



INVEST | THE CORNER OFFICE

Ready Player One

The maker of Grand Theft Auto wants to carjack the video game market in 2012.

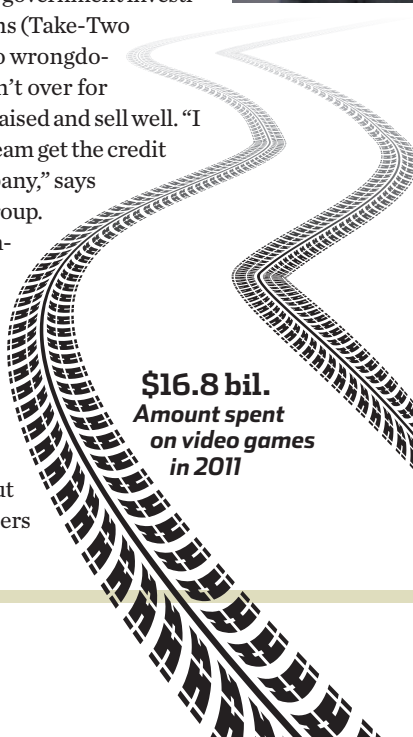
By Linda Lacina

CONTRARY TO popular belief in the video game world, Take-Two Interactive Software hasn't delayed the launch of *every* game it's made—more like half the games, the firm says. Its western game Red Dead Redemption was held up for several months. Grand Theft Auto IV was pushed back six months. Even its popular detective game L.A. Noire, for which developers spent months meticulously re-creating 1940s Los Angeles, was delayed four times. Gamers want “groundbreaking art,” says the firm's boss, Strauss Zelnick.

Investors aren't as enthralled. Since Zelnick arrived at Take-Two in 2007—he began as chairman of the board, then took the CEO job last year—the firm's stock has dropped about 25 percent. “We're judged by the stock price—that's fair,” Zelnick says. Thanks to another game delay, on Max Payne 3, the firm is likely to post a loss in its fiscal year ending this spring. Zelnick has mostly avoided social games (think FarmVille), which are usually cheap to develop; instead, he is banking on immersive games that can cost \$50 million each and take three years to produce.

That approach can be risky in today's \$16.8 billion game business. Americans are spending less on games—sales fell 2 percent in 2011—and few foresee much growth until 2013. Zelnick, a long-time music and movie executive, inherited government investigations into the firm about its stock options (Take-Two paid a \$3 million penalty and admitted no wrongdoing). Still, many analysts say the game isn't over for Take-Two; its products are often highly praised and sell well. “I don't think that he and the management team get the credit they deserve for turning around the company,” says Ben Schachter, an analyst at Macquarie Group.

Surprisingly, the 54-year-old doesn't consider himself a gamer. But he is optimistic Take-Two's best years are ahead of it, thanks to its slate of games, most notably Grand Theft Auto V. We caught up with Zelnick at the firm's headquarters, where the lobby is guarded by a statue of Big Daddy, a villainous, scuba-gear-wearing giant from its game BioShock. Zelnick talked about Take-Two's delays and how his top customers will soon be 50-year-olds.



\$16.8 bil.
Amount spent
on video games
in 2011

In the game industry, it's not even a surprise anymore when you delay a game. Why are they often late?

We've had a lot of slippage this year. We could have said, “Throw it in the box and ship it”—we just didn't think we'd get a good result. We slipped on Red Dead Redemption in 2010, and we still sold 6.9 million copies in nearly five months. Long-term, the market is pretty forgiving.

But who cares that L.A. Noire perfectly rendered the streets of 1940s Los Angeles?

You have to have a willingness to invest in an authentic, creative underpinning, an A+ product, because when you talk to

GROOMING BY NIKKI WANG



analysts, an A- product is a D- product. There are lots of solid games, damn good games, but they're overlooked [by critics and gamers].

Increasingly, games are being downloaded off the Internet instead of bought at stores. How does that affect Take-Two?

Digital is 10 to 15 percent of our business. Over time, it's kind of hard to believe the whole business won't go digital. But it doesn't really matter. We will have intermediaries for digital stores, just as we've had intermediaries for physical stores; that's not going away. The profit margins aren't much different.

Why did you issue \$250 million in convertible debt in 2011? The firm's market value is only \$1.4 billion.

We don't have an immediate need for it, but given that the interest rate, 1.75 percent, is so low, it isn't that burdensome. We also feel like we've reached a level of maturity where we could contemplate some big strategic moves that might use capital, and we wanted to be in a position to have it.

A lot of the industry is focused on small-scale social games. Why has Take-Two mostly avoided them?

The less-kind version of that question would be, "How did you guys manage to miss the boat?" or "Why don't you own Zynga?" The answer is because if we'd had the same vision, we could have made a lot of money. They understood the power of the Facebook platform for engaging players in social gaming. What would surprise us now is if that's important in five years, because we feel those experiences are too light to be engaging long-term.

So you don't rely on casual players. You want the hard-core gamers?

If you make Pepsi, should you try to make chewing gum? I don't think so. You don't benefit from dumbing down the product to attract an audience. The hard-core gamer is attracted by quality.

But aren't hard-core gamers mostly teenagers who eventually grow out of games?

We, as adults, consume the entertainment we avidly consumed when we were 17. So the median age of the average game player is mid- to late 30s, and it's going to continue to grow.

So you think middle-aged people will be playing games like Grand Theft Auto?

You're going to see the median age of game players go up into the 50s. This market is going to be a growth market for the next 20 years. Interactive entertainment is the only growth business in entertainment. ☺

ANTICIPATING A CRIME SPREE

It's not surprising that analysts and gamers eagerly await Grand Theft Auto V, the next version of Take-Two's top franchise. Grand Theft Auto IV has sold more than 23 million copies since its 2008 debut.

TAKE-TWO INTERACTIVE (TTWO)

PRICE
\$16



EST. 2013 REVENUE*
\$1.8 bil.

EST. 2013 EPS
\$2.80

EST. 2013 P/E
6

MARKET VALUE
\$1.4 bil.

*Fiscal year ends 3 / 31 / 13. SOURCE: BLOOMBERG