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**Blu-ray Disc Sales and Transformers Week:  
More Than Meets the Eye..... 1**  
**HD DVD Sub-\$200 and Sub-\$100 Price Moves  
– The Beginning of the Real Format War.... 2**

**November 4 Sunday Circular Report..... 4**  
Firsts: Next Generation Players Dip Below \$200,  
\$100; \$399 Playstation 3 Launches..... 4  
Advertisements by Disc Format..... 6  
Circular Analysis by Retailer..... 8

## Blu-ray Disc Sales and Transformers Week: More Than Meets the Eye

By Paul Erickson

Last week marked another important battle in the next generation DVD software market between HD DVD and Blu-ray Disc, raising more questions than it answered. Since the announcement of the Paramount HD DVD exclusivity deal, HD DVD enthusiasts have awaited the release of box-office hit "Transformers" on HD DVD. The deal made Hollywood blockbusters "Transformers" and "Shrek the Third" exclusive to HD DVD; that exclusivity was expected to help HD DVD match or beat Blu-ray's long-running superiority in weekly disc sales.

As anticipated, "Transformers" sold well upon the October 16 release, with Paramount claiming it had become the fastest-selling HD DVD title in the format's history.. The studio claimed the title sold 100,000 units on its first day of release, and over 190,000 on its first week of release. This number was disputed by *Home Media Magazine*, which placed the actual sales number at closer to 115,000 units. Regardless, "Transformers" was clearly a sales hit for HD DVD, and was anticipated to drive HD DVD to a weekly software sales victory over Blu-ray. When the weekly sales data was tallied, however, Nielsen VideoScan pegged Blu-ray as the week's disc sales victor by a 2% margin. The victory was hailed as a symbolic victory by Blu-ray proponents, as HD DVD's strongest title to date could not best Blu-ray software sales even during a week without major releases from the Blu-ray camp. Combined with Blu-ray's long-running software sales superiority, it seemed an indicator of the overall strength of the movie purchasing power of the Blu-ray installed base.

Looking beneath the surface, however, reveals a more complex picture thanks to a pre-emptive strategy from the Blu-ray camp. Most of the major retailers covered within the Nielsen VideoScan universe launched Blu-ray Disc movie promotions beginning either on the weekend or the day before the release of the "Transformers" HD DVD. Retailers such as Circuit City, Best Buy, Amazon and Fry's offered 2-for-1 promotions and discount prices that reduced effective Blu-ray Disc prices on select Sony and Disney titles to approximately \$10-15. In many circumstances the cost for the Blu-ray Disc version of a title fell below the price of its regular standard definition DVD equivalent. Additionally, enthusiasts on various home theater forums quickly passed word that many titles not on the select list could still be purchased at the reduced prices at retailers like Circuit City. Many enthusiasts produced photographic evidence across several message forums, of buying four or more (in some cases up to 10 or 12) Blu-ray titles at the sharply reduced pricing. Combined with Blu-ray enthusiasts on various forums rallying the community to buy heavily that week to specifically prevent the "Transformers" HD DVD launch from generating a weekly Nielsen victory for the format, it is clear that the victory for Blu-ray in total disc sales during that week is quite unclear as an organic indicator when these contributing factors are accounted for.

The perspective to consider when weighing the importance of the Blu-ray software victory for the week of the "Transformers" launch would be the cost and margin of victory. HD DVD's substantially smaller total user base was bested by 2%, but required selling Blu-ray Disc titles at or below the cost of standard definition. The power of Blu-ray's

numerically superior installed base was demonstrated by the week's sales; however, the purchasing power of the smaller HD DVD installed base was demonstrated, as well as consumer response to pricing next generation content at standard definition prices.

Hardware sales were also noticeably boosted by sales of "Transformers" with weekly HD DVD player unit sales experiencing an increase of 49% for the week according to NPD's weekly POS data. This increase propelled HD DVD to its first week of victory in hardware revenue since late June this year. Distinct rises in hardware sales thanks to content releases have been extremely rare in the next generation player market, largely due to over-\$300 pricing that limited both formats' players in their appeal to wide audiences. The response in HD DVD hardware sales coinciding with the "Transformers" release may indicate that next generation DVD content's capability to drive the hardware purchase decision will only increase as both formats' hardware moves into more affordable price points.

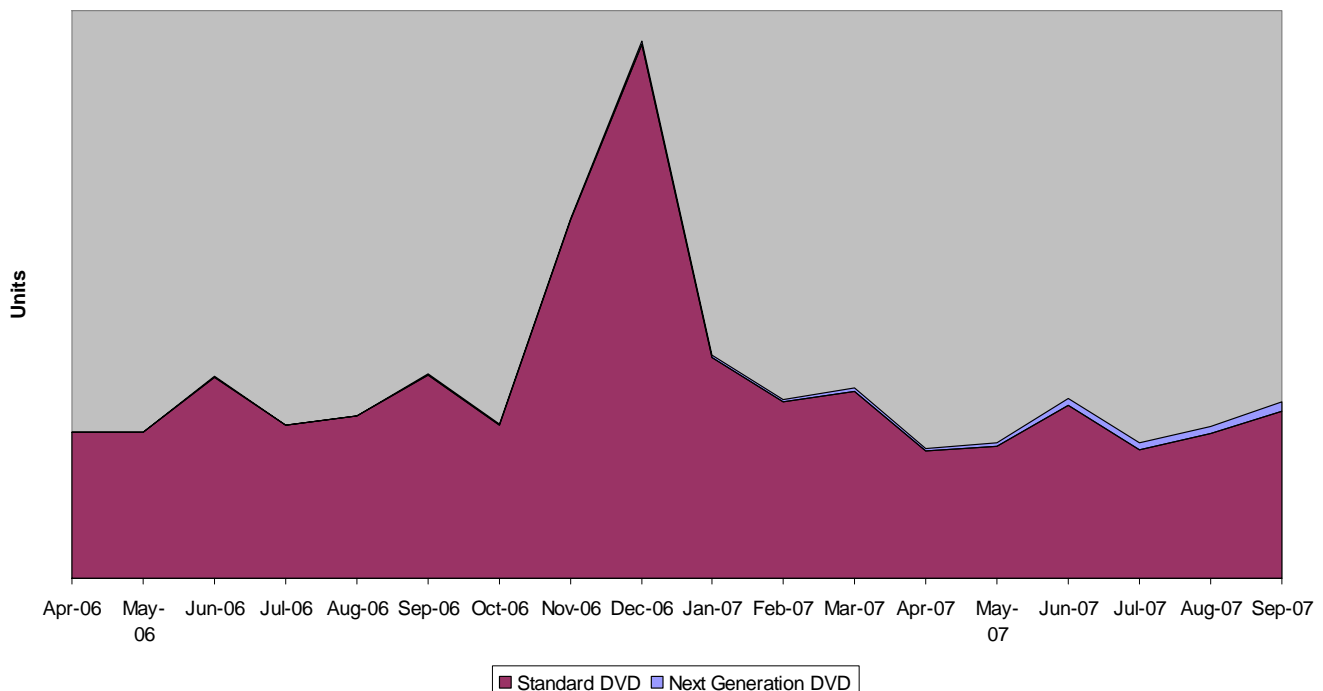
## HD DVD Sub-\$200 and Sub-\$100 Price Moves: The Beginning of the Real Format War

*By Paul Erickson*

Since the beginning of the battle between HD DVD and Blu-ray Disc, the market has seen the distinct positioning of each side along different paths to mainstream success. For Blu-ray Disc, the participation of many CE companies and studios, an advantage in storage capacity, and the help of Sony's Playstation 3 were all expected to drive the format to victory. HD DVD's strategy has been one of offering lower-priced hardware, with advantages in standardized interactive capabilities and Internet connectivity.

According to NPD POS data and DisplaySearch's estimates, neither format has been successful in capturing notable standalone player share beyond the enthusiast and early adopter segments. For standalone players, consumers have shown a stronger sales response to price moves rather than to the inherent technical merits of either format or any advantages in content. This lukewarm level of mainstream interest is partially responsible for both sides' installed bases remaining dominated by game console-related hardware: Playstation 3 for the Blu-ray Disc camp and the Xbox 360 HD DVD attachment for the HD DVD camp. As shown in Figure 1 below, next generation standalone player share growth has remained difficult, reaching just over 5% unit share of the overall DVD market as of the end of September.

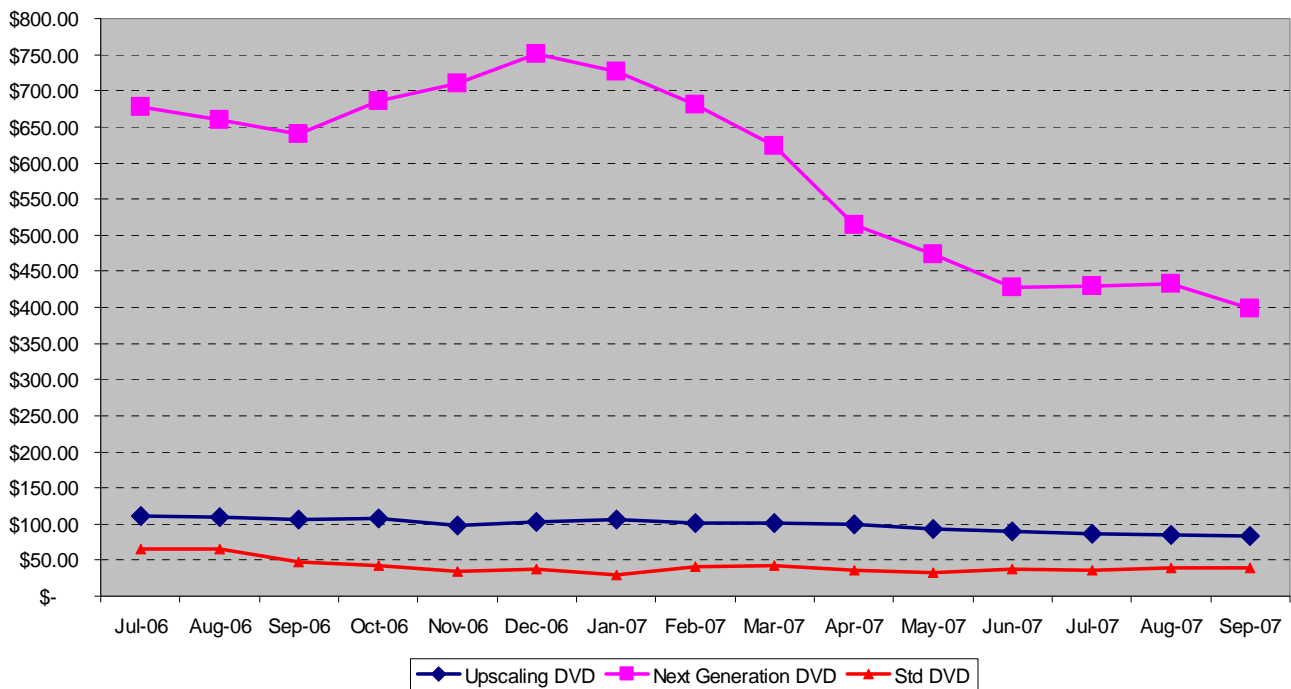
**Figure 1** Next Generation vs. Standard DVD Standalone Player Sales



Source: NPD Retailer Tracking Service

Additionally, NPD's recent consumer survey research revealed that the two most significant reasons why consumers have not purchased a next generation player were high prices and satisfaction with regular DVD. The popularity of up-scaling DVD players as an inexpensive complement to an HDTV has proven to be the next generation segment's competitive manifestation of these two sentiments. The biggest challenge for next generation DVD has now become the reduction of the price differential between next generation DVD and up-scaling DVD hardware, to levels where the consumer is willing to consider HD DVD or Blu-ray as a viable and affordable option above up-scaling DVD players. As of September 2007, the differential between next generation and up-scaling DVD players remained close to \$360.

**Figure 2 Next Generation Price Differential with Standard and Up-scaling DVD Players**



Source: NPD Retailer Tracking Service

Last week, HD DVD struck the first blow towards this end, with prices on Toshiba HD DVD players dropping below \$200 at several retailers. Several enthusiast forums revealed that Wal-Mart would be stocking the Toshiba HD-A2 HD DVD player for \$198, marking the first foray of a brand-name next generation DVD player below the \$200 price point. Amazon.com and Circuit City quickly followed suit, offering the HD-A2 at a \$197.99 price even before the official November 3 launch date of Wal-Mart's new pricing. In leaked Black Friday offer information, it was revealed that Sears will be offering the Toshiba HD-A3 player for \$169.99 on Black Friday with two included movies. As of October 31, Best Buy had reduced the price of the Toshiba HD-A2 player to \$179.99. The same week, Wal-Mart also announced a "secret" Friday November 2 sale on select items, with prices to be revealed on Thursday, November 1. One of the five items prominently featured when the offers were revealed, was the Toshiba HD-A2 HD DVD player at \$98.87.

The result was another firestorm. Not to be outdone, Best Buy quickly dropped the price of the HD-A2 to \$99 on Thursday, and quickly sold out. Best Buy's intentions for the rapid price drop became clear on Friday, as the retailer dropped the price of the Toshiba HD-A3 to \$199.99. Combined with Best Buy's own two-free-HD DVD offer, Toshiba's five-disc mail-in offer, and the two packed-in titles for all third-generation Toshiba players, the resulting total of nine free HD DVD titles was also a strong appeal to go along with the sub-\$200 price. Beginning Sunday, November 4, Best Buy increased the offer from two to three in-store titles, bringing the free disc total to ten. Online retailer Crutchfield dropped its HD-A2 pricing to \$109 on Friday as well, also quickly selling out. At the time of writing, several other on-line retailers had instituted price drops, with Tiger Direct dropping the HD-A2 to \$149.99. The price drops continued in retail stores from Friday through the weekend, as Circuit City responded by dropping the regular price of the HD-A2 to \$129.99 and the HD-A3 to \$199.99. Fry's offered the HD-A3 for \$99 in-store, seemingly in response to Wal-Mart and Best Buy, and Sears dropped the regular price of the HD-A3 to \$199 while dropping HD-A2 pricing to \$98.

It is nearly certain that the flurry of \$99-129 pricing on Toshiba HD-A2s is intended to pave the way for the newer HD-A3 entry model to enter holiday inventory as the HD DVD player at the sub-\$200 price point. Nevertheless, these price reductions represent a significant milestone for the HD DVD format, whose proponents have maintained that more accessible mainstream pricing would be the factor that would ultimately drive wide adoption. Thus far, the least expensive offering from the Blu-ray Disc side of the format war remains the 40 GB Playstation 3 game console, at \$399.

As Black Friday nears, it will be interesting to see how the Blu-ray Disc Association responds, and what the mix of software and hardware promotions will be to address the increased hardware price differential between the two formats. As of the time of writing, Sony representatives had indicated to the press that a drop to the \$399 price point for the holidays was likely for Blu-ray stand-alone players. Should several of the players currently at \$499 drop to \$399, this would complement the existing \$399 40 GB Playstation 3 that was just launched last week. DisplaySearch currently estimates that 2007 sell-in for next generation DVD standalone players will be approximately 961K units; however, this may change if the holiday price warfare results in regular pricing for entry-level HD DVD and Blu-ray players dropping below \$199 and \$399, respectively.

Above the fray, Warner Bros. continues to observe this fourth quarter with measured interest, with the dual-format-supporting studio reportedly mulling a decision to go to a single next generation format by Q1'08. Much of the decision would seem to hinge on Toshiba's ability to sell through substantial numbers of HD DVD players through the holiday. This prospect is aided by the strong contribution of the always-influential Wal-Mart, which also launched television commercials showcasing a Toshiba HD DVD player last week. Significant hardware sales would help validate the HD DVD camp's position that accessible mainstream pricing is the key to the quickest possible ramping of mass market penetration of standalone players, which are the hardware preferred by studios due to their higher movie attach rate compared to console-related devices. Without this validation of HD DVD's fundamental value proposition based on cost advantages, Warner's favor may move to the Blu-ray camp given the format's installed base and disc sales advantages driven by the Playstation 3.

With HD DVD's pricing now at mainstream sub-\$200 pricing, this holiday season thus marks the first viable retail battlefield test of whether or not HD DVD's proposition of greater affordability is more valuable to consumers than Blu-ray's proposition of storage capacity and content advantages. This quarter may mark not only the true beginning of the two formats' war for mainstream buy-in, but also the war's most important battle to determine the ultimate victor.

## November 4 Sunday Circular Report

*By Paul Erickson*

### **Firsts: Next Generation Players Dip Below \$200 and \$100; \$399 Playstation 3 Launches**

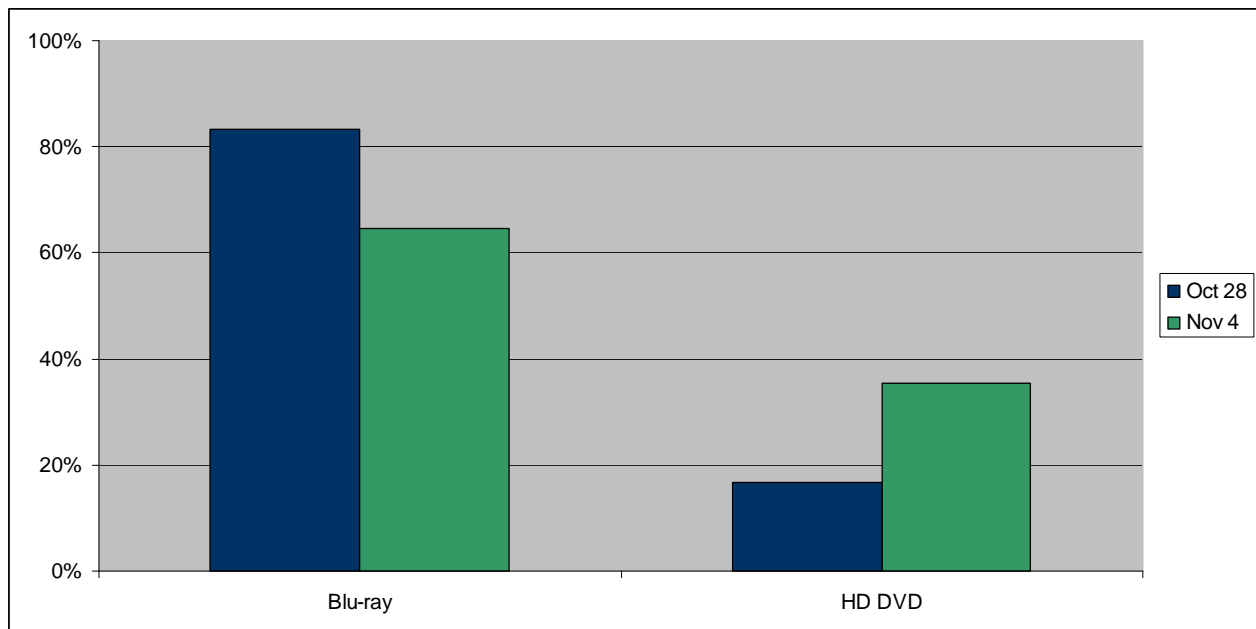
As mentioned earlier in this issue, this week saw a furious wave of price moves on entry-level HD DVD player hardware following the disclosure of Wal-Mart moving below \$200 with the Toshiba HD-A3 beginning November 3, and Sears \$169 Black Friday pricing for the Toshiba HD-A3. With Wal-Mart's "Secret Sale" on Friday, November 2 dropping the price of an HD DVD player below \$100, and the reciprocation by Fry's, Best Buy, and Sears, consumers had access to the lowest prices for next generation hardware in the short history of the market.

Most stocks of Toshiba HD-A2s were depleted Saturday, leaving regular pricing and offers to go back into effect for that model's newer replacement, the HD-A3. Last weekend saw a notable increase in the number of HD DVD promotions offered, which combined with the price activity from Thursday-Sunday, likely indicates the beginning of HD DVD's campaign leading up to the holidays. This week's total of 17 ads is a near-tripling of the 6 featured in retailers' circulars the previous week, primarily due to the launch of the new lower-priced Playstation 3 SKU as well as effort on both sides of the format war to kick off a strong holiday buying season.

**Table 1** November 4 Advertisements by Retailer and Player Type

	Best Buy	Circuit City	CompUSA	Sears	Total
Blu-ray Disc	1	2	0	0	3
HD DVD	2	3	0	1	6
Dual Format	0	0	0	0	0
Playstation 3	3	3	1	1	8
HD DVD (Xbox 360)	0	0	0	0	0
Total	6	8	1	2	17

Figure 3 reveals advertising distribution by disc format of the four surveyed national retailers comparing this Sunday to last Sunday. Blu-ray's advertising presence continued to lead, however HD DVD strengthened its share of ad presence by approximately 18%. This advertising share split between the two formats will be interesting to monitor in the weeks ahead, in the aftermath of the inexpensive HD DVD pricing that was loosed on consumers at the end of last week, generating a substantial amount of free press and awareness for HD DVD thanks to attention-grabbing sub-\$100 pricing.

**Figure 3** Share of Ads by Disc Format—Previous Week to Current Week—October 28 & November 4

## Advertisements by Disc Format

### Blu-ray Disc

**Sony** claimed the majority of Blu-ray ad share this week, thanks primarily to the launch of the 40 GB Playstation 3. The new \$399 price point for this SKU is expected to help the sell-through for the console and to help drive further mainstream penetration for Blu-ray Disc. Both Best Buy and Circuit offered the Playstation 3 in discounted bundle offers with Sony HDTVs as well. Should the 40 GB model continue to be the lowest-priced BD player, it is expected to comprise a larger number of Blu-ray bundling offers to compete against similar bundled offers from Toshiba for lower-priced HD DVD hardware and Toshiba HDTVs.

**Samsung's** BD-P1400 player formed the remainder of the non-Sony BD representation, with the \$499 price in combination with Samsung's representation in other CE categories apparently giving retailers such as Best Buy and Circuit City greater flexibility in offering bundles with other products such as HDTVs and home theater audio systems.

**Sharp** and **Panasonic** are new entrants to the sub-\$500 fray, and are expected to gain more representation in retailer circulars as the holidays approach. With NPD and DisplaySearch data indicating more than 70% of stand-alone next generation player unit volume has now shifted to sub-\$500, retailers are likely to show more confidence in the volume able to be driven by these two brands' BD hardware going forward.

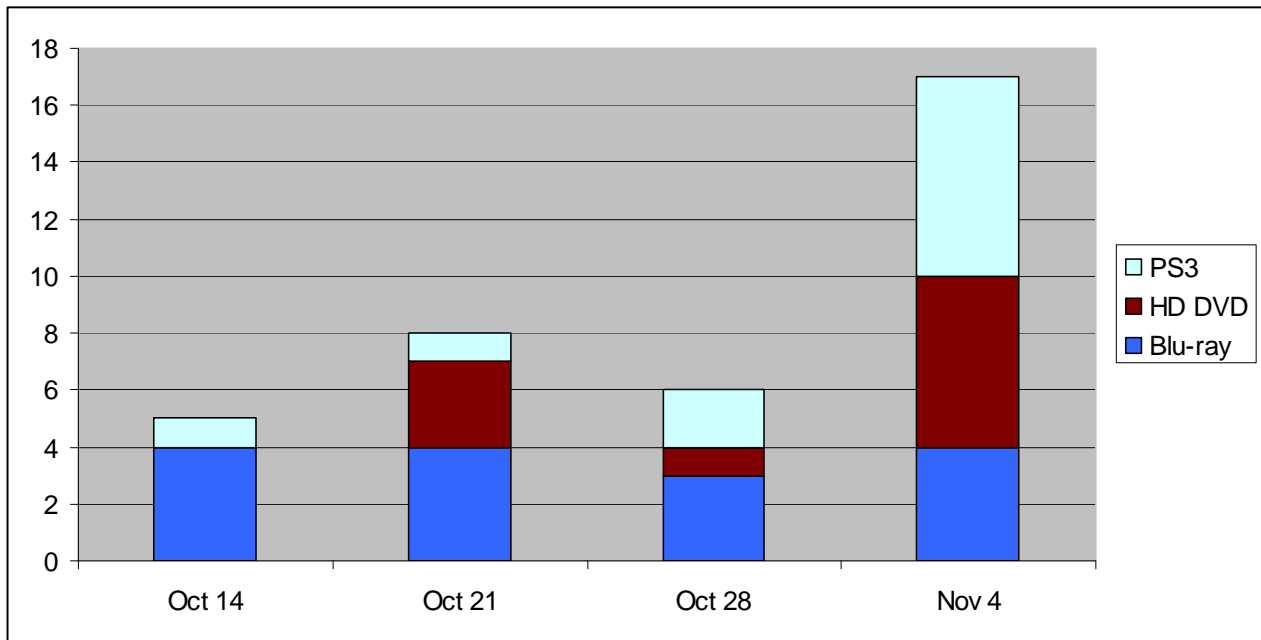
### HD DVD

**Toshiba** claimed all of this week's HD DVD advertising representation, with the Xbox 360 HD DVD attachment absent from the four national retailers' advertisements. The majority of ads showcased the entry-model HD-A3 at \$299, though by the weekend the actual floor and on-line price had dropped to \$199 at most retailers. The five free disc offer was represented at all major retailers, however Best Buy added an additional two in-store titles (which increased to three in-store titles on Sunday, November 4). Due to the recent introduction of the third generation of Toshiba's players (HD-A3, HD-A30, HD-A35), the net effect of the inclusion of "300" and "The Bourne Identity" in the box has yet to be determined. Nevertheless, the combination of these two discs and the standard five-disc offer will make "seven free movies" a common mantra for HD DVD's standalone players through the holidays. Best Buy's addition of three in-store titles certainly sweetened the deal for consumers, particularly for the HD-A3 when it was available for \$199.

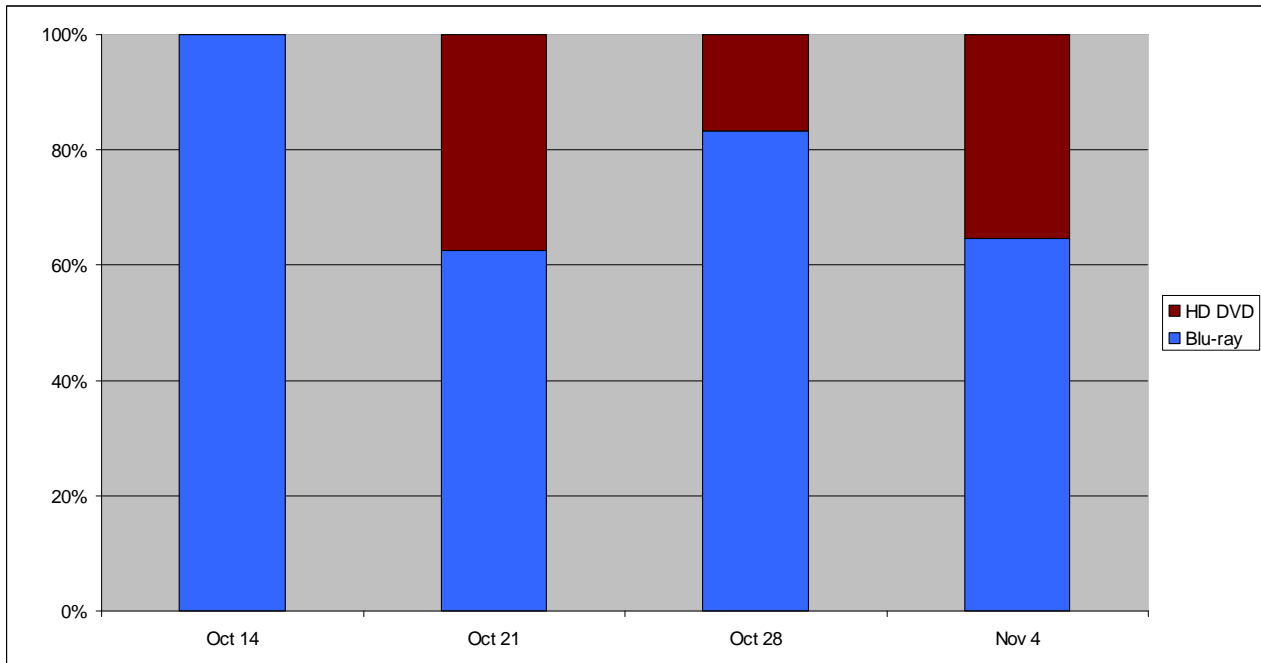
Similar to current offers from **Sony**, additional discounts are being offered when HD DVD players are combined with Toshiba HDTVs. This is expected to continue and expand as the holidays approach, particularly given the expectation that HDTV bundling will be an avenue explored heavily by Blu-ray to maneuver around the price differential between the two formats.

The following figures illustrate the advertising representation by both formats last week, including the portion related to the Playstation 3. The Playstation 3 comprised the majority of BD-related ads last week, due largely to the launch of the more-affordable \$399 40 GB Playstation 3. Total ads increased noticeably driven not just by the new Playstation launch, but also by increased attention given to HD DVD compared to the week before.

**Figure 4** Number of Circular Ads by Player Type – Rolling Four Week Survey



**Figure 5** Share of Ads by Disc Format – Rolling Four Week Survey



### Circular Analysis by Retailer

Best Buy and Circuit City both gave a next generation DVD product front cover; both showcasing the new \$399 40 GB Playstation 3. Across all retailers except Sears, the Playstation 3 received strong representation, primarily due to its release at the lower \$399 price point that week.

### Best Buy

Best Buy featured the Playstation 3, Spiderman 3, and popular game title Ratchet & Clank: Tools of Destruction on its cover. The Playstation 3 was also featured on the cover in a bundle with the buyer's choice of a 46" Sony Bravia 1080p LCD TV or a 40" Bravia XBR LCD with 120°Hz refresh rate for \$2499. Samsung's \$499 BD-P1400 was placed on a page featuring the 40 GB Playstation 3 on a sidebar. On this same page, a Samsung 40" 1080p LCD TV and a Samsung 5.1-channel home theater audio system were shown, and Best Buy offered an additional \$100 if all three Samsung products (BD player, TV, audio system) were purchased together. Prominently featured was an offer for five free Blu-ray movies via mail and two in-store, for a total of seven free titles. On a page featuring a large DirecTV spot, and a variety of up-converting DVD players and recorders, the \$299 Toshiba HD-A3 was featured, with the offer of eight free discs highlighted. With five discs via mail, two packed into the box, and three in-store, buyers were receiving a total of ten discs. As mentioned at the beginning of this issue, Best Buy lowered the price of the HD-A3 to \$199 during the weekend. The price was raised back up to \$299 on Monday, November 5. An additional \$200 discount was offered if an HD DVD player was purchased with a Toshiba HDTV 42" or larger.

Figure 6 Best Buy November 4 Ad Sample



### Circuit City

Circuit City led all next generation DVD in the number of product insertions in their Sunday ad. The majority of these appearances were Playstation 3 (both 40 GB and 80 GB versions). The \$399 40 GB Playstation 3 was also offered as part of a bundle with a Sony 40" 1080p LCD TV for a total price of \$1799. The \$699 Sony BDP-S500 and \$499 Samsung BD-P1400 were the other two Blu-ray models featured in the circular, with the Samsung model also offered as part of a bundle with a Samsung 46" 1080p LCD TV for \$2699 and eight total free Blu-ray movies available via mail. All other BD models including Playstation 3s had an offer for five free Blu-ray discs featured. On the HD DVD side, Toshiba's \$299 HD-A3 and \$399 HD-A30 players were featured in the circular, with the HD-A3 also offered as part of a bundle with a Toshiba 42" LCD TV for \$1399. During the weekend's HD DVD pricing frenzy, Circuit's HD-A3 price was lowered to \$199, before climbing back to \$299 on Monday, November 5. The HD-A30 was accompanied by text highlighting ten free HD DVDs (two in-box, three in-store and five by mail). Circuit City's three-fold presentation of next generation hardware featured the devices in areas concerning console gaming, 1080p HDTVs, and the players themselves.

Figure 7 Circuit City November 4 Ad Sample

The figure displays six distinct advertisements from Circuit City's November 4, 2007, circular. The ads are arranged in a grid-like fashion, showcasing various products and promotions:

- Top Left Ad:** Celebrates the "grand opening celebration 65 new stores nationwide". Features a Mazda CX-9 with a "win a Mazda CX-9" promotion and "up to 10% off TVs." Promotional offers include "300 Panasonic 42" LCD HDTV" for \$1799.99, "DRIVE TO 65 Instant Win GAME" (win a game daily at a Mazda CX-9), and "5 free Blu-ray movies".
- Top Right Ad:** Focuses on PlayStation 3 consoles, offering a "PS3 40GB" for \$399.99 (new only) and a "PS3 80GB" for \$499.99. Includes offers for "2 free games" and "5 free Blu-ray movies".
- Middle Left Ad:** Promotes "Santa's little helper" with deals on HDTVs. Offers include a "42" LCD HDTV" for \$1399.99 and a "46" LCD HDTV" for \$1999.99. Includes "Home Theater service" and "Flat panel installation".
- Middle Right Ad:** Promotes "up to 10% off TVs." and features deals on HDTVs, such as a "42" LCD HDTV" for \$459.99 and a "46" LCD HDTV" for \$319.99.
- Bottom Left Ad:** Features a "Mazda CX-9" for \$1799.99 and a "Sony 40" LCD HDTV" for \$1799.99. Includes a "300 Panasonic 42" LCD HDTV" for \$1799.99.
- Bottom Right Ad:** Promotes "furniture selections to fit every TV & every room" and "10 free HD DVD movies". Offers include a "Tech Craft" TV stand for \$229.99 and a "Tech Craft" TV stand for \$349.99.

Sears

Sears promoted the Samsung BD-P1400 at a discounted \$469, and the Toshiba HD-A3 at \$299. Free offers of seven discs and five discs, respectively, were mentioned in fine print. Both players were featured alongside the circular's selection of LCD and Plasma TVs., about half of which featured the image of Disney's "Ratatouille" and a mention of its release on DVD and Blu-ray. Sears offered an additional \$100 off a purchase of both a Toshiba 1080p HDTV and a HD DVD player. Sears also offered free shipping and a free \$100-value pizza party from Domino's Pizza for those who purchased both an HDTV and an HD DVD player. By the time the circular had reached circulation, however, the price of the HD-A3 had already reached \$199 online and in stores due to the week's HD DVD-related activity.

Figure 8 Sears November 4 Ad Sample

**Table 2 Complete November 4 Advertised Next Generation DVD Price List**

Retailer	Brand	Product Name	Format	Print Price	Web Price	Note
Best Buy	Samsung	BDPP1400	Blu-ray	\$500	\$500	
	Sony	PlayStation 3	Blu-ray	\$2,500	\$2,500	Bundle: KDL-40XBR4, Spiderman 3
	Sony	PlayStation 3	Blu-ray	\$2,500	\$2,500	Bundle: KDL-46V3000, Spiderman 3
	Sony	PlayStation 3	Blu-ray	\$400	\$400	Bundle: Spiderman 3
	Toshiba	Any	HD DVD	(\$200 + OFF)	(\$200 + OFF)	with Toshiba HDTV 42"+
	Toshiba	HDA3	HD DVD	\$300	\$200	Bundle: Bourne Identity
	Samsung	BDP1400	Blu-ray	\$2,700	\$2,700	Bundle: Samsung LNT4665F
Circuit City	Sony	BDPS500	Blu-ray	\$700	\$700	
	Sony	PlayStation 3	Blu-ray	\$400	\$400	Bundle: Spiderman 3
	Sony	PlayStation 3	Blu-ray	\$1,800	\$1,800	Bundle: Sony KDL40V2500, Spiderman 3
	Sony	PlayStation 3 80G	Blu-ray	\$500	\$500	Bundle: MotorStorm game
	Toshiba	HDA3	HD DVD	\$1,400	\$1,400	Bundle: Toshiba 42HL167, Bourne Identity
	Toshiba	HDA3	HD DVD	\$300	\$300	Bundle: Bourne Identity
	Toshiba	HDA30	HD DVD	\$400	\$400	
CompUSA	Sony	PlayStation 3 80G	Blu-ray	\$500	\$500	
Sears	Samsung	BDP1400	Blu-ray	\$500	\$470	
	Toshiba	HDA3	HD DVD	\$300	\$200	

## Important Notices

**This is a sample report. Contact us for more information and pricing at**

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