

The Future of the GameStop Shop

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ABSTRACT

David Yang is the owner of a GameStop store located in Danbury, Connecticut. Over the past ten years, the sales of his shop have declined steadily. In an effort to determine how different product segments are affected by online shopping, David asked his friend, Dr. Youngbin Kim, to analyze the accounting materials he provided as well as the annual reports. After conducting a thorough investigation, Dr. Kim provided several suggestions.

Keywords: GameStop's Failure, GameStop's Online Strategy, Challenges of Brick-and-Mortar Retailers, Strategic Decision-Making, Video Game Industry

INTRODUCTION

David Yang was the owner of a GameStop shop located in Danbury, Connecticut. He successfully ran this shop for two decades, starting from the early 2000s, inside Danbury Fair, which is the second-largest shopping mall in Connecticut. During the first decade, his business grew steadily, with 150 million units of PlayStation 2 and 80 million units of PlayStation 3 sold globally during the 2000s. As more customers bought game consoles like PlayStation or Xbox, GameStop was able to sell more games as well. However, during the second decade, David's shop faced fierce competition from online shopping malls, unlike many other retailers in the shopping mall.

David's retail business has been affected by the rise of online shopping malls. He wants to identify how online products are hurting his business in detail. His store sells four different types of products. The first category is hardware, which includes gaming consoles like PlayStation or Xbox, as well as gaming accessories like headsets and controllers. The second category is new game software, which is typically priced at \$70. The third category is second-hand game software, which ranges in price from \$10 to \$50, but on average, customers pay half the price of new game software. The final category of products is collectible goods such as t-shirts, trading cards, and toys.

David believes that different segments of his store are facing different levels of competition from various online stores. To help him analyze his store's competitive position, David has reached out to his friend, Dr. Youngbin Kim.

BIRTH AND RISE OF GAMESTOP

In 1984, James McCurry and Gary Kusin, who were classmates at Harvard Business School, started an electronics store in Dallas, Texas called Babbage's. The store was named after Charles Babbage, the English mathematician who invented the first mechanical computer. Initially, Babbage's focused on selling software and hardware for home computers, which were becoming increasingly popular at that time. However, the company soon shifted its focus to video game sales, which made up two-thirds of its sales by 1991. To expand its reach, Babbage's acquired other small video game and software retailers. As of 1992, the company had over 200 stores across the country.

In 1999, Barnes & Noble, the book retailer, acquired Babbage's for \$215 million. Barnes & Noble also bought Funco, another video game retailer and entertainment software seller. Later, Babbage's merged with Funco to create a new entity named GameStop Corporation, which was officially formed in 2000. GameStop went public in February 2002 at the New York Stock Exchange.

GameStop experienced significant growth and expansion through both organic development and strategic acquisitions. It aggressively acquired several video game and software retailers to expand its retail footprint. As a result, GameStop became one of the largest video game and entertainment software retailers worldwide. As of February 2020, GameStop has a total of 5,509 physical stores across 14 countries. In addition to its acquisitions, GameStop capitalized on the used game market by allowing customers to trade in their old games for store credit or cash. Additionally, to attract loyal customers, GameStop often offered exclusive merchandise, such as limited-edition games and collectibles, and hosted special events.

Between 2009 to 2016, GameStop had its highest revenue record, with an average of \$9 billion per year. In 2012, the company's revenue hit an all-time high of 9.5 billion. However, the sales started declining due to the increase in digital downloads and online competition. Nowadays, users prefer to purchase games through their console's digital shops.

FALL OF GAMESTOP

GameStop was indeed confronting significant challenges in its core business. The company operated as a brick-and-mortar retailer focusing on selling video games, gaming consoles, and related accessories. However, several factors were negatively impacting its operations.

GameStop faced competition not only from traditional brick-and-mortar retailers but also from digital marketplaces and online retailers. The convenience of online shopping and the availability of digital storefronts for game purchases provided consumers with alternatives to physical stores. Platforms like Xbox Live, PlayStation Network, and Steam contributed to a decline in the sales of new and used physical games at GameStop stores.

GameStop attempted various strategic initiatives to adapt to the evolving landscape, including diversifying its product offerings and investing in e-commerce. However, the pace of these adaptations was perceived as insufficient in response to the rapid changes in the industry.

The short squeeze, driven by individual investors organizing through online communities like Reddit's WallStreetBets, brought GameStop into the spotlight and had a temporary impact on its stock price. However, the fundamental challenges in its business model persisted, and the company continued to face the ongoing need to adapt to the evolving gaming market.

Over the course of five years, GameStop's revenue underwent a tumultuous journey as indicated in Table 1 (Appendix). After a 3.06% decrease in 2018, the company experienced a sharp decline of 21.96% in 2019, which continued with a 21.28% drop in 2020. The combined impact of these decreases highlights the challenges that GameStop faced due to the gaming industry's shift toward digital gaming and e-commerce. However, in 2021, GameStop experienced a significant turnaround with an 18.09% increase in revenue. This growth was partially attributed to strategic changes and a surge in retail trading fueled by social media that brought GameStop into the global spotlight. In 2022, the revenue growth stabilized with a slight decrease of 1.39%, indicating that the company may be finding its footing amidst the changing retail landscape.

GameStop's net income paints a different picture of the company's financial health. Despite the increase in revenue in 2021, the company has reported a net loss every year. The losses peaked at -\$673,000,000 in 2018 and were reduced in the following years, reaching -\$215,300,000 in 2020. However, the net loss increased again in 2021 to -\$381,300,000, before slightly improving to -\$313,100,000 in 2022.

As indicated in Exhibit 1 (Appendix), GameStop's stock price journey between 2018 and 2022 is a remarkable story marked by volatility, market dynamics, and the unprecedented influence of retail trading. In 2018, GameStop's stock experienced a downward trend reflecting the company's declining revenues and the challenges faced by brick-and-mortar retailers. The stock opened the year at around \$4.67 and continued to decline steadily, with a closing price of approximately \$3.81. The decline continued into 2019, with the stock hitting a low of \$0.83 in August, driven by declining sales and increasing losses. However, in 2020, the stock began to

show signs of upward momentum, opening the year at around \$1.36 and remaining relatively stable until late August. This growth was partly attributed to the announcement of a strategic partnership with Microsoft and a shift in the company's board, signaling a potential turnaround for the business. The stock closed the year at \$4.71.

GameStop's stock was one of the major highlights of 2021. This was due to the surge in retail trading, which was fueled by social media platforms like Reddit. The stock experienced unprecedented volatility as its price skyrocketed from \$4.42 in early January to an all-time high of \$86.88 on January 28th. This extraordinary movement was characterized by high trading volumes and brought significant attention to the phenomenon of "meme stocks." Although the stock eventually stabilized, it remained volatile throughout the year, closing 2021 at \$37.1. In 2022, while the stock did not reach the extreme highs of the previous year, it continued to experience volatility. The stock price ranged from approximately \$18.46 to \$41.25, reflecting ongoing interest from retail traders and the market's uncertainty about GameStop's future. Investors discussed the company's efforts to transform its business model and embrace digital trends.

DISCUSSION

Dr. Kim sat down in his office and tried to understand the revenue structure of David's shop. And he also downloaded and read the annual reports of GameStop. GameStop categorized sales of products into 3 segments.

Hardware and accessories. We offer new and pre-owned gaming platforms from the major console and PC manufacturers. The current generation of consoles include the Sony PlayStation 5, Microsoft Xbox Series X and the Nintendo Switch. Accessories consist primarily of controllers, gaming headsets, and virtual reality products.

Software. We offer new and pre-owned gaming software for current and certain prior generation consoles. We also sell a wide variety of in-game digital currency, digital downloadable content and full-game downloads.

Collectibles. Collectibles consist of apparel, toys, trading cards, gadgets, and other retail products for pop culture and technology enthusiasts, and our digital asset wallet and NFT marketplace activities."

GameStop is often perceived as a game retailer, but it is primarily a hardware store rather than a software store. As indicated in Table 2 (Appendix), in 2022, only 31% of its revenue was generated from game software sales, whereas the remaining 69% came from the sales of hardware and collectibles.

David provided annual reports and other accounting materials to Dr. Kim for analysis of each product segment of the shop. The first segment, hardware and accessories, generated more than half of the revenue. However, due to the increasing popularity of online shopping, hardware sales have been declining steadily. Additionally, customers tend to buy games more frequently than game consoles. For instance, PlayStation 4 owners did not purchase a new console until the release of PlayStation 5 in 2020, seven years after the release of PlayStation 4 in 2013. Based on this, Dr. Kim estimated that an average customer purchases a new game console every seven years.

The second product segment is new game software, while the third product segment is used game software. Unfortunately, these two segments have experienced the biggest decline in sales. As indicated in Table 2 (Appendix), In 2017, they generated 50% of the revenue, but by

2022, this had dropped to only 31%. The reason for this decline is that every game console produced in the 2020s comes with a fast Wi-Fi connection, and major companies like Sony or Microsoft have created their own online game stores. As a result, more and more console players are opting to buy and download new games from the comfort of their homes, rather than visiting physical stores like GameStop. In fact, in 2020, Sony even released an internet-only version of the PlayStation 5, which cannot play any game software purchased from GameStop.

The third segment of products, which is used game software, is more popular than the second segment. This is mainly because it is cheaper than buying new game software. While a brand-new console game can cost a customer around \$70, a second-hand game costs only \$10 to \$50. At GameStop, customers can either buy or sell used game software. People who are interested in this segment are the most frequent visitors to the shop.

The "collectibles" product segment was a rising star in GameStop's shop, consisting of apparel, toys, trading cards, gadgets, and other retail products for pop culture and technology enthusiasts. Unlike other segments, which continued to lose sales, the collectibles segment experienced a consistent increase in sales over the last few years. Due to the fact that most customers for this segment prefer to physically examine the product before buying, it was relatively free from competition with online shopping.

DISCUSSION QUESTIONS

Question 1: In order to avoid competing with online shopping malls on price, Best Buy opted to provide a variety of customer experiences within its large retail stores. Can GameStop replicate this strategy?

Question 2: Several companies, including Microsoft, have launched game subscription services. Similar to Netflix subscribers, members of these services can download and play any games available on an online server. This new trend raises questions about how it will impact the sales of video games at retailers like GameStop. Specifically, it remains to be seen which type of games sales will be affected more by the rise of subscription services: new games or used games.

Question 3: David Yang wants to invest more in the collectibles segment. How should he boost the sales of collectibles?

INSTRUCTOR MANUAL

Following are possible discussion topics and answers to questions.

Discussion Question 1: Online game shopping has one major disadvantage - a customer cannot test the game before buying it. This is where having a showroom can add immense value for potential customers. However, most GameStop stores are considerably smaller than Best Buy stores, making it challenging for GameStop owners to secure the necessary space to set up a showroom.

Discussion Question 2: Game subscription services like Game Pass offer older games for free like Netflix. This can have a negative impact on the sales of used games more than new ones. However, Microsoft has recently been actively acquiring well-known game firms such as Mojang (*Minecraft*), Bethesda (*Doom*, *Fallout*, *the Elder Scrolls*), and Activision Blizzard (*Overwatch*, *Call of Duty*). If Microsoft allows subscribers to play new games from these firms without additional costs, it could have a huge negative effect on new game sales.

Discussion Question 3: Many game enthusiasts tend to spend more money on limited edition collections. Having collectibles such as toys, apparel, and trading cards available only at GameStop stores is crucial to boosting sales.



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APPENDIX

Table 1: Revenue of GameStop

Year (fiscal)	Revenue	Growth Rate	Net (Loss) Income
2022	\$5,927,200,000	-1.39%	-\$313,100,000
2021	\$6,010,700,000	18.09%	-\$381,300,000
2020	\$5,089,800,000	-21.28%	-\$215,300,000
2019	\$6,466,000,000	-21.96%	-\$470,900,000
2018	\$8,285,300,000	-3.06%	-\$673,000,000

(Source: GameStop Annual Report 2022, 2021, 2020, and 2019)

Exhibit 1: The Stock Prices of GameStop



(Source: <https://finance.yahoo.com/quote/GME/>)

Table 2: Sales of GameStop

	Fiscal		
	2022	2021	2020
Hardware and accessories	\$ 3,140.0	\$ 3,171.7	\$ 2,530.8
Software	1,822.6	2,014.8	1,979.1
Collectibles	964.6	824.2	579.9
Total	\$ 5,927.2	\$ 6,010.7	\$ 5,089.8

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