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At Sony, Rivalries Were Encouraged; Then Came iPod

Failure of Broad Cooperation Showed Flaws in Model; A Struggle Over Piracy

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A year ago, Howard Stringer watched helplessly while Sony Corp. fumbled the launch of its online music business.

As head of Sony's U.S. operations, Mr. Stringer had championed a plan for a service, dubbed Connect, to compete with Apple Computer Inc.'s popular iTunes store. But he ran into a problem that was all too common at the electronics giant: Different groups within Sony handled different parts of the service, and they didn't work well together.

The software to organize the downloaded music was made by the Tokyo-based personal-computer group, but it didn't always work smoothly with the new versions of Walkman music players created by the Japanese portable-audio team. That team, in turn, was out of touch with the teens and Web surfers who buy music online in the U.S. By the time Mr. Stringer's Tokyo bosses stepped in to fix the problem, Connect had flopped after its launch in May 2004.

"It took a crisis" for Tokyo to respond, recalls Mr. Stringer.



Howard Stringer

Now, Mr. Stringer has another chance to get it right. Last week, Sony shareholders officially placed the 63-year-old former TV news producer in Sony's top executive post, after a remarkable March management shake-up that saw previous Chief Executive Nobuyuki Idei and President Kunitake Ando offer to step down.

Mr. Stringer, the first foreign CEO to lead Sony, has the daunting task of installing order and direction in a company plagued by confusion and poor leadership. He will be fighting 50 years of history: Sony has long thrived on a hyper-competitive culture, where engineers were encouraged to outdo each other, not work together. Some employees still boast they don't follow orders they don't agree with. That approach created one monster hit after another, from the Walkman to the PlayStation videogame machine, turning Sony into one of the most successful global brands of the past few decades.

But recently, as the company ballooned in size and the number of its competitors increased, the infighting has led to costly mistakes. Rival electronics divisions within Sony pumped out competing products with little guidance from above. Sony's units -- from televisions to insurance -- bucked strategy imposed by their corporate bosses.

The malaise is clearest in Sony's electronics division, which accounts for 70% of the company's revenue. Last year it reported an operating loss for the second straight year as competition pummeled prices for key products, such as TVs and Walkmans. Sony's reputation as an innovator is also suffering as the snazziest gadgets from competitors, like the iPod and the TiVo digital video recorder, increasingly depend on the specific juggling act that Sony can't do well: integrating hardware, software and services.

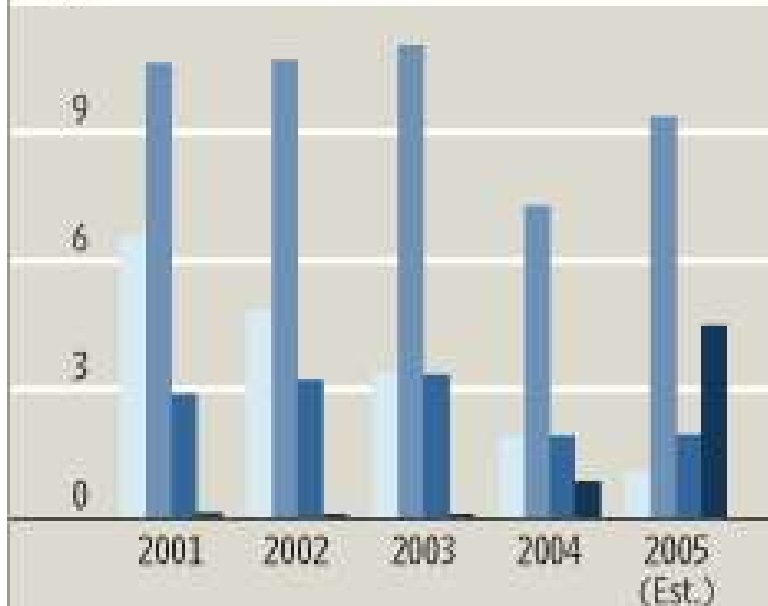
Mr. Stringer has said he'll announce his turnaround plan in late September and won't reveal any details before that. People familiar with Mr. Stringer's thinking say one tactic will be to streamline management and products, merging formerly separate groups so they're forced to talk to each other. "It's about...the number of silos," said Mr. Stringer at a news conference last week, referring to Sony's highly autonomous business units. "It's impossible to communicate with everybody when you have that many silos."

Listeners' Choice

Sony's Walkman music players have struggled to respond to the success of Apple's iPod. World-wide unit sales, in millions:

Legend:
Cassette Walkman (light blue)
CD Walkman (medium blue)
MiniDisc Walkman (dark blue)
Flash-memory and Hard-disk Walkmans (darkest blue)

12



Note: Figures are for the fiscal year ending March 31
Source: the company

An early indicator of whether Mr. Stringer can instill teamwork will be the Connect service and the revamped Walkman line that is crucial to its success. Both are scheduled for a relaunch before the end of the year. Although Sony has plenty of businesses that are bigger and sicker, few reflect the current sprawl and dysfunction of the group as well as Connect.

"All the complexities of Sony are compressed into" Connect, says Koichiro Tsujino, a Japanese engineer who last year was tapped to be co-president of the unit responsible for the online music operation and the music players that will link to it.

Connect was born in early 2003, when Mr. Stringer got a visit from Philip Wiser, then chief technology officer for Sony Music in the U.S. Mr. Wiser, 38, had helped found the pioneering online music service Liquid Audio in 1996. Now, he wanted to build a music-download service for Sony that could compete with Apple's iTunes online music store, which was about to start up.

Sony already had a long, bumbling history with online music. As early as 1998, when college students were starting to load music files onto their computers and exchange them over the Internet, Sony had considered bringing out digital-music devices and online services. But there were big differences of opinion: The PC and Walkman groups each had their own products and technologies they wanted to push. And Sony's U.S. music unit -- formed with the purchase of CBS Records in 1988 -- was afraid its sales would be hit by free music downloads. It wanted to hold off on everything until strict antipiracy measures were ready.

Mr. Idei, then president of Sony, helped broker a compromise, in which electronics would wait a year to put out its gadgets and incorporate the copy protection the music unit wanted. But nobody was completely satisfied. Privately, many electronics engineers complained the copy-protection measures were too strict. In the end, many parts of Sony came out with different devices and services at their own pace. Both the PC and Walkman groups put out rival music players, while Sony Music in Japan, Sony Music in the U.S. and Sony Electronics in the U.S. all had their own music portals or download services.

Mr. Wiser asked Mr. Stringer to let him put together something more coherent. "We can do this in nine months," Mr. Wiser recalls urging. "We've got the product, hardware, software."

Mr. Stringer agreed. He wanted to show that Sony could integrate its software, services and music players in an elegant way -- at a time when more and more people were praising Apple's simple-to-use iPod player and iTunes music-jukebox software, which organizes and plays digital-music files.

But Messrs. Stringer and Wiser had authority over only the services part of Connect. Sony's PC software and music players were controlled by engineers in Tokyo. And Mr. Wiser started running into the same problems that had dogged Sony's previous online-music efforts: The company's diverse divisions didn't like working together.

Sony's electronics dons in Japan eventually agreed to help with the Connect project. But their priorities for gadgets didn't always match those of the Connect service. Some Tokyo engineers say privately that they remain wary of listening too closely to Sony's entertainment units, whom they blame for obstructing new electronics products by worrying too much about piracy.

Mr. Stringer sent Sony executives emails and letters complaining that the company's jukebox software -- created by programmers in the Japanese PC division -- was clunky and hard to use, say people familiar with Connect. But nothing happened. A Sony spokesman in Tokyo says the division didn't have time to make changes given Connect's tight deadline.

On the gadget side, U.S. marketers pushed for a version of the Walkman that stored music on a little hard disk, like the wildly successful iPod, as well as Walkmans capable of playing music files encoded in the MP3 format, the de facto standard in the U.S.

The Walkman division was run by an old-school Japanese engineer named Takashi Fukushima. He was known as a perfectionist who pushed his engineers to reduce the number of screws in gadgets.

Instead of a hard disk, Mr. Fukushima initially opted to have the Connect-linked Walkmans use a high-capacity version of the MiniDisc, which stores music on a removable cartridge and is popular in Japan but never took off in the U.S., say people close to the Walkman division. When Mr. Fukushima's team finally made a hard-drive Walkman, he said in an interview that hard-drive gadgets "aren't interesting" because "anyone can make them."

Mr. Fukushima also didn't make the new Walkman play MP3 files, sticking instead with a proprietary technology called Atrac that was developed for the MiniDisc. Mr. Fukushima declined to comment for this article.

Even within the electronics division, various arms worked at cross-purposes. Both the Walkman and PC groups launched their own hard-drive music players within a month of each other -- without coordinating on product-planning or marketing. At the time, some executives said such duplication was part of Sony's tradition of healthy internal rivalry.

Mr. Wiser was philosophical about the difficulties in coaxing the various units to change their products for Connect. "We took a bunch of things that were already there and glued them together," he says. If Sony had tried to get everything perfect from the start "we never would have gotten it done."

But outside Sony, the view on Connect and the "iPod-killer" Walkman wasn't so sanguine. Reviewers panned them for everything from their reliance on Atrac to their clunky interfaces.

Messrs. Stringer and Wiser took the opportunity to push for improvements across the board. Mr. Stringer emailed a [negative review](#) from The Wall Street Journal's Walt Mossberg to top Sony executives in Tokyo, say people familiar with Connect. To his surprise, Mr. Stringer found that the executives hadn't realized things were so bad, these people said.

Faced with a public-relations disaster, Messrs. Idei and Ando took action. In November, they set up a separate company, which was also called Connect, and got a

veteran Japanese engineer to help run it. Their choice was Mr. Tsujino, 47, a polished English-speaker who had overseen Sony's successful DVD recorder line.

Mr. Tsujino had worked all over the Sony empire -- in PCs and TVs, both in Japan and the U.S. He knew Mr. Wiser. And until recently, he had been working with both the software and services groups on Sony's version of the TiVo. That was just the kind of cross-company cooperation called for in Connect.

Mr. Tsujino agreed to help with Connect. But he had one condition: He needed control of both software and hardware to make it succeed, people close to Connect say. Mr. Idei promised to move all the necessary divisions into the Connect company, and appointed Messrs. Tsujino and Wiser as co-presidents.

With their new authority, Messrs. Tsujino and Wiser started reorganizing the business. They asked a Sony software team in San Jose, Calif., to revamp the music-jukebox software previously handled in Tokyo. Mr. Tsujino began directing a redo of Sony's hard-drive Walkmans, which had been brought into the Connect company.

Then Mr. Tsujino heard some troubling news: A Walkman team that made flash-memory players -- tiny devices that store music on memory chips -- wouldn't be coming to the Connect company as promised. Instead, it would be moved, along with Mr. Fukushima, to another division. Sony insiders speculate that Mr. Fukushima was reluctant to part with the team. Sony declined to comment on the maneuvering.

Mr. Tsujino went to Mr. Idei to demand an explanation, say people familiar with the events. He found that Mr. Idei hadn't known about the move, the people say. The transfer of the flash-memory players out of Connect's orbit went through in February. Sony declined to make Mr. Idei available for an interview.

In March, Mr. Idei said he'd step down and hand over the reins to Mr. Stringer, amid a worse-than-expected slump in electronics earnings. Contributing to that slump, Sony executives say, was the poor performance of the Walkman line, whose CD and MiniDisc players were seeing their share eroded by the iPod.

Some of the organizational disarray is now receding, Sony insiders say. In mid-April, Connect finally managed to win control of the flash-memory Walkman group. The PC group quietly stopped production of its rival hard-disk portable audio device in May.

Sony's new flash-memory Walkmans, fashioned to look like little perfume flasks, have been top sellers in Japan -- beating Apple's equivalent iPod -- since they were launched in April. Its latest line of hard-drive Walkmans is starting to take share from hard-disk iPods in Japan as well, according to sales tracking service BCN Inc.

People close to Connect say Sony is pushing hard to roll out in the fall a fully revamped version of the Connect service, complete with jukebox software, a retooled Walkman and a video-download service. Connect is also working with the videogame and cellphone groups, in a stab at true cross-company cooperation.

Some people close to Connect say cross-Pacific communication is still tough, and tensions inside the company remain high -- particularly between the Japanese hardware engineers and the U.S. music and software teams.

"Sony's gotten so big that things don't connect any more," says Yukio Hata, an executive at Sony Music Japan who oversees a Japanese music-download service allied with Connect. "They've got to get connected again. That's the mission of Connect."

--- *Kate Kelly and Ethan Smith contributed to this article.*

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