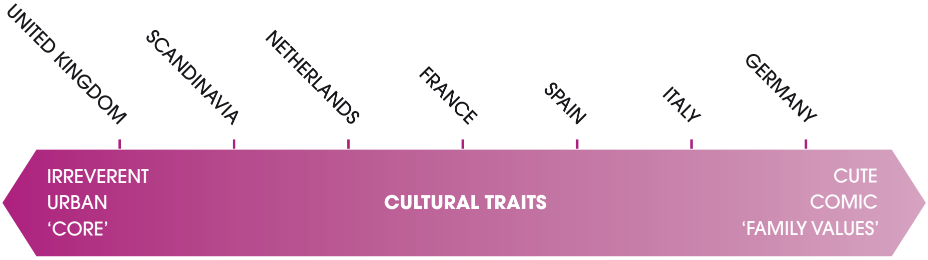
LOOKING AHEAD

Consolidation in the offline, traditional publishing sector will drive market share and margin expansion. Video games remain a scale-driven industry. Vendors must increase market share to boost margins, particularly in vibrant markets like MMOGs and casual gaming, and by acquiring key franchises and new intellectual property in traditional markets.

There are two outstanding deals – EA's bid for Take-Two and Vivendi's Activision deal – along with a host of potential buyout candidates such as SCi in the UK. Warner Brothers has started to invest in new gaming divisions to exploit the games market potential for its movie licences and Paramount Studios has just announced a similar strategy.

Future expansion of the industry will not be as dramatic as 2007, when the new consoles made such a significant impact. But the market will continue to grow to new, record levels in each of the next few years. In the first quarter of 2008, sales are already revealing a record performance for this time of the year. Games will sit side by side with other media on exciting portable devices and feature in leisure environments as the most fun, interactive form of entertainment. Finally, more mainstream media companies will enter the games market.

TABLE FOUR: **CULTURAL DIFFERENCES IN KEY EUROPEAN MARKETS**



Source: GameVision Europe/Game Group