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Electronic Arts



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Executive Summary

Electronic Arts’ recent profit downturns raise serious strategic questions. This downturn has been attributed to shifts in American gaming preference away from EA’s offerings. To find new areas of profitable growth, EA should apply its strengths to burgeoning Asian online gaming markets, projected to reach \$1 billion in 2005.

The massive multiplayer online game (MMOG) market is too potentially lucrative for EA to bypass, even as a latecomer. Acquiring local content creation capabilities and coupling that with EA’s existing technical expertise best brings forth EA’s strengths and mitigates its weaknesses. Proper marketing and securing vital distribution channels should initially be done through joint ventures. Initially entering “stepping stone” geographic markets avoids serious political pitfalls. Additionally, some of EA’s franchises, such as the *Sims*, are naturally positioned for the emergence of mobile phones as networked gaming-platforms – a phenomenon underway in Asia.

The table below summarizes the recommended strategies EA should follow in Asia:

	MMOG	Mobile Sims
customers	serious gamers	moderate-casual gamers
geographic target	initially Taiwan, Hong Kong, & Singapore subsequently China	Japan Korea
rivals	NCSOFT Sony Online Shanda	NCSOFT Lager Nokia
venue	internet cafés	mobile service providers
platform	PC	Mobile phones
EA’s value added	technical expertise capital marketing experience with <i>Ultima Online</i>	The <i>Sims</i> franchise sports brands technical expertise

EA's Predicament

Electronic Arts, Inc (EA) is the largest video game publisher in the world, with a strong presence in the North America and Europe.¹ Its success can be attributed to the strategy of developing games for all major platforms and expanding successful games into profitable franchises. Though it publishes a variety of games, it is strongest in family-friendly games based on sports, movies, and social interactions (i.e. *The Sims*). EA also published the first successful massive multiplayer online game (MMOG), *Ultima Online*. It has international sales forces, but individual studios are responsible for developing distinct game series. EA tends to buy independent studios after they develop successful games, e.g. acquiring Maxis and Origin for *Sims*² and *Ultima Online*, respectively. EA enjoys tremendous brand recognition in certain genres and possesses enormous financial capital.

EA has been labeled the Disney of video game publishers because it avoids developing games with adult content.³ Although three of 2004's top ten games were made by EA, the top two games were both rated "M,"⁴ possibly because the average gamer is aging.⁵ Mature MMOGs, led by Blizzard's popular *World of Warcraft*, chipped away at *Ultima Online* sales. The domestic MMOG market is also drawing Asian developers. Even if EA's core franchises, like sports games, are not threatened by MMOGs, platform convergence and free flow of capital makes any successful gaming enterprise an eventual competitor.

EA also relies on existing storylines and characters by basing games on sports and movies. While this takes advantage of existing fan bases, EA lacks experience in developing original plots. In fact, EA's reliance on American sports fans is risky, as Take-Two Interactive is undercutting EA with cheaper ESPN based games,⁶ including two of 2004's top ten games.⁷

Because of these threats, EA suffered a 90% decline in fourth quarter FY 2004 net income and lowered FY 2005 estimates.⁸⁹ (See [Exhibit](#).) Consequently, it is desperately testing new strategies. In an attempt to expand into Europe, EA has bought 19.9% of shares of UbiSoft, a major French competitor.¹⁰ EA is also developing a mature game based on "The Godfather," a risky move for a company with neither experience nor reputation in mature games.¹¹ Additionally, it is setting up marketing and development sites in Asia, but has yet to announce detailed plans. EA is also seeking to enter the wireless gaming market.¹² Rather than invest in wildly different strategies, EA should focus on a few complementing strategies. Instead of competing as an inexperienced entrant in the cut-throat mature, domestic market, EA should focus its energy on leveraging its existing expertise – in acquiring and marketing successful franchises, family-friendly content, and sophisticated graphics – in the attractive Asian market.

Why Expand into Asia?

IDC projects the Asian online gaming market to reach \$1 billion in 2005.¹³ By expanding into Asia, EA can apply its strengths to markets with unexploited franchises still in need of capital investments and 1st tier technical competency in graphics. Asia is the best geographic market because it has two promising gaming segments that can benefit from EA's expertise. The first is a booming online game market. The second is the nascent wireless gaming market.

Referring to Asia as a monolithic market would be a big mistake. Japan reflects a mature gaming market with strong console presence, high home PC and internet penetration rates, and many domestic game content providers (much like the USA). Meanwhile Korea, where gaming at

internet cafes has become a national phenomena and broadband coverage is at an unprecedented high, constitutes the largest online gaming market in the world. Taiwan, Singapore, and Hong Kong boast affluent economies which are coupled with loyal gaming communities. What China lacks in terms of development – disposable income, PC and console penetration, and internet (much less broadband) coverage – it makes up in size and booming potential.

Also, the Asian online gaming market is attracting international interest, with many U.S. game makers trying to enter it. Microsoft is signing famous Asian game developers to attract attention for its games.¹⁴ Other entrants include Sony Online Entertainment, which teamed up with an Asian partner, Gamania, to release Everquest II in 2004¹⁵, and Blizzard, which teamed up with a popular Korean game publisher, Hanbitsoft, to bring its first game to Asia.¹⁶ Given the potential in the Asian market, as well as increasing competition in the domestic market, Electronic Arts must at least explore the Asian market now so that it does not fall behind its competitors.

Analysis of EA Opportunities in Asia

Although games are like movies and music, with sales changing significantly with the latest hits, it is possible to assess market potential based on quantifiable (or at least describable) criteria of complements, consumer driving forces, and market size. See the appendix for the [data chart](#) which the subsequent analysis is based upon.

Korea – Reigning Champion

EA has opportunity in Korea because of the developed customer base and deep complement penetration. Over half of Korean internet users play online games. Although this statistic includes casual users of free online games, which fall outside EA's target demographic, it clearly demonstrates a receptive audience.¹⁷ Gaming, thanks to the clans that form in cooperative play, has become a mainstream way for young Koreans to interact socially. Like most of Asia, the majority of serious online gamers continue to be young males.¹⁸ This suggests both an untapped market – young females – and the potential of established customers.

Korea enjoys high broadband coverage, which resulted from a unique confluence of government policy, geography, and competition.¹⁹ EA cannot expect similar coverage in other Asian countries without similar policies and economic conditions. Given this, EA should be patient elsewhere about introducing games that require large home broadband penetration to succeed, such as multiplayer console games. Many of EA's domestic game titles should not merely be ported to new markets.

The Korean residential teenage market is driving mobile service provider revenue, so applications that attract usage from this market are in high demand. Online games may be well positioned for this task and present a growth opportunity for EA. Service providers control content provisioning in mobile services, so their demand is crucial for EA. Other Asian countries, particularly Japan, exhibit similar potential. [See [Exhibit #1](#)]

China – Open Questions

Most of the growing Chinese gaming market lies with internet cafes. As of 2003, over 100,000 internet cafés, mostly mom-and-pop shops, served the nation. These free wheeling hubs of internet usage have attracted government scrutiny. Legislations banning internet café operation near schools and requiring censorship software²⁰ are enforced by waves of government-forced

shutdowns, a threat that induces most owners to self-censor against content banned by the government. In addition, the government is planning to have all internet cafes under large national, i.e. state-owned, companies.^{21 22}

The proposed government consolidation of distribution channels may alter market potential by increasing buyer bargaining power and creating entry barriers, especially for foreign entrants. If the transition to government control accelerates, EA must establish a presence immediately with local regulatory know-how, or risk being shut out. Most EA content, rated Teen or below, will be socially acceptable. However, content that touches on political topics such as *Command and Conquer* have been banned, and EA should take care to ensure that its games will be acceptable to the Chinese government and public.

The online gaming market is dominated by MMOGs in China. Gamers have gravitated towards themes grounded in traditional mythology or history²³, but games with a Western twist, like *The Matrix Online*, may also be successful.²⁴ For EA to exploit this market, it must develop content that appeal to Chinese tastes and have strong storylines, which analysts believe is key for a game's success.

However, the mobile market in China is less attractive than the online gaming market. Unlike in Korea, there is very limited mobile gaming and entertainment there. Furthermore, China's mobile market is controlled by a China Unicom and China Telecom duopoly,²⁵ so viability of mobile gaming would be at the whim of these service providers.

Japan – Cutting the Cord

The Japanese gaming market is a large yet saturated market, which is similar to the USA in terms of prevalence of consoles and console games. In addition, buyers have many games to choose from, and many entertaining alternatives to gaming in general.²⁶ Like in Korea, opportunities lie in new platforms like mobile phones.

Japan's ranks of successful content developers, console makers, etc. are well known. It has taken a back seat to Korea in developing MMOGs yet has had notable success with fantasy and role-playing games (RPGs). Hence, EA may find a saturated market in traditional genres. This necessitates looking to underserved demographics or novel platforms.

The convergence of mobile devices and gaming consoles is a plausible scenario since game-capable phones have been out for years and technology advancement continues. 95% of teenage girls in Japan own cell phones (80% for teenagers in general) and 81.2% of mobile subscribers accessed games through their mobile devices. Games from the role-playing and fantasy genres are already common on mobile devices.²⁷ Interoperability of mobile with consoles and PC games is a commonly discussed possibility. High quality 3-D games, in which EA is strong, are still hard to come by on the mobile platform. EA possesses existing content, including the Sims and certain sports franchises, to satiate anticipated mobile demand.

Taiwan, Hong Kong, and Singapore

These three pan-Chinese online gaming markets are noteworthy for their commercial size, relatively uninhibited access, and potential to open doors to other markets. The prevalence of PC's and broadband complements bodes well for online games. Culturally, these countries have readily adopted or created the kinds of games that are popular in the more attractive growth markets. The cultural and economic conditions of these Little Tigers reflect the conditions in the

more affluent urban regions of China, making them fertile proving grounds for new games. EA may find this region an attractive entry point for games targeted at serious gamers (MMOGs) since it is free of China's unpredictable regulations and Korea's entrenched competitors.

Piracy and Distribution

Piracy is a formidable problem in Asian countries, though Japan is the exception.²⁸ Because of this, EA should develop online games, whose authenticity must be verified before a user can play the game. This model has been successfully adopted by other game companies in Asia.²⁹ This model allows EA to reap profits from subscription costs, not sales of packaged games. Korea's high broadband penetration allows users to play in their own homes, but China's low broadband penetration forces them to play in internet cafes. EA should emulate existing publishers, which offer free game downloads and trial periods, but require users to pay subscription fees after this trial period to keep playing the game. Various subscription models are currently used in Asia, ranging from monthly to hourly fees, to accommodate gamers with different levels of disposable income.³⁰ Players can also buy "time cards" that allow them to play for certain periods.³¹ These models are rare domestically, but are crucial in Asian markets because of different consumer habits.

In addition to the internet, games are also distributed through cell phones in Japan, where 44.9% use cell phones to play wireless games.³² However, EA has limited access to mobile distribution channels at this point, and will need to partner with local cell phone providers and manufacturers to distribute its games.

Entry Barriers

One of the entry barriers that EA faces is lack of brand recognition in Asia. Heavyweights like NCSoft enjoy strong reputation in local markets, while EA is virtually unknown. However, this barrier can be overcome by the development of a good game, since gamers make purchases primarily based on word of mouth and editorial reviews.³³

Other entry barriers include the need to attract gamers quickly to recuperate the costs of producing games, sunk costs in developing a game, and strong presence of existing game companies in parts of Asia. In China, EA must be wary of government censorship of games since the government has already banned various EA games, though allegedly to curb piracy.³⁴ It may be wise to first release new games in less regulated markets, such as Taiwan, and partner with local companies to minimize the threat of censorship.

Suppliers

Traditionally, suppliers for packaged video games include firms that make game disks and cases, and instruction booklets. EA can purchase these items from many sources at volume discounts, with the exception of certain console-specific game discs. Shortages in such components have caused problems in the past.³⁵ Online PC games will not be dependent on such specialized discs, but EA will require suppliers of server space, which should be readily available.

Based on the current abundance of online games offered in the Asian market, there should be no shortage of game designers. Due to EA's strong position in the U.S. and Europe, it can afford to offer slightly higher salaries than Asian competitors to initially attract new employees.

Substitutes

Video games are part of the entertainment industry, so anything that competes for a customer's leisure time is a substitute, such as television and movies. Japanese consumers generally have more entertainment options to choose from, whereas Chinese and Korean consumers have more limited choices. Therefore, an immersive game would be better suited for Chinese and Korean players, whereas a casual game would be more appealing to Japanese players.

Network Externalities

While the network effects on single-player console games may be minimal, they are significant on any multi-player game. This is especially true for MMOGs, whose strong appeal is based on a player's ability to socialize with thousands of other players in an extensive online community. Without a widespread, established pool of players, the MMOG becomes just another single player video game and loses much of its allure.

Competitors

Sony

Sony Online Entertainment (SOE) is one of EA's strongest competitors in Europe, North America, and Asia. SOE has a strong in-house game development and design capability for both MMOGs and casual games, and has released several top-selling fantasy MMOGs including *Everquest* and *Everquest II*. It has also tried to enter the Asian market in recent years but found trouble since Asian players could not culturally identify with the games.

SOE and EA offer different types of online games. SOE offers games targeted towards hard-core, mature gamers, while EA offers games targeted towards a more general audience. EA has not committed serious effort to MMOGs to match *Everquest*. The Asian market also has different demands than the U.S. market, so SOE's domestic success may not translate into success in Asia. As a result, SOE will take extra steps to counter EA's entry by increasing the quality of its content for the Asian market in particular and securing channels to reach gamers.

SOE will aggressive partner to localize content and fight with EA over quality instead of price. It will work with local companies to make its content more culturally Asian in theme. In addition, SOE will react to EA's entry by securing distribution channels, which is especially important in China and Korea. In China, where a large portion of players access online games through internet cafes, and in Japan and Korea, where wireless cell phone game play is projected to increase, SOE will look to create contracts that would allow pre-loaded games. This will significantly increase customer's access to SOE's games over other game-makers' content.

If EA responds with similar actions, it will be able to minimize the differences between competing in Asia and the U.S. EA will be competing with SOE on the level of content, and it will be up to EA to ensure any new games it releases in Asia are up to par. EA could guard against SOE's monopolization of mobile channels by offering service providers – who control provisioning – alternatives to supplier hold-up.

NCSOFT

NCSOFT's strategic position is defined by its mastery of Korean MMOGs through the *Lineage* series. It has solidified competencies in the technological backend, content creation, technical

artistry, service infrastructure, and marketing required for successful MMOGs. It wields extremely robust cash flow in its quest to expand geographically and content-wise, and has proven ability to develop and market games in Asia and North America. However, it is vulnerable to a successful entry into base territories due to the fad nature of games, and will be challenged by more experienced players when moving into different genres and platforms.

While EA's current market positions do not compete directly against NCSoft, except *Ultima Online*, any move into the MMOG market will compete against NCSoft. In addition, the enormous revenue streams allow NCSoft to move into locations or genres that EA considers its base. In fact, NCSoft has already moved into the American MMOG market with its acquisition of ArenaNet and the April 2005 launch of *Guild Wars*, a highly anticipated game with the largest pre-order volume. Another title, *AlterLife*, is a social MMOG that competes with EA's *Sims*.

If EA were to enter the Asian market with a RPG, NCSoft would likely respond with increased activity from *Lineage II* – expansion, upgrades, etc. This would force EA to up the quality bar and let consumers capture most of the value added. NCSoft's strengths can be skirted in markets not as saturated and with stronger growth than Korea. That suggests Taiwan and China.

An EA introduction of Sims-like games would face less entrenched opposition. Brand does not translate well over demographic groups. NCSoft's *AlterLife* is still under development, leaving EA a window of opportunity. *AlterLife* is in an unfamiliar genre where EA has significant experience through *Sims Online*.

A judo strategy where EA introduces increments of persistence to more traditional style games, targeted at more casual players or novel sub-segments, would be hard for NCSoft to counter. NCSoft has no experience with affiliated content (e.g. sports and movies) or making smaller scale multiplayer games. Given its lucrative serious-gamer MMOG position, diverting resources to other audiences would be unattractive.

Shanda

Shanda is the leading Chinese maker of MMOGs and ultimately hopes to become a Chinese entertainment console maker and provider. It distributes outside developers' games, such as *Dungeons and Dragons* in China³⁶, and the Korean-made *The Legend of Mir II*, and recently began in-house development of games and game content.

At this point, if Electronic Arts elects to enter the Chinese market, Shanda's control of distribution channels and base of self-developed games is not great enough to shut out outside competitors. However, if Shanda is able to establish its console like platform, it may be able to control the content seen by those customers. EA should not be concerned since no console has been successful without open interoperability with competing publishers' titles – e.g. Sega & PS2. For the proven PC-based internet café market, it will likely be a content war—the manufacturer who makes the game with the best content will attract the players. If EA enters the MMOG market, Shanda will step up its efforts to develop an internally-made popular game.

U.S. retail distribution is quite different from Chinese distribution, so EA should learn from some of Shanda's shrewd strategies in complement provisioning, particularly strategies regarding partnering with internet cafes and cell phone providers.

Lager

Game development houses such as Lager Interactive Inc. play a dual role of competitor and supplier to game publishers like EA. As a Taiwanese developer successful in historical-fantasy MMOGs, Lager possesses creative content in tune with Asian gaming tastes. Experience developing the successful *Fairyland Online* adds experience with non-traditional (e.g. female) audiences to its repertoire. Nevertheless, it lacks the marketing reach to promote, or the capital to undertake, many development efforts. As customer expectations for technological sophistication rise, Lager may be resource-constrained to remain competitive. Opportunities lie in the growing Chinese & Taiwanese serious MMOG markets and the potential to tap female audiences.

EA entry into Asia – particularly Taiwan and China – with in-house developed MMOGs would be a direct threat to Lager. In particular, the *Sims* franchise would target the same market segments – female and more casual gamers. However, as a development studio, Lager's options for response would be limited to more aggressive content and feature development since price competition is not driving factor in subscription. Because so many of Lager's opportunities require the marketing strength and capital that EA can provide, there is chance to realize synergies through being acquired by EA.

Potential Competitors

EA must be prepared for potential competitors that enter the online game industry from other industries. One threat is Nokia, which developed N-Gage, a cell phone and handheld gaming device in one. Nokia recently announced the development of *Hinter Wars*, a MMOG for Asia that can be played both on the N-Gage system and the PC,³⁷ allowing users to play the game at home and on the go. The primary threat to EA is that Nokia's strong presence in the cell phone industry facilitates the creation of a Nokia monopoly in the phone-based MMOG market, making any potential expansion into that industry difficult. However, Nokia is disadvantaged because it does not have experience in game design, and must rely on partners for game development. Exclusive partnerships with other game companies imply that any EA-developed MMOGs would be disadvantaged because they cannot be played on Nokia phones. This threat can be mitigated if other cell phone makers are willing to accept EA games, or if the industry moves to an open standard so that games are not restricted to specific phones or carriers.

Other potential entrants include companies that specialize in simple online games, and online gambling companies. They may be attracted by the high broadband penetration and large number of serious gamers in Asia to develop traditional online video games, and thus compete with EA in this market. They have more experience in the online infrastructure of games and enjoy existing subscription bases, but are less well-versed in the specifics of video game development.

Specific Strategies

Narrowing Down

Due to EA's past success with sports games, it appears that EA should develop similar sports-themed games for Asia. However, the Asian market is not as receptive to such games as Western markets. Competitive team-based sports are less popular in Asia, which is dominated by individual-based sports like badminton and table tennis. Games based on such sports are not ideal online games because they do not take advantage of the large number of online players.

Additionally, because there is not enough brand appeal for specific sports teams or individual athletes in Asia, EA cannot rely on the loyalty of sports fans for game sales. Thus, concentrating efforts on online sports-based games is not a recommended strategy for the Asian market.

Furthermore, since high piracy rates in Asia force potential EA games to adapt an online model, it is best to rule out any other games that are primarily single-player or few-player. One of the strongest appeals of online game play is the ability to interact with many players at once, which allows players to build a virtual community and enhances gaming experience. This rules-out first person shooter games and basic online games like chess. The latter has not attracted significant profits for EA in the past.³⁸ First person shooter games would also be unattractive since most, like Halo, are rated “M,” and EA has little experience in developing mature games.

Therefore, it would be best for EA to develop a non-“M”-rated online game that allows thousands of people to play together simultaneously, giving them a forum for social interaction while they are gaming.

Sims on the Go

One proposed strategy for EA’s entry into the Asian online gaming market is to target the online mobile phone gaming sector, and target both female and male audiences. Among all the Asian countries, Japan, Singapore, Malaysia and South Korea are the most suited for the introduction of a MMOG targeted towards both females and males, since these countries have relatively high percentages of female gamers. Among these, Japan is especially ideal for mobile gaming because “Japan...has leaned toward mobile games, as 44.9 percent of Japanese use the mobile Internet and play wireless games on their palm-sized gadgets.”³⁹

Given EA’s limited access to mobile networks, EA would need to partner with a mobile phone company in Asia. For this reason, China would be a particularly difficult market to enter due to the duopoly-controlled mobile market of China Unicom and China Mobile. It may be possible to partner with one of these companies to distribute EA’s games, as Shanda has done, but if neither company is willing, EA will have a hard time entering the Chinese mobile game market.

The potential game would be very different from a PC-based MMOG, which caters to mostly hard-core gaming males who are looking for hours worth of entertainment. The proposed mobile phone game, on the other hand, would target people trying to pass idle time, such as when traveling to work or school. One possible game to target this market would be a localized version of EA’s MMOG *Sims Online*. The original version of *Sims*, which was not an MMOG, attracted a consumer demographic of approximately half female and half male, and so would be well suited for the target audience in Asia.

While the *Sims Online* failed in the United States, it may have failed because of its lack of “custom object features” and a lack of cooperation among subscribers. However, versions of the game where people were allowed to play at frontier cities were much more popular, possibly due to the less rigid set of game rules at these locations.⁴⁰ Another possible reason for its failure is the lack of a fast-forward mode, since the game moves quite slowly at times⁴¹, and the lack of a sense of geography.⁴² EA should deal with these issues by adding requested features and elements of clan-building or social interaction, and localize the game to the Asian market. To more effectively target the Asian mobile phone gamer, Asian cultural elements should be added to localize the game, such as family, financial success, college admissions, and English learning.

Moreover, the subscription for this game should be per hour or minute rather than per month, as for most MMOGs, since people will be playing this game in their idle time. Incorporating these elements would provide a uniquely Asian game for both female and male idle gamers. While it would not specifically be marketed to the female market, it would provide an alternative to the hard-core MMOGs targeted towards the male audience. It would be a MMOG that both males and females could enjoy to pass time with friends, or pass time while traveling.

MMOG

EA cannot afford to cede the MMOG market in Asia for several reasons. As complements such as broadband, gaming platforms, and discretionary income rise, strong growth is predicted. Yet, in order to generate returns in a piracy ridden Asian market, game publishers must control content online. The MMOG, especially the RPG genre, has demonstrated its potential to cultivate paying, returning customers. This market represents the most viable demand of EA’s technical game making skill. Leaving whole profitable market segments uncontested to potential competitors, who utilize the same skill-set, would be unwise in the long run.

How does EA move into the MMOG market given that its strength has been in solo-play games with strong American cultural emphasis (e.g. football and basketball franchises)? Crucial in a fad-driven, highly differentiated market, EA must garner positive word of mouth.⁴³ EA possesses the underlying technical capabilities to create impressive content – graphic engines, game engines, and experienced artists & designers. Their technical proficiency surpasses that of most of the native Chinese game developers’ and represents a significant value added for EA. What it lacks is strong internal story creation capabilities – a competency even more important in Asia than North America.

Blizzard has demonstrated the viability of morphing creative intellectual property – story-line and characters – from one genre to another in their use of real-time strategy (RTS) characters from *Warcraft III* in *World of Warcraft*. It also demonstrated that expertise in game play from *Diablo II* – a RPG – could be transferred across projects. Likewise, EA should draw from its wealth of compatible storylines such as *Shogun: Total War* and *Command & Conquer* and its experience in *Ultima Online*. EA can also, to a lesser extent, continue its practice of cherry-picking creative IP from movies, etc. Identifying franchises that command consumer attention – such as Anime – in Asia will require local research. Products must appeal to local consumer habits. Because of the social element of gaming, clan building and social interaction in a game is crucial regardless of storyline. Persistent characters and trading capabilities reinforce the personal investments of customers and generate more repeat players. Themes based on historical fantasies, epic mythology, and ancient events have been highly successful. EA, potentially, has a wealth of titles it can evolve into MMOGs. In the interim, EA’s best option is acquisition.

When faced with a situation of mixed capability but very attractive market, creating a subsidiary through acquisition is the best approach.⁴⁴

	Unattractive Market	Attractive Market
Superior Capability	In-house	Subsidiary
Inferior Capability	License	Joint Venture

Purchasing a game development studio that has several successful titles but lacks the technical and marketing expertise to move to the next level of MMOG sophistication would complement EA’s strengths.

We have identified Lager Interactive as an attractive acquisition target because of its success with Chinese themed content creation and non-traditional audiences in *Fairyland Online*. Titles proven in these markets would be potential candidates for China and Korea – a judo assault into core markets. With the increasing complexity of game design and development combined with the exploratory needs of an undefined market, EA should accelerate its efforts to ensure technology sharing – for example sharing of its Renderware platform – among all its Asia bound studios. EA may also consider adopting a common online server platform. NCSoft’s successful Taiwanese distribution of *Lineage II* through native publisher Gamania⁴⁵ stresses the importance of finding native distribution partners.

EA should concentrate on being a service company when in the Asia market. This includes good customer care, constantly renewed storyline, game-play tuning, etc. – all elements often neglected in a “package goods company.” Concerted effort to make games and subscription models amendable to café settings is a must. Subscription options that allow players to buy small chunks of play-time – as opposed to the monthly subscription in Korea, USA, etc. – is another must for the more thrifty Chinese consumers. EA should consider programs to reward serious players, who are the best type of customers, in migrating to intra-company titles.

Without getting into the specifics of game design, there are several steps that EA can take to build a successful entry. Initially targeting stepping stone markets such as Taiwan, Hong Kong, and Singapore would allow EA to ease into a similar cultural climate without the risks of government censorship, uncertain access to distribution channels, etc. that fraught the mainland market.

Final Thoughts

EA should approach Asia with a two-pronged strategy that is sensitive to its strengths and weaknesses. First, EA can extend its Sims franchise to the mobile platform and target casual gamers in the more receptive Japanese and Korean markets. Concurrently, EA can target the MMOG market by acquiring native creative content and talent to merge with EA’s existing strength in technically sophisticated games.

Regardless of how EA proceeds, it must avoid past mistakes, such as emphasizing deadlines over quality. Differing revenue models and customer sensitivity in MMOGs amplified the repercussions from the premature release of the *Sims Online*.⁴⁶ A poor initial reputation dooms future subscription revenues, which constitute the core of profits. Even a weak packaged game may recuperate much of its costs in opening-week sales. MMOG players are more willing to wait for a superior game than sports gamers, who, for example, demand *Madden* with the latest NFL line-up. Because Asian sales rely less on seasonal periods, e.g. Christmas shopping, seasonal deadlines are less rigid. If EA eases its deadlines, it may also prevent costly class-action lawsuits from overworked employees.⁴⁷

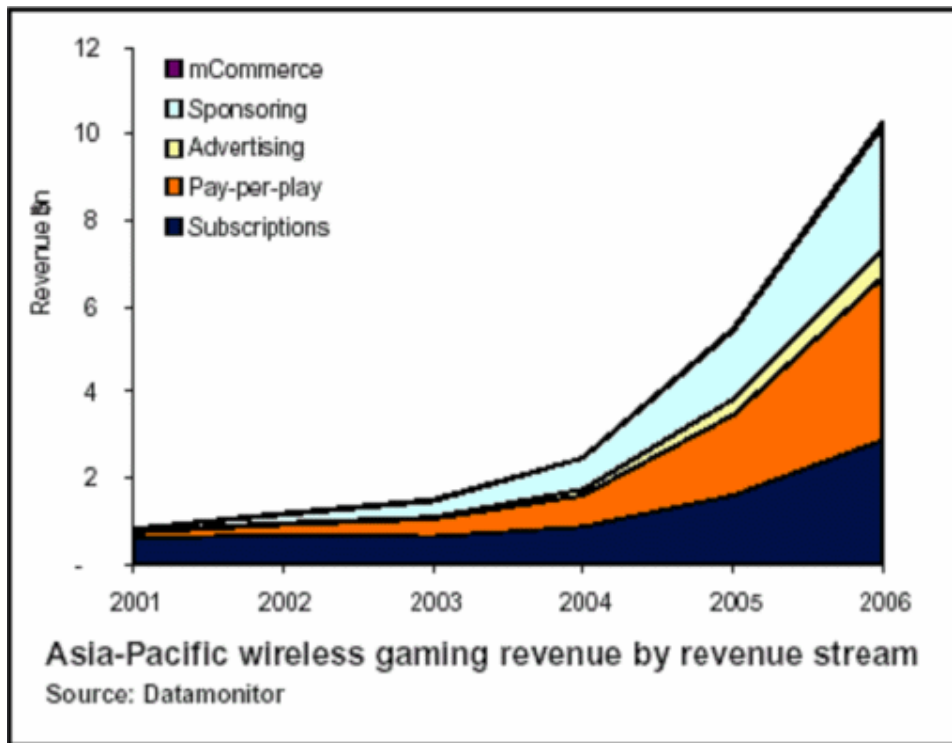
Appendix

Market Characteristics

	Korea	China	Japan	Taiwan, Hong Kong, Singapore
Teenage male population		234 million (14-24) ⁴⁸		
Disposable income				
Online game market size	\$159.7 million ⁴⁹ \$500 million ⁵⁰	\$467.8 million (2004) ⁵¹		\$170.4 million (Taiwan) \$21.9 million (Hong Kong) \$0.8 million (Singapore)
MMORPG size		76% (2004) ⁵²		
PC penetration rate (per 100 inhabitants)	49.33%	2.76% ⁵³	38.2	42.28 (Taiwan) 42.40 (Hong Kong)
Broadband penetration	25% (2004) ⁵⁴	0.2% ⁵⁵	6.2% ⁵⁶	9.4 (Taiwan) 14.6 (Hong Kong) ^{57, 58}
Broadband affordability	99% (2003) ⁵⁹	87% ⁶⁰		0.99 (Taiwan) 1.00 (Hong Kong)
Ratio mobile internet to broadband	1.69 ⁶¹		7.36 ⁶²	
Female Gamers	36.5% (online) ⁶³			47% (online gamers, Singapore) ⁶⁴
Preferred Platform	PC ⁶⁵	PC	Console	
Preferred Settings	Internet cafes (“PC Bangs”) ⁶⁶	Internet cafes (~100,000) ⁶⁷		
Preferred Genres	Group-play ⁶⁸	Historical fantasy		
Mobile	80% Internet capable. ⁶⁹ Game capable for several years. ⁷⁰	33.9% use data services. ⁷¹	11.09 million subscribers of high-speed wireless in 2003. ⁷²	
Mobile data revenues	34.2% from “games and entertainment” ⁷³	Mostly data use for news, e-mail, text message. ⁷⁴		
Piracy (measured by RIAA)	25%	91%	N/A	44% (Taiwan)

Exhibits

Wireless Gaming Growth in Asia

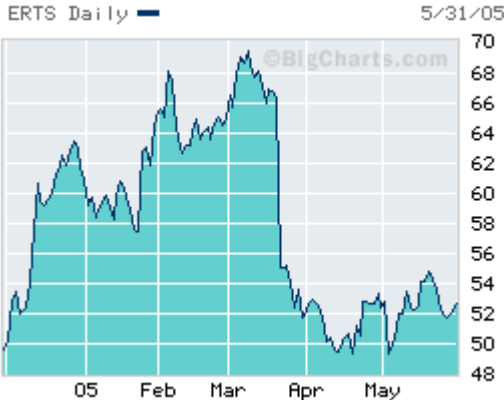


Online Game Revenue Growth

CARG – compound annual growth rate.

	2003	2008	CAGR (%)
Korea	72.5%	41.7%	25.7%
PRC	20.1%	40.3%	61.4%
Australia	2.6%	7.4%	72.9%
Thailand	2.1%	3.6%	56.4%
Malaysia	0.3%	1.7%	107.2%
Philippines	0.4%	1.4%	77.7%
Hong Kong	0.7%	1.2%	57.9%
Taiwan	0.7%	1.0%	51.9%
Singapore	0.5%	0.9%	57.2%
India	0.1%	0.8%	128.0%
Total (US\$M)	237.4	1,297.10	40.4%

EA Stock Performance



Competitor SWOT Analysis

Sony

Statistics

Sony Online Entertainment is an extremely successful massively multiplayer online game maker. Its top MMOGs, *Everquest* and *Everquest II*, generated \$500 million in profits in the first eight years and have over 300,000 subscribers each.

Strengths

SOE is skilled in developing and designing games for a variety of platforms, including PC and Mac, PSP handheld, and consoles. SOE prides itself on its rigorous quality control measures, with 500 internal testers, and numerous outside testers for each new game that is released.

In addition, they have become game-maker leaders in facilitating the “secondary market”, or the buying and selling of in-game characters, items, and coins, with the introduction of Station Exchange, where they receive a portion of sales for each item sold. Figures indicate that this market has a \$100 to 800 million dollar annual trade volume, so getting a piece of every sale is very lucrative for Sony.⁷⁶ According to SOE’s president, John Smedley, “When 40 percent of our customer service man-hours are dealing with fraud, it's in our interest to deal with it. We don't want to hide the fact that we're going to make money.”⁷⁷

Weaknesses

While SOE has done particularly well targeting games to hard-core (20+ hour-per-week) players, it is also seeking to expand its target audience. Like its competitors, EA and Blizzard, SOE seeks to expand its audience to the middle ground players—those who play less than 20 hours a week yet are willing to pay for games. With the launch of *Everquest II*, SOE included a tutorial meant to teach and attract less hard-core players, and minimal success was seen in this effort.

SOE has had a hard time entering the Asian market. It released a slightly altered version of *Everquest II* in China in 2003 with distribution partner UbiSoft China. However, it was so unpopular in China due to cultural differences in the game and differences in operating mode (many Asians prefer using the mouse, instead of the keyboard controls used in North American markets) that UbiSoft decided to stop distributing the game in China. After this failure, SOE partnered with Gamania Digital Entertainment Co. Ltd. to localize the game, and it recently began alpha testing for the new *Everquest East*, a localized version of *Everquest II*.⁷⁸

Opportunities

In addition to the Asian and wireless markets, the international play market is unfilled. MMOG players are increasingly expressing the wish to play internationally, so SOE is currently working on language translating technology that would allow this to be possible. It has been suggested that this would make it easier to enter the European market as well, where there are many little countries, but maybe not the critical mass to sustain an MMOG in one country and one language.

SOE has seen limited success in providing games to non-hard-core gamers, and even non-fantasy/medieval MMOGs so far, but it is making steps towards appealing to a larger audience and it should continue doing so.

Threats

SOE should be careful of Asian game companies entering the U.S. market. Additionally, SOE has not developed any MMOGs beyond *Everquest* and *Everquest II* that have been really successful, leaving it in a potentially vulnerable position.

Shanda

Statistics

Shanda is the most successful online gaming company in China, and is growing extremely rapidly. Its FY 2004 second quarter profits, \$36.5 million, were more than double its profits from the second quarter in FY 2003.⁷⁹

Strengths

Shanda is setting its sights beyond online games by trying to become a leading entertainment console maker and provider. The online games it distributes have seen great success, with *The Legend of Mir II* being the most popular online game in China in 2002 and 2003.⁸⁰ They have also released several fairly successful self-developed MMOGs, such as *The World of Legend*, which have not done as well as the externally-developed *Legend of Mir II*.

Shanda has a very strong position in China. Because of its early entry into the Chinese online gaming market and ultimate goal of becoming a Chinese entertainment console and provider, it has been particularly aggressive in pursuing Chinese complements. It is developing, with major industry partners, a set-top gaming box for televisions.⁸¹ This is especially important in China, where there are seven times as many televisions as PCs.⁸² Shanda has also signed a partnering agreement with China Unicom to provide its games in the 3000 new cafes C.U. will open.⁸³ This is particularly important given the fact that 60% of Shanda's players access the internet through internet cafes.⁸⁴ Additionally, Shanda has partnered with Nokia to release Nokia's new China N-Gage QD gaming mobile phone with Shanda's *World of Legend* MMOG preloaded.⁸⁵

Weaknesses

Shanda has yet to release a self-developed MMOG to top the externally developed *Legend of Mir II*. Additionally, it has not produced or distributed any non-fantasy MMOGs, leaving out some potential audiences, including females and middle ground players (non-hard core or casual).

Threats

Many companies, including EA, SOE, and NCSoft, are eying China because of the huge number of untapped game players. Many of these companies have developed MMOGs which rival, or are better in quality and content, than games Shanda has released. They have the potential to take away much of Shanda's almost exclusive current hold over the Chinese market, so Shanda should continue its self-development efforts and focus on the quality and content of its games.

Opportunities

There are still millions of players who currently do not have PCs in China, and adding them to the online gaming market through set-top boxes or any other type of technology would be very lucrative. In addition, Shanda should look to expanding to other countries in Asia where online

game play is rapidly increasing, including Taiwan and Singapore. It has already set up a U.S office, and should make sure to remember cultural issues when developing its U.S games.

NCSOft

Statistics

NCSOft is, in revenue terms, the world’s largest maker of MMOGs. Its market capitalization of ~\$1.5 billion⁸⁶ is based on ~\$530 million revenues and ~\$100 M profit in FY 2004.⁸⁷ Unlike most game publishers, NCSOft is wholly dedicated to MMOGs and has emerged atop the wave of its flagship product *Lineage* and the sequel *Lineage II* in its native Korea.

Strengths

NCSOft has mastered creating and tuning complex MMOG game-play dynamics.⁸⁸ Through *Lineage II*, NCSOft has demonstrated technical proficiency with sophisticated sound and graphics.⁸⁹ Combined with lauded creative content creation, the aura and look of *Lineage II* is “nothing short of jaw-dropping”.⁹⁰ The operational success has been repeated by NCSOft’s wholly owned American subsidiary, ArenaNet, with *Guild Wars*.

NCSOft’s mastery of the provisioning for MMOGs is another major strength. *Lineage* has for several years delivered added storyline and game-play content in dozens of chapter installments. This contrasts strongly with the growing pains of Blizzard’s *World of Warcraft*. In addition, a service infrastructure of “game masters” and 24-hour support has been implemented.⁹¹

In a market where network externalities dominate, NCSOft’s greatest strength may be a subscriber base that dwarfs all other competitors. This creates a significant entry barrier through an online world that is densely populated and provides ample opportunity for the interactive game play so sought after. Switching costs are high especially since play in Asia is socially oriented. *Lineage I & II* alone can generate ~\$208 million in revenue.⁹² Both its entrenched market power and operational know-how is demonstrated by wholesale transition of half the *Lineage* subscriber base to *Lineage II*.⁹³

	<i>Lineage</i>	<i>World of Warcraft</i>	Source
Korea (concurrent users)	300,000	60,000	94
North America (total subscribers)	60,000	800,000	95

NCSOft adds ability to replicate success abroad to its repertoire of strengths. The *Lineage* and “Korean wave” brand value has demonstrated strong currency in East Asian markets such as China, Taiwan, etc.⁹⁶ Its selection of top American game development talent and their success, under NCSOft, in developing successful games underscores managerial competency.

Subsidiary	Game	Talent	Background
NC Austin	<i>Tabula Rasa</i> (to be released)	Robert & Richard Garriott (made <i>Ultimate Online</i>)	<i>Ultima Online</i>
ArenaNet	<i>Guild Wars</i>	Patrick Wyatt, Mike O’Brien, Jeff Strain	<i>Starcraft, Warcraft, Diablo</i>

Weaknesses

NCSOFT is narrowly experienced in the MMOG – arguably MMOG fantasy combat role-playing – genre. This gives them a steep learning curve in developing other game types – e.g. the 1-50 person multiplayer action games that are holding sway in America. Its half-a-dozen titles – in production and development – do not provide the breadth of EA’s base. It also has limited experience in developing for non-PC platforms and has not demonstrated the management practices and portability in technology to cost-effectively support multiple target platforms.

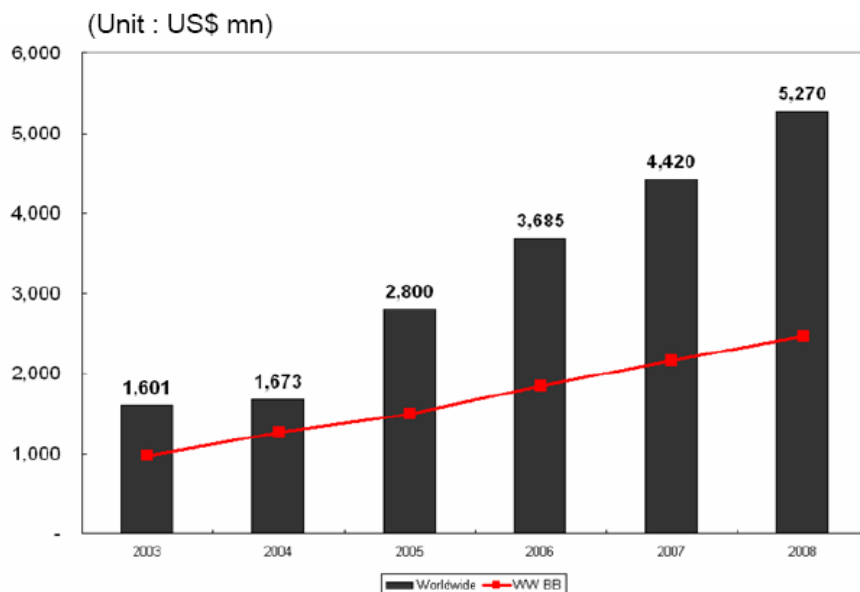
NCSOFT has a one-hit-wonder weakness that is slowly being mitigated. 72% sales still depend on *Lineage*.⁹⁷ It is also vulnerable because of geographic dependence: 47% sales are still in Korea.⁹⁸

Threats

NCSOFT is threatened by challenges to its narrow pillars of success. Blizzard’s introduction of *WoW* into Korea and China is a prime example. Games are fads at the basic level. Plans to expand are threatened by equally well funded and experienced rivals. Changes in platform preference – for example for China to adopt consoles like Japan and the US have – would outflank NCSOFT. In addition, its new subscription-less online game model with *Guild Wars* could potentially leave it with liability to support an unprofitable game.

Opportunities

Utilizing cash flow to grow in different genres and geographic markets is NCSOFT’s best opportunity. Management has identified casual games such as “*Racing, FPS, Sports, Mech Battle* etc.”⁹⁹ In addition, demographic diversification is a goal – *Alter Life* is “targeting for Female in age 10~20”¹⁰⁰ The game is exquisitely tailored to the Korean female with a marketing slogan that roughly translates to “Meet your friends. Make a family.”¹⁰¹ Success of *Lineage II* in Taiwan & China. (122,855 concurrent users) is one way to grow an international customer base. That success translates to 165% revenue growth in China over the last fiscal quarter.¹⁰² In addition, NCSOFT’s core market, MMOG PC games, continue to expand with broadband penetration.



Online Game Market and Broadband Population
(DFC Intelligence 2004, Game Industry Report by GITISS 2004)

The emergence of more powerful platforms better accentuate NCSoft's strengths in the resource intensive delivery of quality MMOGs. The ratcheting requirements of top-tier development are reflected in NCSoft's 50% and 119% increase in payroll and advertising from 2004 to 2005.¹⁰³

Lager

Strengths

Lager is strong in the creative content creation and game-play development of MMOGs. Their roots in text based multiplayer games and their success with *King of Kings* and *Pili Online* has demonstrated skill with creating online environments that can draw returning customer base. Both those titles are Chinese medieval-fantasy themed and have had significant traction in China.¹⁰⁴ *King of Kings II* emphasizes more than individual characters in persistent elements of the game, focusing instead on complex state-building. Rich storylines – especially drawn from oriental history periods – are considered essential to attracting Chinese and Taiwanese tastes.¹⁰⁵

Lager has translated their experience with MMOGs to *Fairyland Online*. This non-violent MMOG loosely based on Hans Christian Anderson fairytales has met with unusual success, especially with the elusive female audience.¹⁰⁶ 400,000 subscribers and an international distribution – notably in Malaysia and the United States – is special for a game not targeting the traditional demographics. The comparatively primitive 2.5D graphics and scarcity of violence emphasizes the strength of Lager in creating the other elements that drive MMOG success – game-play, community, story, and creative content.

Weaknesses

Lager is a game development house and lacks the marketing power and access to customer outlets to propel the game to greater commercial success. Its English website prominently announces that it is searching for a “strategic partner, who [has] experience in publishing Online Games, PC games, or any ISP associated products, in different parts of the world.”¹⁰⁷ Desperation for access to the Chinese market is evident in its joint venture with Searainbow Holding Corp, a poorly positioned distributor of online games.

In addition, all of Lager's offerings fall short of full 3-D immersive environments which are hallmarks of Korean and North American games. The 2.5D flat environments are on par with many of China and Taiwan's game offerings – including some top selling titles. The investment and financial risk requirements to create such sophisticated games seem out of reach.

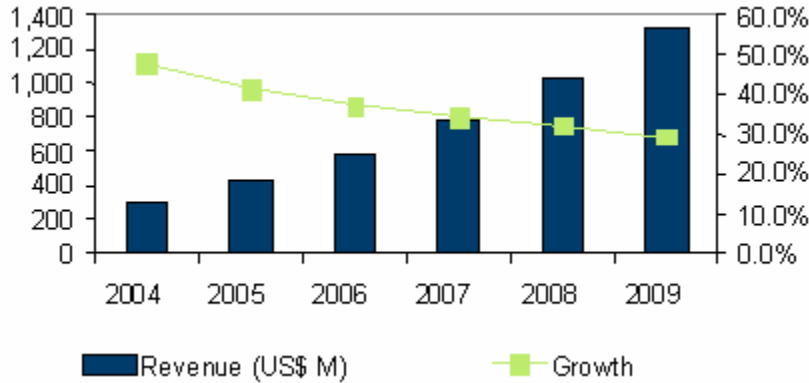
Threats

While the 2.5D primitive graphics were strengths due to lower minimum hardware requirements, they will increasingly be inadequate as user expectations and hardware inexorable march forward.¹⁰⁸ *Lineage II*'s success in China is a barometer that most Asian markets are ready for more graphically appealing games in terms of hardware. Even in smaller market segments like casual games, user tastes and expectations are likely to rise

Because two of Asia's most attractive markets are dominated by PC café's, Lager faces threats to access to distribution channels. Shanda's aggressive position in distributing its own titles, such as *Legend of Mir*, puts Lager in a precarious position.

Opportunities

Growth in the Chinese and Taiwanese MMOG markets is Lager's biggest opportunity. It is a native player in terms of culture and environment. The graph below shows China's projected growth and revenues in the online gaming market.



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Creating a market demand through products that lure non-traditional customers has potential to capitalize on a less crowded market. Female gamers in particular have been elusive. *Fairyland's* success may offer an opportunity to refine the necessary content to attract female gamers. However, realizing these opportunities requires elements of marketing and profile that Lager cannot command on its own.

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