The Need for Innovation

by Andrew Cardno

Innovation is bringing about a massive sea change in your gaming landscape. This massive sea change directs how your industry innovates. The effectiveness of this innovation will in many ways define the vibrancy of your business in years to come.

> *"The most effective way to manage change successfully is to create it. One cannot manage change. One can only be ahead of it. In a period of upheavals, such as the one we are living in, change is the norm. To be sure, it is painful and risky, and above all it requires a great deal of very hard work. But unless it is seen as the task of the organization to lead change, the organization will not survive. In a period of rapid structural change, the only ones who survive are the change leaders. A change leader sees change as an opportunity. A change leader looks for change, knows how to find the right changes and knows how to make them effective both outside the organization and inside it. To make the future is highly risky. It is less risky, however, than not to try to make it. A goodly proportion of those attempting to will surely not succeed. But predictably, no one else will."* – Peter F. Drucker

To be impactful in business and more broadly in the tribal gaming industry, innovation needs to be impactful in both quality and scale. One of the best ways to be impactful at scale is for your innovations to drive change horizontally across the business. This kind of broad scale innovation is called Horizontal Innovation.

Your end customer experience is, in many cases, a mixture of influences from many suppliers. Consider your customers today. They can play on a game made by one game designer on a gaming machine made by one supplier, using a customer management experience and secondary gaming device from a second supplier, a bonusing system from a third supplier, and a ticket printer from a fourth supplier. Your customers experience the gaming device as a whole, and simply have no idea that the gaming experience is provided by an amalgam of suppliers.

Before digging further into the implications of the horizontal innovation model for your gaming business, first look at how this model has worked historically in related industries.

Horizontal Innovation in Video Games

The video game industry is an extraordinary example of the emergence of a new technology and how the entire industry subsequently grew and changed. It also illustrates how change often impacts an entire industry rather than specific players. Now, there is little doubt that the video game industry has thrived, and according to Newzoo, reached $137 billion in 2013.

The arcade industry, however, has suffered a different fate.

In the early 1980s, the arcade industry was having a golden age, having developed into a $14 billion industry in the space of just a few years. However, today video arcades are a small fraction of what they once were, with a few notable exceptions.

In the late 1970s in Little Rock, Arkansas, Buster's restaurant sat side by side with Dave's arcade. In the height of the video arcade golden age, these businesses decided to merge offerings to become Dave & Buster's. This is a clear example of change leadership showing that the combination of products could be a winner. While the arcade industry collapsed, Dave & Buster's thrived by staying ahead of the change, proving the value of being a successful change leader.

What is even more interesting is that this innovation in building Dave & Buster's was a clear example of horizontal innovation. To be specific, it was not the gaming product on its own that enabled Dave & Buster's to thrive – it was the combination of entertainment offerings that brought about this success, a perfect example of horizontal innovation.

Horizontal Innovation in Food Services Industry

Despite the Great Recession and the sophistication of take-home prepared meals, the restaurant industry has thrived over the last decade. According to the National Restaurant Association, 2018 sales were predicted to reach $825 billion, with "2018 being the ninth consecutive year of sales growth for the restaurant industry."

While continued moderate growth is predicted, the past figures have been quite remarkable, and the big question is why? Looking at the industry a little deeper shows that it has undergone tremendous change – and that innovation seems to be driving the entire industry. Events such as the Restaurant Innovation Summit showcase new technology, such as home delivery, electronic menus and even robotic delivery. Innovation is driving success and is being fully embraced by the restaurant industry.

A Change-leading Industry

The world is changing at a rate that is nothing short of astonishing, and entire industries are emerging and dying. It is prudent to heed Peter Drucker's advice: "In a period of rapid structural change, the only ones who survive are the change leaders." The form of this change leadership is of critical interest. Consider two different forms of innovation:

• *Change-Leading Organization* – Where an individual company such as Dave & Buster's leads the change. Now, it is dangerous to say that innovation can bring about success in any industry, and in the case of the amusement arcade industry, it could be that the shift to home gaming systems was inevitable.

However, innovation was a key factor in determining who survived the shift.

• *Change-Leading Industry* – Where the entire industry becomes a change leadership industry. The restaurant industry is a great example of this; it has grown to now employ 10 percent of the U.S. workforce, and it is an industry of tremendous and constant innovation.

The critical difference between the change-leading organization and the change-leading industry is where the growth comes from. In a change-leading organization, the growth can – and often does – come from other competing organizations. In a shrinking industry, it might be the last organization standing. Conversely, in a change-leading industry, the entire industry grows. It is reasonable to say your gaming industry offering is competing with other entertainment offerings.

Innovation Spend

Innovation is a remarkably expensive exercise in which enormous capital amounts are deployed. The R&D spend by top innovators in the U.S. ranges from less than 1% to 9.5% of revenue. It is reasonable to expect standout industries such as healthcare and computing and electronics, who are investing over 5 percent of their revenue on R&D, to show substantial growth in upcoming years. This investment shows how these industries are committed to change.

Innovation Soup

Bringing this all together, your innovation can be characterized as:

• Industry change leadership is more desirable than individual change leadership. If your industry functions to drive innovation, your whole industry can and often does grow as a result. In other words, it is better to grow your pie than to carve up a smaller one.

• Innovation requires you to develop a risk-taking culture. Risk taking is fraught with failure-and learning from this failure. To quote Thomas Edison, "I have not failed. I've just found 10,000 ways that won't work."

• Innovation is expensive, and other competing industries are investing heavily in change. For example, customers may choose an innovative new dining experience over a gaming experience (though of course we would encourage them to enjoy both). This brings us to the innovation soup that is necessary to bring about growth to the industry. This innovation soup will require a lot of hard work, money and commitment to change leadership.

Game Replacement Practice

Slot machines are the backbone of the U.S. gaming market. To gain an understanding of where the gaming industry is headed, let's run a simple scenario of replacement and see what the industry could look like in 2024. There are over 900,000 slot machines in the U.S. gaming market today, assuming a replacement of 50,000 units and a random replacement pattern (this is not unreasonable, as often properties with newer games replace those games) as slot machines continue to age. Each year the industry adds approximately six months to the mean age of machines.

Clearly, this not a sustainable model. Your players cannot be expected to continue to partake in gaming entertainment activities when your product just keeps getting older. Of course, there are some exceptions for games that seem to be classics such as video poker. But these exceptions aside, the answer is clear: the gaming floor needs to become the center of innovation.

Gaming is in many ways much like the restaurant industry in that it is very fragmented. In Indian gaming, it is common for a property to exist as a standalone business and not affiliated as part of any chain. In this highly fragmented environment, oftentimes innovation comes from vendors. They strive to become high-growth companies with new innovations bringing about massive change in the industry. In this role, vendors are like catalysts for change across the whole industry. A successful vendor may change the whole way the industry operates and bring the innovation you need to become a change leading player.

Gaming vendors in many cases are spending aggressively on R&D. What your vendors need are operating partners to be risk sharers of new innovative technologies. In your role as a risk sharer, you can shape and mold the future of these new technologies, and in addition, you will have a competitive advantage over your competitors who are slow to adopt change.

The Opportunity is Yours

The good news is that you are working in a comparatively cash rich and growing industry. The industry is constantly changing and evolving to meet new market changes. However, you now stand at a critical crossroads. Vendors need to take more risks, learn from their failures, and bring about the industry change leadership that will ensure the future of the gaming industry remains bright. ♣

Andrew Cardno is Founder & Chief Technology Officer at VizExplorer. He can be reached by calling (858) 217-4886 or email andrew.cardno@vizexplorer.com.