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Xbox in Japan? Understanding the Distinctions of the Japanese Video Game Market to Increase Microsoft's Competitive Advantage

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XBOX IN JAPAN? UNDERSTANDING THE DISTINCTIONS OF THE JAPANESE VIDEO GAME
MARKET TO INCREASE MICROSOFT'S COMPETITIVE ADVANTAGE

By

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Abstract

As the video game industry has evolved into the world's largest entertainment markets, Microsoft, Nintendo, and Sony remain the biggest players in the video game console space. While all three companies have achieved worldwide success, Microsoft's performance with the Xbox brand in Japan is an outlier for its historically poor sales numbers dating back to its 2001 debut. Despite several efforts to tailor the Xbox to the Japanese market, Microsoft has never managed to launch a console that competed well against Nintendo or Sony. The purpose of this thesis is to unearth the various cultural distinctions inherent to the Japanese gaming industry that Microsoft must consider to gain a stronger foothold in the country, as well as diagnose the biggest issues facing Xbox with Japanese consumers. To accomplish this, the CAGE distance framework and Hofstede's cultural dimensions were used to assess the differences between the United States and Japan at the country level and the video game industry level. In addition, two interviews were conducted with professionals in the video game industry to gain additional insights into Microsoft's shortcomings in Japan. After compiling the information, it is evident that the magnitude of the differences between the U.S. and Japan on a cultural and economic level are vast enough to outweigh the commonalities they share as two of the largest world economies. The differences seen at the country level parallel those at the industry level. For example, the inherent differences between English and Japanese reinforce the difficulties of the video game localization process between languages. In addition, there is a gap between the uncertainty avoidance and long-term orientation scores of the U.S. and Japan run against Microsoft's general business strategy that is tailored more to short-term gains and high-risk endeavors. Finally, the interviews revealed more differences between the preferences of U.S. and Japanese consumers for the genre and design of video games. With this information, a handful of solutions were created to help Microsoft gain a competitive advantage in Japan, which includes tailoring the selection of games on Xbox Game Pass to target a Japanese audience and securing exclusivity deals with Japanese developers to attract new audiences. Even though Microsoft is not positioned to become a market leader in Japan due to the dominance of the Nintendo Switch, there is room for them to build a sizeable, reliable consumer base with Xbox Game Pass and exploit the differences between the U.S. and Japanese gaming industries.

Introduction

The video game industry dominates as one of the largest entertainment sectors in the world, currently projected to generate \$159.3 billion in revenue in 2020 in the midst of COVID- 19 (Wijman, 2020, p. 14). Mobile gaming has driven a large portion of the market's expansion within the last decade with the existence of the App Store and Google Play Store as platforms facilitating game distribution, and technological advancements broadens the scope of games that are playable on the go.

However, the foundation of the gaming industry continues to revolve around console gaming, constituting a \$45.2 billion share of the overall market (Wijman, 2020, p. 14). Within and outside the gaming sphere, Microsoft, Nintendo, and Sony are regarded as the three gaming giants due to their legacy of intense competition in the 2000s. But while this might hold true around the world, it has not translated to equal success for all three parties. In Japan, often considered the birthplace of home console video games, Microsoft historically struggles to establish a significant market presence against its Japanese-based rivals, despite early concerns that the "entry of Microsoft with Xbox may undermine the exclusive advantages on cultural proximity Japanese software publishers enjoyed over the last two decades" (Aoyama and Izushi, 2001, p. 442). According to the most recent aggregate of video game console sales in Japan, Microsoft's Xbox One S and Xbox One S have only sold a combined total of 110,000 units, compared to the 14.52 million and 9.20 million units of the Nintendo Switch and PlayStation 4 (PS4) families respectively.

While the obvious answer might be attributable to Nintendo and Sony's origins as Japanese video game companies, it does not explain how the Xbox brand failed to resonate with audiences, nor its subsequent decline with each console generation. Within the last five years, Microsoft has released Xbox Game Pass, a Netflix-like streaming service that hosts hundreds of games for a monthly fee. In addition, upcoming initiatives such as Project xCloud are geared towards increasing the accessibility of high-fidelity gaming to mobile technology. Microsoft and Sony also debuted their next-generation consoles during the 2020 holiday season, representing a fresh start for the former to officially recapture brand relevance and market share it lost during the last generation. Whether or not Microsoft's long-term strategy to increase the accessibility of video games to new audiences regardless of platform succeeds will be determined by its ability to translate its efforts to international markets, and Japan remains the most essential one ripe for expansion.

The purpose of this thesis is to uncover what cultural distinctions in the Japanese gaming industry must be considered for Microsoft to establish a competitive advantage over its rival companies with the Xbox brand. I intend to use a cross-cultural analysis of the United States (U.S.) and Japanese gaming industries utilizing well-respected frameworks and research methods to provide tangible solutions based on the conclusions drawn. As someone passionate about the collective success of the video game industry across each of its sectors, this thesis also serves as an opportunity to foster more interest in gaming as a medium for research in a business context.

I am confident that the scope of my thesis is manageable with the research available in the literature. While the scholarly work on video games is still young due to its recency, there is ample research material on industry-specific practices, cultural analysis, and international

strategy that I can use to support my research. In addition, gaming is a creative medium that introduces another qualitative dimension to my research (i.e., exclusive games, studio acquisitions, game development processes), which can also be used to assess Microsoft's position (or lack thereof) in the Japanese gaming industry.

Expected Outcome and Potential Significance

After the completion of this thesis, I believe it will contribute an applicable framework for other gaming companies to consider when creating and distributing games on an international scale. The amount of research specific to the gaming industry is still in a maturing phase, with a significant portion focused on the correlations between video games and real-world violence. An ever-growing niche exists to conduct research on the gaming industry from the discipline of international business, especially as video games become more accessible to audiences worldwide. I hope to contribute to the literature in a manner that encourages current and future generations to assess the business of video games with a more critical eye.

On a personal note, I also wanted to conduct thoughtful research within a medium I hold great passion for. I hope to work at a major gaming company in the future, and this thesis is a fantastic opportunity to showcase a deep understanding of the gaming industry, let alone the Xbox brand. Additionally, I hope it will open doors for me to pursue research opportunities in Japan on other areas of entertainment, such as Japanese animation.

Literature Review

Japan's Gaming History

The driving reason for the Japanese video game industry's persistence in reputation and global reach lies in its origins, of which it is attributed as the bedrock of gaming as an economic and social force. Put in the words of Blake J. Harris, the author of *Console Wars*: "Without the contributions of Japan, we wouldn't have a video game industry" (Prisco, 2017). While the first video games were developed in the West, with the first game believed to be *Tennis for Two* created by American physicist William Higinbotham in 1958, Japan's unique position in the creative and technical spaces fostered the conditions for gaming to prosper (2008). In several respects, Japan can be considered an early adopter of the medium that capitalized upon its potential.

Despite its origins as a *hanafunda* (Japanese playing card) company, Nintendo took a strong interest in swerving to consumer electronics. By collaborating with Sharp and Mitsubishi Electric, two of Japan's manufacturing powerhouses, Nintendo utilized the expertise of engineers to develop arcade games and original hardware, which culminated in the released of the Famicom in 1983 (Aoyama & Izushi, 2006, p. 1847).

Around this time, the U.S. video game industry was undergoing a severe economic crash. The lucrative potential of video games led multiple companies to cash in on the medium with video games on their own. This created an oversaturation of the market with a race to the bottom in terms of quality due to the lack of controls to ensure functionality and enjoyment, tarnishing consumer confidence in the medium. With Atari and Intellivision at the forefront of the U.S. gaming industry, these companies were slammed with abysmal sales and eroded revenues that brought the rest of its contemporaries down with it. Overall revenues of the video game industry

had stood around \$3.2 billion in 1982, but that number dropped to \$100 million by the end of 1985 (Caruso, 2009).

However, the impacts of the video game crash did not trickle outside U.S. borders. In fact, the Famicom managed to flourish in Japan after its 1983 release. In spite of a graphics chip issue at launch that led to a national recall of consoles, the Famicom managed to become the best-selling console in Japan at the time with over 2.5 million consoles sold by the end of 1984 (Goldberg, 2005). By the time Nintendo started looking towards an international release of the Famicom in the U.S., it had the foresight to address the lingering skepticism that remained from the video game crash.

In addition to rebranding the Famicom as the Nintendo Entertainment System (NES) for the Western markets, Nintendo implemented rigorous standards, such as game release quotas, to ensure that games released for the console met Nintendo's expectations. Emblematic of these policies was the Nintendo Seal of Quality that was meant to give consumers assurance (McFerran, 2019). When the NES launched in 1985, its immediate success completely overshadowed its competitors to establish itself as the market leader in video games. During its peak, Nintendo captured over ninety percent of the U.S. video game market, which persisted for a short time into the 1990s with the release of the Super Nintendo Entertainment System (SNES) in 1991 (Pham, 2003).

These years in Nintendo's history are an essential part of Japan's worldwide dominance in the video game space, particularly because it paved the way for other Japanese countries to establish themselves in international territories. The 1990s represented a vibrant era for gaming, whether it be the "console wars" between Nintendo and SEGA or Sony's debut of the PlayStation in 1994. In addition to Nintendo becoming a household name through successful releases in the

Super Mario and *The Legend of Zelda* series, third-party Japanese companies capitalized on the resurgence to create titles that captured domestic and worldwide acclaim, including *Final Fantasy VII* from Square Enix. As a result, the Japanese gaming industry became a stand-in for the global industry because it lacked viable competitors anywhere else.

Microsoft's Gaming History

As video games exploded in popularity, it was inevitable that the largest technology and entertainment companies were exploring options to incorporate the medium as part of their business model. Yet the fierce competition between Nintendo, SEGA, and Sony during the 1990s led to such market dominance and innovation as to make it extremely difficult for new entrants to gain traction. During this time, Microsoft was the most equipped to enter the gaming space given its enormous amount of capital. It also had a massive incentive too: former Microsoft CEO Steve Balmer expressed that Microsoft “needed to penetrate the living room” with home entertainment out of fear that Sony was overtaking the space with the PlayStation brand (Bass, 2021).

While Microsoft's strongest competencies lied with Windows, pressures from the gaming publishers prompted their engineers to create an original device with custom architecture that did not utilize Windows software, much to the dismay of Microsoft co-founder Bill Gates, but it ultimately received the blessing and support of the company to move ahead with production. (Bass, 2021). Because SEGA was losing market share in the game console space from a weak Dreamcast launch, Microsoft was eager to court support from some of the biggest Japanese gaming publishers, including Square Enix and Koei Tecmo, to bolster their games lineup. Microsoft also reached out to Nintendo with an interest in acquiring the company for software development, but nothing tangible came from the discussions. This resulted in Microsoft

redirecting their focus towards the acquisition of Bungie, a PC game developer responsible for creating the *Halo* franchise, and courting their games for timed exclusivity on Xbox (2000)

In January of 2001, Bill Gates officially unveiled Xbox at the Consumer Electronics Show (CES), and the console launched in U.S. stores in November of the same year (NeoGamer, 2020). The console had a tremendous launch, selling 1.5 million consoles through the end of 2001, driven by the enthusiasm around *Halo: Combat Evolved* as a launch title (Dyer, 2021). Establishing itself as a viable force in the video game console market, the Xbox continued to experience unprecedented success across its lifetime. Microsoft introduced Xbox Live, an online gaming service that enabled users to play games with others online and access downloadable content (DLC) that allowed older games to be updated with new content. And in 2004 Microsoft released *Halo 2*, which became the most successful entertainment launch in U.S. history with \$125 million in sales (2008).

As a result of the Xbox's success, Microsoft has debuted three more generations of consoles: the Xbox 360, the Xbox One, and the Xbox Series (X and S). The Xbox 360 is the most successful console from Microsoft, where it doubled down on online gaming as its competitive advantage to attract a hardcore audience. Since then, it remains one of the ten best-selling video game consoles in the world (Sinari, 2021). However, the Xbox One experienced middling success after its debut in 2013 and vastly underperformed against the PS4. To recapture relevance in the gaming industry, Microsoft took steps to bolster the breadth and depth of the Xbox brand, which included the acquisition of other gaming studios such as Obsidian Entertainment and ZeniMax Media. On January 18, 2022, Microsoft announced its intentions to purchase Activision Blizzard, the developer and publisher behind franchises like *Call of Duty* and *World of Warcraft*, in an all-cash deal valued at \$68.7 billion that will become the largest gaming

acquisition of all-time assuming it goes through (Mukherjee & Patnaik, 2022)

Xbox in Japan

Even tracing back to the successful global debut of the Xbox, Microsoft's lack of success in the Japanese market remains its most consistent sour spot. The original Xbox came out in Japan in February of 2002, a few months after its North American release. At the time, Microsoft Japan's Managing Director Hirohisa Ohura indicated that Japan was "the most challenging market for the Xbox" due to its need to compete against the Nintendo GameCube and PlayStation 2 (PS2), both created and manufactured by beloved Japanese gaming companies (Lu Stout, 2002). However, two other major issues were identified with the console's performance in Japan. First, the large size of the console was incongruous with the designs of Japanese households, which tended to smaller than homes in North America or Europe. Second, the console's games lineup skewed towards the preferences of Western players. One of the most persistent stereotypes in the industry is that "Japanese gamers like role-playing games (RPGs), and Western gamers prefer first-person shooters (FPS)", and Microsoft's massive marketing push with *Halo 2* further entrenched consumer preferences (Ashcraft, 2012).

Because Japan remained one of the top gaming markets in the world, Microsoft took its shortcomings in the country to heart during the development of its next-generation console: the Xbox 360. Peter Moore, a former Xbox marketing executive, recounted how the design team travelled frequently to Japan to workshop designs and test their appeal with Japanese gamers (Hayes, 2010, p. 13). Microsoft also made stronger attempts to secure Japanese titles such as *Final Fantasy XIII* and *Tales of Vesperia*, the latter a timed exclusive. When the Xbox launched during the 2005 holiday season, it cost 39,795 yen (about \$330 at the time), which was cheaper

than the \$399 launch in North America (2005)

This combination of factors helped Microsoft achieve higher success in Japan than the original Xbox, with numbers speculated to be around 1.65 million units sold by 2013 (Fleming, 2013). However, this number still pales in comparison to its Japanese rivals; the PlayStation 3 Nintendo Wii sold around 9.50 million 12.75 million consoles despite both releasing one year after the Xbox 360 (Fleming, 2013). As of writing, the Xbox 360 is the best-selling Xbox console in Japan.

Microsoft's next console, the Xbox One, performed abysmally in the Japanese market. The console had already underperformed globally, and it was mired in controversy prior to launch due to anger surrounding the console's "always-online" policy and forced bundling of the Xbox Kinect (Microsoft reversed course on both decisions). However, the International Data Corporation reports that only 0.3 percent of Xbox One consoles were sold in Japan. (Haigh, 2019). There are no official sales numbers for the Xbox One, but the current estimates lie around 50.19 million consoles sold across its lifetime, meaning the console failed to sell more than 200,000 units in Japan (D'Angelo, 2021).

The Xbox Series X and Xbox Series S, Microsoft's newest consoles, debuted worldwide in 2020. Despite its tumultuous history in Japan, the company expresses affirmation that the Japanese gaming market remains important for Xbox. Phil Spencer, the head of the Xbox brand, stated in an interview that Xbox's position in Japan "isn't acceptable to [him]," elaborating that he wants to ensure that it becomes easier for Japanese players to engage with the Xbox brand with services like Xbox Game Pass (Robinson, 2020).

Main Insights

When considering the histories of the Xbox brand and the Japanese video game industry in isolation, both are influential stories that shaped the business and creative trajectories of video games forever, pioneers of innovation in their own respects. Yet when considering them together, the incompatibilities of the two paint a different picture. Microsoft never managed to get off the ground running in Japan because the console did not address the preferences of Japanese consumers. The dominance of Nintendo and Sony in their home country inherently puts Microsoft in an underdog position that requires greater efforts to overcome. And because Japan is intrinsic to the historical success of video games, Microsoft is committed to leaving its footprint in the market. Research about the business of video games is in its early stages. Moreover, there is a small body of literature that assesses the success (or lack thereof) of video game companies on an international scale. This research intends to address the Xbox's shortcomings in the Japanese gaming market using a methodological approach that unveils how Microsoft can leverage its existing strengths while adapting to the needs of Japanese players.

Methodology & Approach

In order to fulfill the goals of this thesis, there are two areas that I intend to focus on:

1) the cultural differences between the U.S. and Japanese gaming industries and 2)

Microsoft's gaming initiatives in context of these differences and its competitors.

For the first part, I intend to reference two cultural tools to map out the characteristics that distinguish the U.S. and Japan from one another: Pankaj Ghemawat's CAGE distance framework and Geert Hofstede's cultural dimensions. The CAGE distance framework is useful for highlighting the differences that arise between places at the country and industry levels

according to their “distances” on four metrics: cultural, administrative, geographic, and economic. This model accommodates my research because it can be used to showcase the distinguishing factors between the United States and Japan as well as their respective gaming industries.

Geert Hofstede's cultural dimensions are rooted within management theories meant to help comprehend the tenets of businesses and organizations but is popularly used to quantify cultural values on a country-per-country basis to aid international negotiation and communication. There are six dimensions to consider: 1) power distance, 2) individualism vs. collectivism, 3) masculinity vs. femininity, 4) uncertainty avoidance, 5) long-term vs. short term orientation, and 6) indulgence vs. restraint (Hofstede Insights, 2021). Each one implies specific characteristics of culture depending on how a country scores. While these values do not hold constant for every individual of a given country, it gives an overview that facilitates the navigation of different cultures. Hofstede's cultural dimensions will be used as a supplement to the CAGE distance framework to provide additional explanation for differences between the U.S. and Japan.

It is essential to cross-reference multiple tools with each other to simultaneously draw the most relevant insights while accommodating for their shortcomings. For example, the CAGE distance framework's purpose is to highlight the importance of considering the differences between countries alongside the similarities, but its application is not ideal for assessing specifics. Meanwhile Hofstede's cultural dimensions are helpful in extrapolating the cultural values of a given country in a business context but are limited when applied on an individual basis. Together, the CAGE distance framework and Hofstede's cultural dimensions can address the limitations of each other while garnering a clearer picture of the U.S. and Japan

gaming industries and their intersections with culture.

The CAGE distance framework will be used to compare the U.S. and Japan at the country level, as well as the U.S. and Japanese video game markets at the industry level. The purpose of doing both the country-level and industry-level analysis is to ensure that as much relevant information is compiled to understand both the differences between the video game industries that is relevant for Microsoft, but also situates it within the context of both countries. It will also provide strong reference material that holds practical use for assessing the distinctions between the Western-based corporate culture of Microsoft against those present within Japanese gaming companies. This also fosters a foundation for which practical results can be composed for successfully revitalizing the Xbox brand amongst Japanese consumers. To gather additional information,

I will conduct multiple interviews with video game industry professionals. The individuals that will be interviewed for this research have experience navigating the American and Japanese gaming markets, and they will be able to introduce relevant insights that are not accounted for in the current literature. A survey was considered to gauge the video game preferences of Japanese consumers and compliment the qualitative research. However, the availability of reliable consumer data and the difficulties administering a survey outside the United States made it unfeasible, and it is a limitation that future research hopes to overcome.

In the discussion section, actionable solutions will be created that are aimed at exploring the avenues by which Microsoft can revitalize the Xbox brand in Japan from its current position based on the research compiled from the cultural tools and the interviews.

CAGE Distance Framework Analysis

The CAGE Distance Framework was used to compare the U.S. and Japan at the country level, as well as the U.S. and Japanese gaming markets at the industry level. As a reference, Figure 1 and Figure 2 show a comprehensive chart that breaks down the major differences at the country and industry levels across cultural, administrative, geographic, and economic lines. This section will begin with the country analysis to provide the foundation for looking at the video game industries in both countries with sufficient context.

Country-Level Analysis

The most visible cultural difference between the U.S. and Japan lies with the language barrier. English and Japanese are the official languages respectively, and both feature qualities that foster different communication styles and cultural values. The Foreign Language Institute also classifies Japanese as a Category IV language, indicating that it is one of the most difficult languages for English speakers to learn alongside Arabic and Chinese (2022). While the sentence structure and writing system pose challenges, the subtler qualities of communication also contribute significantly to the distance between the languages. The existence of *keigo*, a Japanese honorific system that roughly translates to “respectful language”, accentuates the importance of hierarchy when addressing other people based on factors such as age, professional status, and familial relationship. Non-verbal cues also play a larger role in day-to-day Japanese communication to better understand one’s true message or intentions, since the Japanese language reflects a preference for implicit communication compared to the preference for explicit communication in the U.S. Japan’s cultural and ethnic homogeneity simultaneously allows for indirect communication to flourish in day-to-day interactions and traditional social values akin to maintaining order and valuing hierarchical

differences to persist.

Two of the qualities that Ghemawat notes as having the greatest impact on international trade lie with colonial ties and common currency, both of which the U.S. and Japan lack (Ghemawat, 2015 p. 1). The closest thing to a colony-colonizer relationship was the U.S. military occupation of Japan upon the conclusion of World War II, which set the precedent for a new political relationship between both countries. Currently, Japan is the U.S.'s fourth-largest trading partner, accounting for 4.5 percent of U.S. international trading activity, and remains one of the strongest world alliances despite their physical distance (2022). Both countries do not share a trading bloc, but both maintain the U.S.-Japan Trade Agreement and the U.S.-Japan Digital Trade Agreement to further reduce the economic barriers for agricultural exports and strengthen the processes for exchanging digital technologies and information (2022). Their presence as two of the largest free market economies in the world also encourage the maintenance of a robust global partnership on various grounds.

Briefly mentioned earlier, the U.S. and Japan are geographically far from each other in terms of physical distance, but there remain other differences that separate them. One of the most extreme differences lies with the time zones, which can range from thirteen to nineteen hours depending on one's location within the U.S. This creates an obstacle for timely cross-cultural communication due to the reduced timeframes where the working hours of American and Japanese individuals overlap. Japan's isolation from the rest of the world as an island nation bring difficulties from a logistical standpoint when needing to export or import products or resources, as it shares no land borders.

Geographic differences also reinforces other cultural and economic differences

between the U.S. and Japan. Figure 3 shows a comparison of the U.S. and Japan based on Hofstede's cultural dimensions, and it highlights a major difference on the metrics of uncertainty avoidance and long-term orientation. One of the common sources noted for such high scores for Japan is the persistent threat of natural disasters in the form of tsunamis, earthquakes, and volcanic eruptions that could bring devastating consequences for the entire country. There is a seventy percent chance that an earthquake with a magnitude-7 rating or higher will strike Tokyo in the next thirty years, and Japan has taken numerous steps to further develop a robust infrastructure that anticipates the worst-case scenario, such as building towers that resist sway (2021). While the U.S. has a wider range of geographic concerns that are region-specific, its lowered severity relative to Japan means it plays a smaller role in informing economic policy.

The U.S. and Japan are the first and third largest world economies respectively, but digging into the overall economic picture unveils a distinct palate of challenges. For example, the inflation trajectories of both countries run in opposite directions. The U.S. is grappling with major inflation concerns after consumer prices posted the highest annual increase (7.9 percent) in forty years, which does not reflect the inflationary consequences of the Russia-Ukraine conflict at the time of writing. (2022). Japan is experiencing the opposite problem. After a period of economic collapse between 1991 and 2001 termed Japan's "Lost Decade", the country has struggled with persistent deflation that is resulting in stagnant wages and lower rates of corporate investment for two decades (Fujikawa, 2021). This translates to higher prices for goods and services in the U.S. compared to Japan, but it also lends itself to a more favorable exchange rate for the dollar against the yen. Also aligned with Japan's deflation trend is the "greying" workforce as the country undergoes a steady population

decline due to the birth rate not exceeding the replacement rate. As Japan's population distribution skews older, more economic burdens will be placed upon the working and younger generations. The U.S. is also projected to experience a population decline over the next few years, but it still posted a 7.4 percent growth rate between 2010 and 2020 (Frey, 2022).

Industry-Level Analysis

When applying the CAGE distance framework to the video game industries of the U.S. and Japan, the differences assessed across the four dimensions on a country basis manifest in more nuanced ways. It holds especially true on a cultural level since video games are an audiovisual medium that Ghemawat would label as one with "high linguistic content", where he believes differences are most prominent. Just as learning Japanese as an English speaker (and vice versa) is a challenging endeavor, the localization process from English-to-Japanese or Japanese-to-English is arguably tougher. In the context of game development, localization is the process for bringing a game to a foreign market through activities such as translating in-game text or hiring new voice actors. It is not uncommon for game content to be altered to meet local requirements. For example, a handful of games in Australia are not approved for purchase each year because they prominently feature alcohol or drug content. The structural and cultural differences inherent to English and Japanese are most commonly found when translating dialogue and text. Since both languages feature phrases, words, and cues that are not directly translatable to other languages, responsibility is placed on the translation team to adopt the source material as accurately as possible while maintaining the original intent. And with a significant time zone difference in the mix, additional consideration is needed for coordinating schedules and meetings that accommodate the working schedules of employees

in the U.S. and Japan, with a stronger possibility for delayed communication.

Amongst the three biggest console hardware manufacturers (Microsoft, Nintendo, and Sony), Nintendo and Sony both originate from Japan as the dominant competitors. Both companies used to compete in the home console and handheld spaces dating back to 1994, but Nintendo's consolidation of its gaming console divisions with the Nintendo Switch and the discontinuation of the PlayStation Vita in 2019 led to the investment of their resources in one platform. As a result, Microsoft is the only non-Japanese console manufacturer of the three.

One can also observe major differences on the consumer level. Some video games genres are heavily associated with one country: Japanese role-playing games (JRPGs) emerged as its own subcategory to accentuate its unique features against other role-playing games (RPGs), including the use of an *anime* art style or a greater emphasis on slower, detailed storytelling techniques (i.e., *Dragon Quest*, *Final Fantasy*, *Persona*). These games, alongside others in the RPG space, constitute the most-played genre amongst Japanese gamers, where they were twice as likely to have played an RPG in a six-month timespan as their global counterparts (Kuzuhara, 2021). Along those lines, U.S. video game players demonstrate a stronger preference for games in the shooting and sports genres, with titles in the *Call of Duty* and *Madden NFL* franchises consistently topping sales charts (Grubb, 2022).

The Japanese gaming market is also driven more by the mobile gaming sector relative to the rest of the world. It is the largest source of video game revenue in Japan, and it accounts for twenty-two percent of all global mobile gaming revenue (Chapple, 2020). While higher smartphone adoption rates from country-to-country also position mobile gaming as a lucrative segment in the video game industry, its dominance in Japan is also attributable to its unique gaming landscape. Japanese homes tend to be smaller than U.S. homes, necessitating the

existence of “Internet cafes” as an outlet for console and PC gaming enthusiasts. In addition, Japanese citizens rely heavily upon public transportation whereas U.S. citizens commute by car more often. The free time opened up from public transit provided the perfect conduit for smartphone games to flourish as a means to fill the time.

To ensure that video games are assigned a proper rating to reach the most appropriate audiences, the U.S. and Japan depend upon independent rating boards. In the U.S., the Entertainment Software Rating Board (ESRB) is a self-regulating organization affiliated with the Entertainment Software Association, and the Computer Entertainment Rating Organization (CERO) fulfills the same purpose as a non-profit organization in Japan. From an administrative standpoint, the major difference between the rating boards is concentrated with its stricter ratings. If a game receives a “Mature” rating from the ESRB, it indicates the content is suitable for individuals aged seventeen or older and requires an ID to purchase it. On the basis of age, the “CERO D” rating is the closest equivalent, but it does not require an ID for purchase. The “CERO Z” better serves that purpose, banning the sale of games with this rating to those under the age of 18, but the additional threshold means that a smaller proportion of titles are inaccessible for purchase compared to the U.S. (2022).

Microsoft's acquisition of Activision Blizzard is representative of the increasing consolidation amongst U.S. entertainment companies over the past decade, but this trend does not translate as accurately to Japanese business culture. One element that shields Japanese companies from foreign mergers and acquisitions lies in the form of a popular business partnership. Keiretsu, which roughly translates to “system” or “group”, refers to a network of businesses who are intertwined through relationships and shareholdings that are represented by a central bank (Twomey, 2022). A distinguishing characteristic of Japan's corporate

governance policy, companies within a keiretsu foster harmony amongst affiliate companies and protect themselves from potential takeovers due to the complicated nature of the social and financial networks. The reduced risk associated with becoming part of a keiretsu is also a reflection of Japan's high uncertainty avoidance. Within the U.S., keiretsu would be frowned upon based on antitrust law since the business groupings represent a potential threat to competition, and its practice amongst American companies could undermine the role of the stock exchange.

Due to the sheer size of the U.S. gaming market, there is more incentive for Japanese gaming companies to establish local subsidiaries rather than vice versa. While Square Enix concentrates most of its game development in Tokyo, for example, it also has an American subsidiary that oversees the North American publication of games and assists in game development at its U.S. studios such as Crystal Dynamics, best known for their work on the Tomb Raider reboot. The international reach of video games also extends to game development: outsourcing various parts of a project is an increasingly common practice to reduce development costs and expedite game development. On geographic terms, the U.S. has the easiest access to Canada and Western European countries for such purposes, whereas Japan has the easiest access to East Asian countries.

The U.S. and Japan occupy the second and third spots when assessing the valuation of their domestic gaming industries around the world, but it is separated by about \$18.4 billion (2022). Although both markets generate billions for their economies, the Japanese economy is more intertwined with entertainment. In order to leverage Japan's modern pop culture to drive economic growth, the Japanese government directed the Ministry of Economy, Trade, and Industry (METI) to establish the "Cool Japan Initiative" under the Creative Industries

Promotion Office in 2010 (2012). The U.S. does not currently have similar strategy that aligns its pop culture with its economic outlook, signaling that Japan views its entertainment properties as an essential medium for creating soft power and expanding its market. The initiative is more pertinent for video games in recent years as Japan also faces stiffer competition from China as an easy target for acquiring Japanese talent and drawing inspiration from Japanese developers to create its own popular games such as *Genshin Impact* (Dooley & Mozur, 2022).

Interview Insights

To gather additional information about the nuances of Xbox's situation in Japan, I interviewed two individuals with extensive experience in the video game industry. The first person is Dr. Serkan Toto, the CEO and founder of Tokyo-based independent video game consulting firm Kantan Games. His work and coverage focus on the Japanese video game industry, and he is often tapped for commentary by international media outlets. Appendix A includes a transcript of Toto's interview. The second person is Nathan Brown, a freelance video game consultant and writer, and the former editor of UK video game magazine *Edge*. He currently runs *Hit Points*, a newsletter providing commentary on the video game industry. Appendix B includes a transcript of Brown's interview.

When asked to give an assessment on Xbox's overall performance in Japan, Toto described it as a "struggle" for Microsoft because of their lackluster performance in one of the biggest gaming markets and most populous countries in the world (See Appendix A). Even though the Xbox brand never took off in the manner that Microsoft hoped, their persistence is attributable to their overall profitability. At its core, Microsoft is a services company that generates most of its revenues from Microsoft Office Suite software and subscriptions. This

allows the company to invest resources towards its Xbox initiatives in Japan despite its lackluster performance. Brown built upon this idea by noting that Game Pass is likely to experience success during this console generation “in the context of itself”, meaning that it would not pose a major threat to Nintendo or Sony in their home market (See Appendix B).

Toto noted that there two fundamental differences between the U.S. and Japanese gaming industries, one concerning the supply side and the other concerning the demand side (See Appendix A). On the supply side, there is fierce competition between the publicly traded companies in Japan, inclusive of Nintendo and Sony, which are quite large in scale. However, the U.S. features a “much richer ecosystem on the supply side” of gaming because there is a larger proportion of video game companies that deviate from the norm (See Appendix A). There are a number of independent (indie) game developers scattered across the U.S., and the indie gaming scene in the U.S. remains vibrant. Some of the most popular games of the last decade came from smaller American creators, including *Rocket League*, *Stardew Valley*, and *Undertale*.

On the demand side, Toto believed the biggest difference lied in the different tastes of American and Japanese players based on gameplay and design (See Appendix A). This aligns with previous research asserting the dominance of RPGs in Japan, as well as shooting and sports games in the U.S. Brown introduces another perspective that focuses on the general priorities of game developers, with Western studios striving towards realism in games and Japanese studios striving towards fantasy (See Appendix B). He summed up this point by asserting that based on previous trends, “American users play Japanese games, but Japanese users don’t play American games” (See Appendix A). The historic success of the Nintendo Switch from a hardware and software perspective in Japan underlies this statement; Nintendo

accounted for eighty-seven percent of all video game hardware sales and half of all video game software sales in Japan in 2020 (Dring, 2021). Brown further underscores with the notion that portability is a driving factor behind the success of most handheld consoles in the country (See Appendix B).

One of the questions centered around Microsoft's acquisition strategy to bolster its gaming catalog against its competitors, and whether it was feasible to acquire a Japanese gaming company. Here, Toto acknowledged the homefield advantage Nintendo and Sony hold compared to Microsoft because there is a lower barrier to entry in initiating business discussions between two Japanese companies, but was also explicit in citing it as the key element for Xbox's lagging performance in the Japanese market (See Appendix A). Instead, he traces back to the launch of the original Xbox in Japan as the source of the brand's current woes because the initial batch of consoles had issues with hardware quality (See Appendix A). A common issue with the original Xbox arose when a flashing red and green light appeared around the power button, meaning that there was a system failure. And when Microsoft launched the Xbox 360, it reemerged in the form of the infamous "Red Ring of Death" that indicated the need for service repair. Microsoft was already caught in a difficult position attempting to enter as a third major competitor in the video game console market in 2001, but hardware shortcomings tarnished Xbox's reputation in the long-term.

Brown offered the argument that Microsoft does not need to purchase a Japanese gaming studio, and that such a move "could be counterproductive in a way" in light of concerns about the consolidation of game studios in the hands of a few major players and that it would not translate to more Japanese players transitioning to Xbox (See Appendix B). His commentary touched upon the idea of brand loyalty in video games, which is most prevalent

when someone sticks to a certain brand of video game consoles. One of the driving forces behind consumers sticking with Microsoft, Nintendo, or Sony consoles lies with the exclusive games available on each platform. Since there is a deficiency of Japanese video games on the Microsoft platform, one acquisition might not be enough to draw people who enjoy those games from its competitors.

An optimistic note during the interview accompanied the discussion around Xbox Game Pass. The value proposition of Xbox Game Pass for Japanese customers is even more compelling than its U.S. counterparts because the average game cost in Japan can trend upwards of eight thousand yen, or eighty dollars in nominal terms (See Appendix A). The average game cost for a new video game in the U.S. is \$59.99, although many of Sony's first-party games (i.e., *God of War: Ragnarök*, *Horizon Forbidden West*) retail for \$69.99. This difference is intensified with the context that Japan is currently in a deflationary bubble, as well as the notion that discounting is a less common pricing tactic for Japanese products and services (See Appendix A).

Since Microsoft has competed in the Japanese video game space for over two decades, Toto believes that Microsoft requires a "big solution" that amounts to more than the smaller steps they have taken thus far because Nintendo and Sony are (and have been) are dominating the Japanese gaming market. (See Appendix A). While Microsoft can take strides to improve Xbox Game Pass or secure Japanese titles for exclusive distribution on Xbox devices, a big step equates more to an acquisition of a Japanese gaming company or a brand-new initiative that focuses on gaining market share. Building upon that, Brown touches upon an important initiative that Microsoft seems to be moving towards: "untethering" the Xbox brand from hardware to become accessible in as many formats as possible (See Appendix B).

Discussion

When viewing countries in terms of their economic power, it might indicate that the U.S. and Japan share more common ground as two of the most developed nations in the world. Across the various dimensions of CAGE, however, the sum of their differences is placed at the forefront. One of the most apparent areas of divergence lies with the processes for communication. Much of Edward T. Hall's seminal work in cross-cultural research discusses the differences between high-context and low-context cultures, with high-context cultures like Japan's featuring groups of people that "have extensive information networks... and who are involved in close personal relationships" (Hall, 1990). This runs against the conventions of the U.S., which is classified as a low-context culture for its reliance on explicit social conventions.

Yet the difference runs much deeper than the amount of information shared, and it reinforces the cultural nuances that separate the two countries in various circumstances, including business. When assessing the CAGE distance framework, one can see that many of the differences at the industry level reflect those noted at the country level. As noted, the localization process for translating video games from English to Japanese or vice versa stems from the more general difficulties associated with translating between each language. This also extends to the geographic separation between the U.S. and Japan, which consequently forces game developers and publishers to remain conscious of time zone differences when conducting cross-border communication.

On a broader scale, each dimension of the CAGE distance framework correlates with specific elements of the U.S. and Japanese video game industries. The cultural differences between the two countries translate to different tastes and preferences for video games amongst the populations, with Toto reaffirming the deep associations of RPGs and FPS games with Japan

and the U.S. respectively (See Appendix A). Administratively, the laws and regulations of one country not only impact the ease of access to certain video games based on their content, but also the extent to which companies like Microsoft can pursue growth in the Japanese market when its rules differ from the ones it is accustomed to. Because Japan is located west of the U.S., American gaming companies with Japanese ties tend to base their operations on the West Coast to ease travel and communication to Japan, just as many Japanese gaming companies establish subsidiaries in the same location with similar intentions. It is also no small coincidence that the three largest gaming markets lie with the U.S., Japan, and China.

When Hofstede's cultural dimensions are factored into the equation, some of Microsoft's key disadvantages as a competitor in the Japanese gaming market come to the forefront. Two of the most glaring differences between the U.S. and Japan can be seen with their scores on long-term orientation and uncertainty avoidance. The U.S. and Japan received long-term orientation scores of 26 and 88 respectively, and they received uncertainty avoidance scores of 46 and 92 respectively (Hofstede Insights, 2021). Considered alongside each other, Japan's high scores indicate that Japanese businesses tend to behave in a manner that minimizes risk and prioritizes sustainable growth, placing a more equal balance on stakeholders over stockholders. For Japanese gaming companies, behavior reflecting this can include participating in a *keiretsu* partnership or depending on past success to guide future business decisions.

From this standpoint, Microsoft's general strategy with the Xbox brand runs counter to the conventions of Japanese business. Besides the legal difficulties associated with acquiring a Japanese company from outside the country, Microsoft is reflective of the opposite priorities associated with U.S. companies, placing more emphasis on short-term needs and innovation to drive their growth to new heights. For example, Microsoft has never turned a profit on an Xbox

console before and depends on game sales and subscription revenues to recuperates the costs (Kent, 2021). On the other hand, Nintendo made it a priority to not sell the Nintendo Switch at a loss from the moment it launched to turn a profit from the beginning, while also pricing it in line with consumer expectations (Grubb, 2016).

What the CAGE distance framework and the interviews ultimately demonstrate together is that the scale of the differences between the U.S. and Japan across multiple dimensions informs how the video game industries of both countries developed with unique characteristics that requires gaming companies to consider how to tailor their products and services to the local market. The clear dichotomy between Microsoft's success in Western markets against the Japanese markets demonstrates room to improve Xbox's performance. Even during the eighth generation of video game consoles, where the Xbox One sold woefully against the PS4, it is estimated that the console sold just over fifty million consoles, but Xbox One sales in Japan constituted less than two hundred thousand of total sales (Alsop, 2022). With its Japanese contemporaries finding consistent global success across the board, Microsoft can leverage the cultural distinctions of the Japanese video game industry to lay the roadmap to fulfill its potential in Japan

Potential Solutions

The goal of this research was to diagnose Xbox's performance in the Japanese gaming market across its history, while identifying solutions that consider Microsoft's competitive advantages and disadvantages in the context of the nuances inherent to Japan as an economic and gaming leader. After gathering information from the U.S.-Japan cross-cultural analysis and the interviews with leading experts in the video game industry, five solutions were created to provides avenues for which Microsoft can grow its presence in Japan.

Tailor Game Pass to Japanese Preferences

Xbox Game Pass is the driving force behind the current momentum in the Japanese market due to its large catalog of games at an affordable price point. Even though it lags behind Nintendo and Sony in hardware and software sales, the relative performance of Xbox Series X and Xbox Series S compared to previous Xbox consoles is promising. Since the average Japanese gamer is geared towards RPGs, appealing to this preference can focus Microsoft's efforts on the games it needs to include on Game Pass. *Dragon Quest XI S: Echoes of an Elusive Age* and *Yakuza: Like a Dragon* are two of the headlining JRPGs on Xbox Game Pass, and there are opportunities to expand the catalog to demonstrate Microsoft's commitment outside of the biggest, newest releases. For example, there is a gap in legacy content that Game Pass stands to benefit from through the inclusion of older titles. *Blue Dragon* and *Lost Odyssey* were two Xbox 360 exclusive JRPGs published by Microsoft Game Studios (now Xbox Game Studios) that are currently unavailable on Xbox Game Pass. A precedent has also been set with entries in popular JRPG franchises (i.e., *Final Fantasy*, *Tales*) appearing on the service, leaving the door open for additional titles to be added in the future.

Forge Relationships with Biggest Japanese Publishers

Microsoft has the financial capital to acquire one of the large Japanese gaming companies, but its status as an American company places it in a disadvantageous position against Sony, which was founded in Japan, and those same companies are also potential acquisition targets for bolstering the PlayStation brand. However, that does not prevent Microsoft from establishing long-term partnerships. Last November, Microsoft and SEGA announced a strategic alliance that "produce large-scale, global games in a next-generation development environment built on Microsoft's Azure cloud platform" (2021). The fruits of this effort will not be clear until

future SEGA titles are released, but it represents a major step towards engaging with the Japanese game development scene through means that leverage other elements of Microsoft's business. Such ventures also create the ideal conditions to jumpstart conversations about other elements of their relationship. In Microsoft's case, this could extend to securing a publisher's title for release on Xbox platforms or funding development of next-generation games. This approach also subverts some of the complications of navigating Japanese business law to bring a large game publisher under its roof.

Secure Exclusivity Deals with Big Japanese Games

Whereas Microsoft aims to integrate new studios under Xbox Game Studios, Sony favors locking in exclusive deals for major third-party games, especially Japanese ones, with *Final Fantasy VII Remake* and *Guilty Gear: Strive* headlining the slate of games with PlayStation console exclusivity. Even *Ghostwire Tokyo*, a game developed by Microsoft-owned Tango Gameworks, has one-year timed exclusivity on PlayStation 5 until March of 2023 (Kiya, 2022). Because high-quality games are the driving force behind the success (or lack thereof) of a video game console, Microsoft has room to spend its capital smarter by taking greater advantage of console exclusivity for third-party games. To maximize Game Pass engagement, it is wise for Microsoft to target games that will encourage Japanese consumers to gravitate towards the service. This distinguishes it from the previous recommendations because it offers Microsoft a chance to strengthen its value proposition against its competitors.

Pursue Organic Growth from Within

Through the acquisition of ZeniMax Media, Microsoft finally acquired a reputable Japanese video game developer in Tango Gameworks, headquartered in Tokyo. Starting with *The Evil Within*, the studio has published three console games over eight years. Since Tango

Gameworks represents Microsoft's only major footprint in Japanese game development, it should direct large investment efforts towards the studio to assist in game development and expand their talent pool to foster better conditions for releasing a steady pipeline of high-quality Japanese games. Most of Microsoft's strategy with the Xbox brand is centered around inorganic growth, which depends on mergers and acquisitions to achieve greater economic benefit. While it expands Microsoft's gaming footprint quickly, it poses its own challenges in regard to integrating new studios under a new management structure. To balance out its recent activity, Microsoft should pinpoint areas to slowly grow Tango Gameworks into a bigger presence or establish new studios in Japan from the personnel already developing games under Xbox Game Studios.

Acquire a Smaller Japanese Game Developer

If Microsoft can navigate Japanese business culture well enough to position itself to acquire a Japanese video game company, an ideal scenario has the company focusing on bringing in a smaller Japanese game developer rather than a larger one. There are two reasons for this: 1) assuming the successful acquisition of Activision Blizzard in 2023, Microsoft will have its hands full integrating one of the largest gaming companies in the world and tackling its promises to address the concerns about Activision Blizzard's company culture, and 2) it allows Microsoft to test the waters with a smaller investment and avoid the risks associated with a larger acquisition. While a large portion of the competition in the Japanese gaming industry is concentrated with publicly traded companies, there are a handful of smaller studios that are strong candidates for acquisition. One of them is PlatinumGames, a private Osaka-based studio that is well-known for action games such as *Bayonetta* and *Nier: Automata*. Microsoft and PlatinumGames once partnered for development on *Scalebound*, an action RPG intended to

come out for Xbox One, but it was cancelled in 2017 due to development troubles. Since then, several executives from PlatinumGames have expressed willingness in jumpstarting conversations with Microsoft again, as well as an openness to acquisition conversations (Robinson, 2022). Other potential candidates to bring under Xbox Game Studios include CyberConnect2 and Kojima Productions.

Conclusion

When Microsoft first made its debut with the Xbox in the Japanese market, the momentum it created in the U.S. and Europe did not translate to Japan because the nuances inherent to the Japanese gaming industry amplified the shortcomings of the console and positioned it as a non-competitor ever since. The Xbox 360 was the most successful console of the brand, but it fell to a new low with the Xbox One. Evaluating the performance of the three biggest console manufacturers (Nintendo, Microsoft, and Sony) in the most lucrative gaming markets further cements Xbox's disappointing performance in Japan. However, the recent debut of the Xbox Series X and Xbox Series represents another opportunity for Microsoft to reinvigorate the brand's presence. Given Nintendo and Sony's historical dominance in the country, it is unrealistic that Microsoft can usurp either company in terms of market share over the course of the next generation. Instead, Microsoft's main goal should focus on building a sizeable, reliable consumer base in Japan, with Game Pass as the foundation for attracting new consumers to the platform. There is no question that the company has the resources to change its fortunes, but it must be paired with a deep awareness of the nuances inherent to Japanese gaming industry and Japan to pursue strategies that fulfill its promises to better serve the Japanese market. Outside of Microsoft's ambitions, however, encouraging healthy competition within the

video game industry from country-to-country fosters the conditions for its players to deliver innovative experiences in the medium from a technological and artistic standpoint.

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Figures

Figure 1

CAGE distance framework chart between the U.S. and Japan at the country level

Cultural	Administrative	Geographic	Economic
<ul style="list-style-type: none"> ▪ English and Japanese are both distinct languages, and they are some of the most difficult languages for native speakers to learn respectively (2022) ▪ Demographics are distinct (U.S. is more ethnically diverse while Japan is more homogenous) ▪ There are more implicit cues in Japanese communication as a result ▪ Insularity/nationalism for both countries manifest in different contexts ▪ Traditionalism resonates more in Japanese culture when it comes to social norms (i.e., cuisine, hierarchy) 	<ul style="list-style-type: none"> ▪ The United States and Japan do not share colonial ties with each other. ▪ Tensions were highest during WWII after Pearl Harbor bombing, U.S. military occupation set a new precedent for country relationship; now considered one of the strongest global partnerships ▪ U.S.-Japan Trade Agreement and U.S.-Japan Digital Trade Agreement (2022) ▪ No shared trading bloc; closest was the TPP before U.S. withdrawal in 2017 ▪ No common currency (\$ vs ¥) ▪ Both use free mixed market economies 	<ul style="list-style-type: none"> ▪ The U.S. and Japan are about 10,000+ km away from each other. ▪ Large time zone difference (can range from 13-19 hours) ▪ Japan is isolated as an island nation ▪ Japan is much smaller (the size of California, but higher population per capita) ▪ More difficult access to goods and resources in Japan; U.S. has easier ties with Mexico and Canada ▪ Robust transportation and intracommunication systems within Japan; U.S. has weaker national transportation infrastructure ▪ Japan is more susceptible to natural disasters 	<ul style="list-style-type: none"> ▪ GDP per capita: \$63,593.40 in the U.S. and \$40,193.30 in Japan (2020) ▪ 1st and 3rd largest world economies ▪ Inflation trajectories of both countries are polar opposite. U.S. is currently struggling with inflation concerns (Fujikawa, 2021) while Japan continues to suffer deflationary pressures that are driving consumer prices down and stagnating wages ▪ Japan experiencing population decline, which will lead to smaller workforce (U.S. still increasing but will follow the same trajectory)

Figure 2

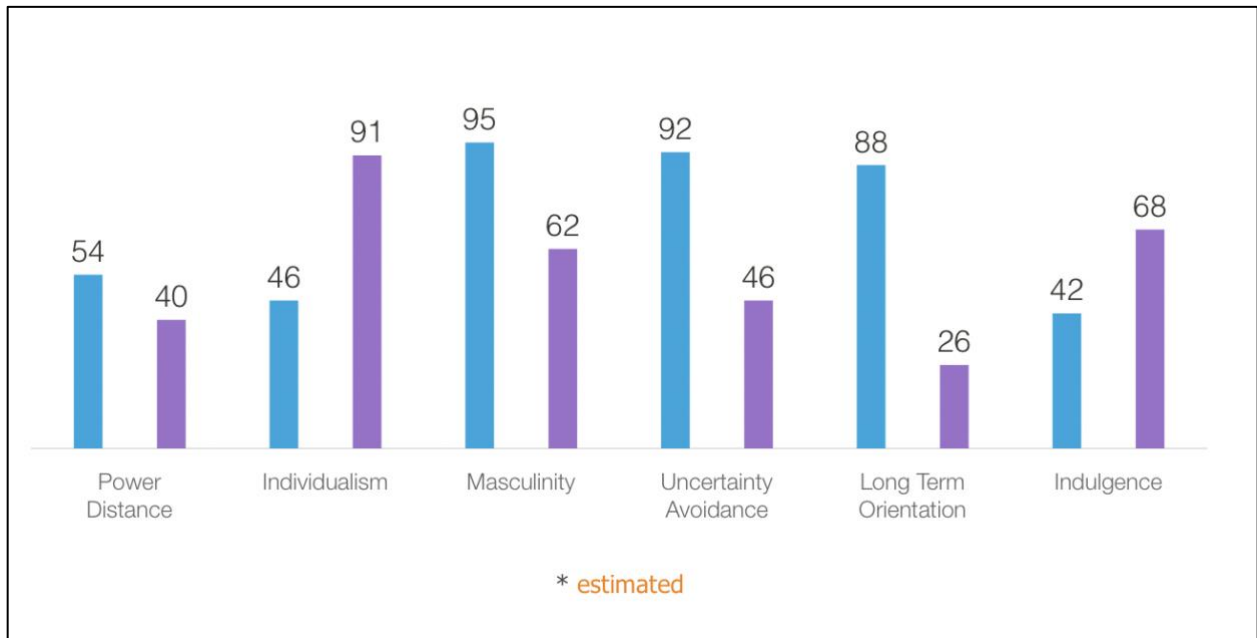
CAGE distance framework chart between the U.S. and Japan at the industry level (video games)

Cultural	Administrative	Geographic	Economic
<ul style="list-style-type: none"> ▪ Video games are considered to have “high linguistic content”, where differences are most prominent ▪ English to Japanese localization is a tough process (uses different scripts, indirect translations are frequent) ▪ Some video game series are heavily associated with each country (i.e., JRPG has specific connotation compared to RPG) ▪ Mobile gaming constitutes a bigger proportion of Japanese gamers due to space constraints and constant mobility ▪ United States gaming attitudes; perception that more men play games than woman (the ratio is roughly 55/45) ▪ In the Japanese mobile gaming space, the inverse is true (55% of mobile users are female) ▪ JRPGs, action-adventure are more popular in Japan, whereas shooters 	<ul style="list-style-type: none"> ▪ U.S. and Japan use different ratings boards to assess the content of games: the ESRB for the U.S. and the CERO for Japan ▪ While both are non-profits, the ESRB is a self-regulatory board with more independence ▪ If a game receives an M-rating in the U.S., you must legally be 17 years old to purchase and show ID. In Japan, it is similar for CERO Z ratings (but for 18 years of age) ▪ Acquisition culture is different ▪ Keiretsu is a common form of business partnership that links companies together through network effects 	<ul style="list-style-type: none"> • Geographic clusters of game development are more varied in the U.S. • Most game development is heavily centralized in Tokyo (Nintendo is rare exception based in Kyoto) • Many Japanese gaming companies have American subsidiaries rather than the other way around • Game development is more global (i.e., outsourcing parts of projects to different countries) • COVID-19 pushed game development more virtually; • During the localization process, distinct time zones and physical distance require very specific timeframes for communication • Proximity to 	<ul style="list-style-type: none"> • U.S. game industry valued at \$40.5 billion, Japanese game industry valued at \$22.1 billion (2022) • They are the 2nd and 3rd largest gaming markets behind China • Japan’s economy is more intertwined with entertainment; major part of the “Cool Japan” initiative • Nintendo and Sony are Japanese competitors in the console hardware sector, whereas Microsoft is the sole console manufacturer in the U.S. • Japan once dominated the video game industry (50%) but it has fallen under 10% with the U.S. and China overtaking its position (Buchholz, 2021) • Japanese labor costs are rising

<p>and sports are more popular in the U.S.</p>		<p>China is an important consideration</p>	<p>in the gaming industry with China becoming a star player; economically closer to Japan (Phillips, 2022)</p>
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Figure 3

Hofstede's cultural dimensions comparison between the U.S. and Japan



<https://www.hofstede-insights.com/country-comparison/japan,the-usa/>

Appendices

Appendix A. Interview Questions and Answers with Dr. Serkan Toto

Could you provide a temperature check on Xbox's performance in Japan?

The best way to describe it is a struggle. Microsoft never really took off despite trying for decades, but everything else works well for Japan. For Microsoft overall, Japan is one of the biggest markets. It is one of the biggest economies in the world, there's a lot of people here as the 11th most populous country. So, Microsoft does make a lot of money in Japan, except the Xbox.

So, the Xbox is very much an exception to the rule compared to their other products and services?

Yes.

Got it. When I did some research initially, I know that the Xbox didn't have the greatest start in Japan. They were trying to find ways to adopt the Xbox 360 (in Japan) after the original Xbox went out with a whimper even though they considered it an essential gaming market. They tried to make adjustments, such as making it slimmer and making it more adaptable to the house. It's very interesting now that a lot of the PR from Microsoft executives claims that Japan is the fastest growing market for [them] and it's interesting how they've persisted and viewed it as an important market despite [the Xbox] not flourishing as much as it did before.

There's a couple of points about that. First, Microsoft has the money to do so. If it was an American company, they would have stopped fifteen years ago. But Microsoft is such a profitable company that they're able to pump money into the Xbox brand in Japan. They're losing so much money every single week, every single day, every single month, so Microsoft can stomach the loss from a financial perspective. I think the second point is that one of the big reasons Microsoft is still doing that is because as you alluded to, Japan is still a major force in gaming, and they want to have a certain presence in Japan. It reminds me back in 1999 when I did an internship at General Motors (GM) in Japan. It's another giant corporation that is quite successful in its home market in the U.S. when it was unbelievably profitable, whereas they had almost no presence in Japan. And they told me that the reason they were in Japan was for the representation: they were the biggest car company in the world, and they couldn't not be there. Microsoft wants to represent, they want to show that the Xbox brand exists, and even though they are not making any money with it they still have business in Japan. And there's also a certain level of corporate pride and the branding that comes with it.

If you had to list out two or three key differences between the U.S. and Japanese gaming industries that someone should be aware of, what would they be?

One of them is on the supply side because of the much bigger competition in Japan. In Japan, there are 10-15 publicly traded video game companies, and about six or seven of them are really big. These are large-scale companies that have a billion-dollar valuation at least such as Konami, Square Enix, Sony, and Nintendo. You don't have that in the U.S., and in terms of video games

(not mobile games or PC games), there is a much richer ecosystem on the supply side with smaller and mid-sized video game companies that are not publicly traded, as well as big publicly traded companies on top of the pyramid.

On the demand side, I would say the biggest difference is one of taste in games and design and genres. In Japan, the number one genre is RPG, and in the U.S., it is first-person shooters and sports games. It's not like people don't play these games in Japan, but they play a much smaller role in the gaming company compared to the U.S.

That was one of the stereotypes I had about gaming preferences as well. It was entrenched in my mind that RPGs tended to be more popular in Japan compared to the U.S. and FPS and sports were bigger in the U.S., especially when I look at the NPD numbers and see Call of Duty, Madden reliably in the Top 5. In Japan, you usually see Nintendo games dominating the charts, with the exception of a popular series like Dragon Quest or another prominent RPG.

It also changes all the time. As we speak right now, Nintendo controls 80-85% of the Japanese video game market because the Switch is such a big platform here. The conversation would be different five years ago when the PS4 was big and the Wii U never really sold. American users play Japanese games, but Japanese users don't play American games.

Much of the coverage I've seen about Microsoft trying to break into Japan was the need to tailor their selection more to the Japanese. Xbox is selling better with Series X/S than the Xbox One. Are consumer needs moving towards Xbox games, or is Microsoft better adapting to the Japanese market?

I think it's a little bit of both. If you look at the first Xbox, Microsoft didn't do a lot of original Japanese games, and it completely flopped. Bill Gates was over in Japan presenting the console while he was still working actively for them. With the Xbox 360, Microsoft had localized games made in Japan only for Xbox. Some of them are collector's items now, and that didn't work. They soured on the Japanese market, and when the Xbox One came around there weren't a lot of games made in Japan for that platform anymore. And now with the newest Xbox, Game Pass is the biggest seller. And I think the big driver for Xbox Series sales is that subscription service. It's not that Microsoft did a lot of "Made in Japan" games like the Xbox 360 times. They don't secure a lot of Japan-only games for themselves either; it's really driven by Game Pass.

And the second point is that you can't really buy the PS5 in Japan. The Xbox supply situation is not great in Japan, but it's much better than the PS5 situation. So, if you want to play next-generation games now, financially and time-wise, you probably have to buy an Xbox Series X and that is helping Microsoft this generation.

That's absolutely true. It's also the same case in the U.S., where it's still difficult to find a PS5 or Xbox Series X. You can't walk into a store and find it; you have to order it ahead of time to purchase one. I have seen Xbox Series S on the shelves whenever I go to Best Buy or Target, but I cannot find PS5 or Xbox Series X.

In Japan, you will sometimes see the Xbox Series X, but you will never find the PS5. I am in the retail stores all the time as part of my job, or “channel checks” that I do for my clients, and I still haven't seen one.

There's been a lot of speculation about the possibility of Microsoft trying to acquire a Japanese gaming company. First, do you think this is a real possibility for Microsoft given that Japanese business law and culture poses different challenges to the U.S. Second, why do you think Microsoft hasn't taken a similar approach to Sony in going after specific Japanese titles?

Sony has a homefield advantage. Even though they've closed down development and deemphasized Japan as a target for their consoles. They're also allocating more hardware away from Japan, they're still a Japanese company. The Japanese economy is much more closed than the American economy and reflects a different business culture. There's peace of mind with a Japanese gaming company talking to another Japanese gaming company rather than Microsoft, for example. Another point is because of Microsoft's poor performance in Japan, that really hasn't instilled a lot of confidence in the local game makers that their games will be taken care of properly in terms of marketing and customer support. In addition to homefield advantage, Sony's hardware is selling better overall.

Microsoft can do the same thing as Sony and sometimes go out to buy individual games for timed exclusivity, but it is a different approach. The biggest reason for the different approach is that Sony doesn't have the capital that Microsoft has. They cannot go and buy Activision Blizzard because it would have been half of their market capitalization, unless they pulled an unbelievable financial stunt. You're looking at two totally different companies in terms of size, capital, power, and clout. Sony has to be more creative, and you can see that in their strategy.

With Nintendo and Sony being Japanese companies, that certainly is a factor when you consider that Microsoft is the only non-Japanese company of the three competing in Japan. Even though it plays a role, do you feel that when someone says that Microsoft isn't doing well in Japan because there's immediate preferences towards Nintendo and Sony that it's overblown, or is there a more complicated mix of factors?

I think it doesn't really play such a big role in this game. If you look at Apple, the iPhone is unbelievably popular in Japan even though there are homegrown companies like Sony and Panasonic that have their own handsets. The iPhone was accepted, and Apple became an unbelievably popular brand. I think the American factor doesn't play a role, but I think the real problem for Microsoft was something we haven't mentioned yet. When Microsoft launched the Xbox in Japan, the initial batch of Xbox deliveries were really faulty in terms of hardware quality with the “red ring of death” not only in Japan, but America and everywhere where the Xbox was sold. Because Japan is a country focused on perfection, service, and the expectation that everything works, it scarred Microsoft for life. That initial failure meant that some Japanese customers never looked back, and they just bought a Playstation or Nintendo device as their next console, which was bad branding and PR for Microsoft. But Microsoft being an American company and having a strategic disadvantage probably isn't the case.

We've talked about Game Pass being an attractive option for the Japanese market as a more affordable option and letting users access a larger catalog of games. Another initiative is xCloud that is still testing the waters, but offers the opportunity to play games on a mobile device or screen. Do you feel that because mobile gaming is such a dominant force in Japan that xCloud could benefit from it in the future?

It makes sense on paper, but it's a little bit conceptualized. It sounds so good on paper that maybe it has to be true, but as you noted it's not a big deal outside of Japan. There are some deals with carriers in Japan to bring xCloud to people's devices, but it seems like a non-factor right now. The big point is really about Game Pass. To also add this point, don't forget that the average game cost in Japan is higher than the U.S. So, if you want to buy the latest Xbox or PlayStation game, you pay more than the U.S. There's less discounts and less ways to save money. In light of that pricing policy, the Game Pass offerings look even better in Japan than the U.S. or Europe, where you can get certain games two months after release for \$30 instead of \$60. Of course, in Japan, there are discounts, but they don't have the discount culture as seen in the U.S. And again, that makes the Game Pass offering even more attractive to Japanese users than people in other territories.

In terms of the yen (Japanese currency), how much is the average game cost?

8,000 yen. It depends on the store, the game, and the platform, but it is not unheard of.

Do you see a future where Microsoft could rival Sony in terms of market share, and what do you think is Xbox's ideal positioning in the Japanese market?

Their ideal position in the Japanese market is that they're killing Sony and turning the tides, but I think that's going to be difficult. What Microsoft really needs in Japan is an Activision Blizzard type of deal. They need a big solution. Making Game Pass a little more attractive, purchasing SEGA games to put them into Game Pass, agreeing to put a game like Final Fantasy XVI on Game Pass... these are small steps that help, but if they really want to make a big step ahead in the Japanese market, they have to pull out their camera. You cannot make baby steps anymore because Sony's too big for that, Nintendo's way too big for that. To create meaningful business in Japan, they need a big solution.

Are there any final remarks that you wanted to add that weren't covered by the questions?

I don't think so. The one thing I really wanted to focus on earlier was the initial disappointment from the Japanese user base from the Xbox's hardware quality. I guess one more thing to note is that the Japanese has a religious, fanatical obsession with quality. You can make American users mad when you deliver low quality products and things get broken, but in Japan it is on a completely different level. When you disappoint the Japanese consumer, it's almost impossible to get them back. This is one of the factors that's not being discussed a lot when talking about the failing performance of Microsoft in Japan. The first impression of the Xbox in Japan was so negative that Microsoft basically never recovered.

Appendix B. Interview Questions and Answers with Mr. Nathan Brown

Could you give a temperature check on Xbox's performance in Japan (past and present)?

The only Microsoft console to make anything you could reasonably call headway in Japan was Xbox 360, with sales of 1.6 million, which can largely be attributed to the extra focus Microsoft put on Japanese studios during that generation — four of the top five selling Xbox games in Japan were Xbox 360 exclusives (see above link). But across Xbox's 20 years of existence less than one third of one percent of console sales have been in Japan. Phil Spencer has promised to do better in the Xbox Series era, and there's already progress of sorts: Series S and X have already outsold Xbox One. But that's a low bar to clear indeed. I think Game Pass alone should see Xbox enjoy a certain level of success this generation, but only in the context of itself. I highly doubt Nintendo or Sony are losing much sleep about being overtaken in their home market.

What are the key differences between the U.S. and Japanese gaming industries?

Speaking in extremely broad terms, as a rule the Western game industry dreams a little bigger, and thinks more globally. Western companies spend more on development on the assumption that their games will find a big global audience and make a lot of money. Japan, by and large, tends to have fewer resources to play with, and tends to think of its native audience before a global one. (Japan's industry tried to reverse this in the 360 era, but it didn't really work: there's some good stuff on this [here](#)). Western developers tend towards realism, and Japanese to fantasy. And while western gamers prioritise PC and console, in Japan mobile is equally, if not more, precious. This isn't just about phones: PSP was huge in Japan, largely thanks to Monster Hunter, and I'd venture that Japan's love of portable play isn't only key to Switch's success in Japan, but was a driving factor in its original design.

Do you think Microsoft competing against Nintendo and Sony as the only non-Japanese company plays a role in their weaker performance?

Honestly, I don't know for sure. It's a popular theory but I don't think Xbox's hitherto struggles can be blamed on patriotism, or nativism, or whatever you want to call it. Instead, I think it's simply a reflection of Microsoft's failure to offer a value proposition that appeals enough to Japanese players to enable it to break through. Sure, it signed up a few exclusives in the Xbox 360 era, and that worked reasonably well. But let me put it this way: would you choose an Xbox console to play four Japan-made exclusives, if doing so meant losing access to the dozens of Japan-made exclusives on PlayStation? It's only ever going to be additive, I think, the thing the committed, and monied, core gamer buys when they've bought everything else.

Microsoft's Xbox strategy centers around acquisitions (Bethesda, Activision). There's a lot of speculation about them trying to bring a Japanese gaming company under their roof. Is this a real possibility given Japan's corporate governance, and is it a necessity?

I think the article I wrote about this speaks for itself, though one thing I'd add that I perhaps didn't focus on enough in the piece was that if Microsoft really, really wants something to

happen, then it can make it happen. As we've seen from the Activision deal, it will quite happily pay through the nose for a company mired in scandal. It is willingly submitting itself to an antitrust investigation and a number of misconduct lawsuits because it believes having Activision in its stable will improve its gaming business. So yes, there are a lot of barriers to overseas companies buying Japanese ones. But when you have access to infinite money, there are few barriers that can't be scaled.

I certainly wouldn't say that a Japanese acquisition is a necessity for Microsoft. In fact I think it could be counterproductive in a way. There is already unrest at the flurry of consolidation going on around the game industry, but gamer's darlings have, so far, been largely left alone. Microsoft's acquisitions to date have been almost entirely focused on the west (the exception being Tango Gameworks, which it got as part of the Bethesda deal). If it starts picking up Japanese companies and taking their games off PlayStation/Switch there will be uproar, and I'm not sure that necessarily translates into sales. It just means a chunk of players don't get to play games that they would otherwise have bought. If you're on, say, iPhone, and some new game launches exclusively for Android, you don't just go and get a new phone, right? Players who are comfortable in the PlayStation or Switch ecosystem aren't going to drop them because a game they want is now only on Xbox. My fear, if I were Microsoft, would be that buying a Japanese studio wouldn't lead to that many new console sales or Game Pass subscriptions, and that it would just mean games selling less because they're less widely available, and western fans of Japanese games having a stick with which to beat Spencer and Xbox.

Xbox's flagship initiative Game Pass is an attractive option for its cheaper price tag and access to games. Is this the key for Microsoft to make more headway in Japan?

I don't have much insight into how popular subscription services are in Japan. I can certainly see it bringing success on PC, though, and mobile. There were rumors going around a couple of years ago that Microsoft was trying to get Game Pass on Switch; something like that would surely do very well. And since Microsoft's long-term plan is untethering Game Pass from dedicated hardware — be that through an HDMI streaming stick of some kind, a native smart TV app, or similar — then yes, I can see that penetrating the market in a way that Microsoft's consoles have not.

What do you believe is Xbox's ideal positioning in the market?

As I said above, I think it's more about Game Pass on non-dedicated hardware — PCs, phones and tablets, and down the line TVs — than it is about signing exclusive games or buying Japanese companies. I think Microsoft has long since realised that it will always be in third place in Japan, and has pretty much made its peace with the fact. Unless it acquires PlayStation or Nintendo, of course, but honestly I'd rather not think about that. The sky would fall in.