

Antti Kotaniemi

2nd year Full-time Master Studies, International Business

Downfall of nokia

Introduction

Mobile phone industry is one of the most dynamic and competitive market in the world. During the last decade the mobile industry have experienced many notable changes such as introduction of Apple's iPhone and Google's Android operating system. Last major change occurred when the Finnish mobile phone manufacturer Nokia was acquired by Microsoft in 2013. Microsoft switched the brand name Nokia Lumia to Microsoft Lumia and continued developing Lumia series smartphones without Nokia. For a decade Finnish mobile phone manufacturer Nokia was a market leader in mobile phone market. Since the early 2000s smartphones became increasingly popular segment inside the mobile phone industry. Mobile phone market leader Nokia underestimated the importance of smartphones, and although remaining as a market leader for entire mobile phone industry until the early 2010s, it was underachieving in the smartphone market in comparison to its main rivals Apple and Samsung. Nokia tried to gain a market leadership in the smartphone industry through strategic alliance with technology company Microsoft, which, however, failed to achieve its goal.

This article attempts to explain through descriptive research method the main reasons that caused the downfall of Nokia from being the mobile phone market leader to becoming a former mobile phone manufacturer in less than 10 years. This article suggests that industry changes and company's decision making environment caused an irreversible decline in Nokia that resulted in acquisition of Nokia's Devices & Services unit to Microsoft.

1. Smartphone market

In the early and mid-2000s Finnish company Nokia was a trusted brand and the undisputed market leader in mobile phone market. Nokia had gained market leadership from Motorola in 1998. However, Nokia did not understand a critical change in customer demand on time. Consumers interests changed from feature

phones¹ to the modern smartphones in relatively short period of time. Although Nokia and many other mobile phone manufacturers had smartphones long before the introduction of modern smartphones. The first iPhone in 2007, changed the direction of the whole mobile phone industry and the modern smartphones quickly began to increase their popularity. Nokia on the other hand overestimated the value of its own brand and reacted slowly to the rapid changes in the smartphone market. Instead of focusing on the software, Nokia stubbornly held on to its outdated Symbian operating system and hardware design.

Symbian OS had helped Nokia establishing its market leader position in the early 2000s. However unlike its rivals Google and Apple, Nokia was not able to modernise Symbian OS, which had since the introduction of modern smartphones become outdated. Early smartphones, such as Nokia communicator series, were mainly targeted on business users or to satisfy a need of certain other consumer segment. For example, Nokia N-Gage, handheld gaming device and a phone, was marketed for gamers. By modern standards, early smartphones were often complicated and hard to use and develop apps to since every smartphone operated differently².

Mobile ecosystem is somewhat an abstract term that can be understood as a group of mobile devices, software development tools, device manufacturers, app stores, application developers, applications, accessories, cloud services, smartphone users and operating systems that are all symbiotically linked to each other³. How well all the elements around the ecosystem work, defines the value of the particular ecosystem. Operating system is a easier to understand. The operating system (OS) is a sub-program that runs other programs in every computer. Microsoft's Windows is probably one of the most well-known operating system in the world. Since smartphones are basically a handheld computers, they also require operating system to run and maintain apps (programs) and other functions. The Symbian was the main operating system for Nokia's smartphone's between 2002–2011.

2. Development of the smartphone market

Nokia enhanced its market share in mobile phone market until 2007. According to David J. Cord Nokia's share of the global mobile market had climbed from 33 per cent in 2005 to 35 per cent in 2006. Next year was even better; Nokia was

¹ Feature mobile phone is an industry term for low-end mobile phones.

² T. Martin, *The Evolution of the smartphone*, Pocketnow, 28 July 2014, <http://pocketnow.com/2014/07/28/the-evolution-of-the-smartphone> [access: 29 November, 2016].

³ *What Is Mobile Ecosystem*, LearnDataModelling.com, 31 August 2015, <https://learndatamodeling.com/blog/what-is-mobile-ecosystem/> [access: 29 November 2016].

able to sell 436 mobile phones and its market share was around 40 per cent in 2007⁴. Nokia's nearest rival at the time was Motorola⁵, who sold around 164 million mobile phones during that year⁶. Nokia was by far the dominant mobile phone manufacturer.

Due to rising consumer demand for smartphones, the focus of mobile phone manufacturers had gradually started to shift from hardware to software. This meant that things such as the number of applications in app store replaced the amount of megapixels in mobile phones camera as an active element in the purchasing decision of average consumer. Consumers wanted to perform increasingly complex actions with their smartphones, not merely making phone calls, taking pictures and sending text messages or emails. Smartphones became smarter and started to resemble small handheld computers with their complex software related functions such as browsing the internet, uploading pictures, watching video clips, accessing digital music stores, maintaining virtual music or movie libraries and downloading apps⁷.

The mobile phone industry began to experience a fundamental change during the end of first decade of the 21st century. Something new and exciting was introduced in mobile phone industry. The launch of iPhone and, soon after Google's open-source Android operating system transformed smartphones into a hybrid of computing and communications devices with enormous and ever increasing amount of software apps. Modern smartphones have since that not only created new industries around their ecosystem but replaced entire industries. Interestingly technology blog Gecko&Fly have calculated that smartphones have replaced 50 everyday items such as cameras, laptops, voice recorders etc.⁸

There are number of factors and strategic errors that caused Nokia's failure to adjust to changes in consumer demand and entirely new competitive environment. Most notably in 2006 Nokia decided to move its focus from smartphones back to feature mobile phones. While Nokia's core competence was in radio technology and hardware engineering, smartphones required software, user experience design skills and competence in touch screen technologies that Nokia, to some extent, simply lacked during that time.⁹ Nokia failed to understand the

⁴ D. Cord, *The Decline and Fall of Nokia*, Schildts&Söderströms, Borgå 2014, p. 13.

⁵ In 2011 Motorola Mobile was acquired by Google and in 2014 sold to Chinese Lenovo.

⁶ M. Ahmad, *Nokia's smartphone problem: The end of an icon?*, CreateSpace Independent Publishing Platform, North Charleston, South Carolina, May 6 2013, p. 84–85.

⁷ M. Ahmad, *Nokia's smartphone problem...*, p. 92–93.

⁸ N. Tengyuen, *50 Things Your Smartphone Replaced [Or Will Replace In The Future]*, Gecko&Fly, November 19 2016, <https://www.geckoandfly.com/13143/50-things-smartphone-replaced-will-replace-future/>, [accessed 29 November, 2016].

⁹ T. Vuori, Q. Huy, *Distributed Attention and Shared Emotions in the Innovation Process: How Nokia Lost the Smartphone Battle*, "Administrative Science Quarterly" 2015, p. 1–43.

importance of building of an mobile ecosystem around the smartphone¹⁰. In a nutshell, Nokia's demise was fundamentally caused by its inability to adapt and develop a working operating system, smartphone ecosystem and to attract mobile app developers and interest of consumers.

During the late 2000s it became increasingly evident that Nokia would need a partner that would have software expertise. Symbian operating system that Nokia was using as a platform for its smartphones during that time had become outdated compared to its rivals Apple's iOS and Google's Android. At the time Nokia was developing a new Linux-based operating system with Intel to replace Symbian. Maemo's development was later abandoned when Nokia and Microsoft announced their strategic alliance. Nokia had two options; it could start developing operating system with Google's Android or Microsoft's Windows mobile OS. Nokia chose to enter cooperation with Microsoft. Microsoft had tried to enter mobile market first time in 2000 when it introduced Tablet PC, with mobile version of Windows OS¹¹ Nokia's problems with smartphones presented a new opportunity for Microsoft to enter potentially lucrative market.

3. Strategic alliance

Much like a marriage, strategic alliance is a form of partnership where two companies take advantage of each other's core strengths and share their own strengths with their strategic partner. Partners can be potential competitors. Global Strategic Alliance is a term used of strategic alliance partnership when cooperating partner companies originate from different country. The main benefit of strategic alliance is that it enables complementary skills and assets that a single company couldn't easily develop on its own.

In 2011, Nokia and Microsoft established a broad strategic alliance that aimed to use their complementary strengths to create a new mobile ecosystem under Microsoft's Windows Mobile OS. Microsoft had extensive software engineering skills and Nokia had a strong global brand and skills regarded to mobile phone manufacturing, electrical engineering, design and marketing. An additional aim of the strategic alliance was to introduce a competitive operating system to Apple's iOS and Google's Android. The first smartphone that resulted from strategic alliance between Microsoft and Nokia reached the market in late 2012, but was too late to challenge dominance of Samsung and Apple at that time¹².

¹⁰ M. Ahmad, *Nokia's smartphone problem...*, p. 91.

¹¹ *A Brief History of Windows Mobile*, Notebooks.com, 12 April 2010, <http://notebooks.com/2010/04/12/a-brief-history-of-windows-mobile/> [access: 29 November, 2016].

¹² C. Hill, M. Schilling, G. Jones, *Strategic Management Theory: An Integrated Approach, 12th edition*, Cengage Learning, Boston 2016, p. 269.

According to Chris Huxham and SivVangen, organizations typically collaborate if they are not able to achieve their objectives alone. Collaboration often means bringing together different resources including technology or expertise. Such as it was the case during Nokia's and Microsoft's collaboration, with inter-company collaboration two companies can take a product to market; one company provides the product while other provides the access to the market. Huxham and Vangen states that seeking collaborative advantage is a resource-consuming activity which should only be considered when the goals are really worth pursuing¹³. Under Windows Mobile OS Nokia created a smartphone series Nokia Lumia. It seems obvious that Nokia's motivation to enter strategic alliance with Microsoft was to regain the lost market leader position by gaining access and exploiting Microsoft's major software resources.

4. Elop buried Symbian alive

In September 2010, Stephen Elop, a former head of Microsoft's Business Division, was appointed as the CEO of Nokia Corporation. In February 2011, Elop sent his famous internal memo titled the Burning Platform to all the employees of Nokia. Soon after this, the memo was accidentally leaked to media. The memo compared the situation of Nokia in the smartphone market, to a person standing on a burning oil platform¹⁴. Thanks to Burning Platform memo and Elop's announcement to stop the development of the in-house mobile operating systems, Symbian OS and Maemo, Nokia's smartphone sales declined significantly. Nokia released its only Maemophone N9 in June 2011. Despite the generally favourable review most reviewers did not recommend to buy the N9 because of Nokia's earlier decision to stop the development of Maemo. It would not make any sense to buy a smartphone that would not have any content or updates in the near future.

Elop's actions during that time can be compared to the Ratner Effect and Osbourne Effect. Elop managed to do premature announcement of new product and comment negatively on existing products. Although it was known for some time that Nokia's Symbian phones were no longer competitive against iOS and Android, they still generated significant profits. Elop's announcement was the last nail on the coffin that effectively transformed the Symbian market to virtually non-existing. At the same time, Nokia's first Windows Phone would not be ready for a year, and once they were released their sales were not enough to replace the

¹³ C. Huxham, S. Vangen, *Managing to Collaborate: The theory and practice of collaborative advantage*, Routledge, New York 2005, p. 5, 13.

¹⁴ A platform is used as a synonym for an operating system.

volume and profit of Symbian devices had generated. Furthermore the first Lumia phones were released in 26 October 2011¹⁵.

5. Cross-border acquisition

Cross-border mergers, strategic alliances and acquisitions have become more common way to a company to gain growth and expansion, but they must value the target enterprise on the basis of its performance in the market through enterprise valuation and by combining elements of strategy, management, and finance. The potential core competencies and competitive advantages of the target firm attract the acquisition from strategical point of view¹⁶.

In this article we will focus on the concept of cross-border acquisition from viewpoint of Nokia case. Cross-border acquisitions have many notable benefits and advantages. Through acquiring an existing company, buyer company shortens the time that is required to gain a competitive entry and position in the market. Acquiring existing company through cross-border acquisition may be a cost-effective way of gaining new technology, brand names and logistic or distribution advantages, while similarly eliminating a local competitor. However, much like all acquisitions, the cross-border acquisitions don't lack its disadvantages. Much like all acquisitions, there is always a risk of paying too much or suffering other financial costs. History has shown that integrating different corporate cultures may be a difficult process. Often after acquisition, considerable downsized are required due to economies of scale and profitability. In most cases the threat of downsizes further lowers the company's productivity when employees attempt to save their jobs. In cross-border acquisitions host governments might try to intervene in acquisition processes for political reasons¹⁷.

On 3th of September 2013 Microsoft announced its plans to acquire Nokia's Devices & Services unit and all of its businesses for EUR 3,79 billion and in addition pay EUR1,65 billion for licensing of Nokia's patents. EUR 5,44 billion deal was closed on 25th of April 2014. On the same day Microsoft formally appointed former Nokia CEO Stephen Elop as the new head of Microsoft's Devices Group. Devices Group added Lumia smartphones and tablets, as well as other Nokia mobile phones, to its existing portfolio. Device Group portfolio already existed of Microsoft Surface tablets, Xbox video game console, and various hardware acces-

¹⁵ *How Stephen Elop killed Nokia: Two key lessons for your business*, Startup Smart, September 4, 2013, <http://www.startupsmart.com.au/technology/how-stephen-elop-killed-nokia-two-key-lesson-for-your-business/> [access: 29 November, 2016].

¹⁶ D. Eiteman, A. Stonehill, M. Moffet, *Multinational Business Finance: Eleventh Edition*, Pearson Education Inc., Boston 2007, p. 614.

¹⁷ *Ibidem*, p. 617–618.

sories. Through acquisition 32 000 employees of Nokia moved to work for Microsoft¹⁸.

Conclusions

After acquisition was completed, a conspiracy theory circulated widely in Finland's media, accusing Stephen Elop for being a Trojan horse planted by Microsoft in Nokia to lower Nokia's market value. According to theory after lowering value of Nokia's shares, Microsoft could acquire the former mobile market leader in cheaper price. The burning platform memo and Elop's refusal to move his family from Canada to Finland during his tenure in some sense supports this claim. In retrospect, however, the Trojan horse theory seems highly unlikely. There are number of factors that back this up. First of all Jorma Ollila, former CEO and chairman of Nokia (1999–2012) had a major role in selection of new CEO as a replacement for Olli-Pekka Kallasvuo. Ollila has publicly stated that Stephen Elop was not his first choice, but has refused to name the first candidate. However David J. Cord concluded in his book, *The Decline and Fall of Nokia*, that the number one choice for position was Scott McNealy, the co-founder of Sun Microsystems, who however turned the offer down after contemplating it for a long time. The two remaining candidates left were Executive Vice President and a member of Nokia Group Executive Board Anssi Vanjoki and Stephen Elop¹⁹.

It is fair to say that problems that Nokia was experiencing during 2010 had started long before Elop was appointed as CEO of Nokia. Biggest problem was the operating system and the entire ecosystem which did not attract consumers as a same level as iOS and Android. Nokia's decision to react slowly to a disrupted smartphone market was a costly mistake. Instead, Nokia should have introduced a competitive smartphone operating system significantly faster than it actually did. Instead the management of Nokia decided to ignore changes in consumer preferences long before Stephen Elop was appointed as the CEO of Nokia. Shrinking market shares and shrinking profit margins and declining sales should have caused a way greater reactions in Nokia's management. There is no realistic scenario that the old Symbian OS would suddenly result in increased demand or even attract application developers. Nokia had to change the operating system and create an entire ecosystem much faster than it actually did to remain competitive²⁰.

¹⁸ *Microsoft ostaa Nokian matkapuhelimen*, Taloussanommat, 3 September 2013, <http://www.iltasanomat.fi/taloussanommat/porssiuutiset/art-2000001808135.html>, [accessed 29 November 2016].

¹⁹ D. Cord, *The Decline...*, p. 190–192.

²⁰ *Ibidem*, p. 213.

Smartphone market operates in a paradoxical manner; consumers will not buy a mobile device if it doesn't offer at least the minimum amount of applications, and developers won't invest development resources unless the platform offers a significant number of users. In a sense, Microsoft had a considerably more assets to loose when they engaged in strategic alliance with Nokia. Nokia was supposed to work as a showcase to Windows Mobile which no major smartphone manufacturer was using as an operating system in their phones and number of applications remained very limited compared to Android and iOS.

Why did Nokia choose to have strategic alliance with Microsoft instead of Android? This comes down to the operating system and ecosystem and Nokia's differentiation strategy. Windows Mobile OS (Windows Phone) offered a third alternative and a way for Nokia to differentiate itself from competitors platforms: Google's Android and Apples iOS. Many of the mobile phone manufacturers such as HTC, Samsung, Sony-Ericsson (Sony), LG and Motorola gradually switched to using Google's Android OS. If it had chosen Android, Nokia would have not been able to differentiate from other mobile phone manufacturers. With Microsoft, Nokia was able to bring an alternative on the table.

After the beginning of the smartphone wars, the heavyweight title fight over the market shifted to be resulted between Apple and Samsung, while Nokia's role was to fade away from the entire market with constantly falling market share. Nokia's fate resembles now bankrupt home-video rental chain the Blockbusters. Blockbusters, much like Nokia, failed to recognize and react to the threat of novel innovation on time. Technological improvements, such as increased broadband speed, enabled streaming large video files over the internet. Companies, such as Netflix, took advantage of new model. While Blockbuster failed to recognize the threat that online streaming services posed to its chain of brick-and-mortar video stores. Yet another example is Kodak. The company entered bankruptcy in 2012, after smartphones replaced digital cameras²¹.

References

- A Brief History of Windows Mobile*, Notebooks.com, April 12 2010, <http://notebooks.com/2010/04/12/a-brief-history-of-windows-mobile/>.
- Ahmad M., *Nokia's smartphone problem: The end of an icon?*, CreateSpace Independent Publishing Platform, North Charleston, South Carolina, May 6 2013.
- Brassington F., Pettitt S., *Essentials of Marketing: Third edition*, Pearson Education Limited, Essex 2013.
- Cord D., *The Decline and Fall of Nokia*, Schildts&Söderströms, Borgå 2014.

²¹ L. Downes, P. Nunes, *Big Bang Disruption: Business Survival in the Age of Constant Innovation*, Portfolio Penguin, UK, 2014, p. 189-192.

- Downes L., Nunes P., *Big Bang Disruption: Business Survival in the Age of Constant Innovation*, Portfolio Penguin, UK, 2014.
- Eiteman D., Stonehill A., Moffet., *Multinational Business Finance: Eleventh Edition*, Pearson Education Inc., Boston 2007.
- Hill C., Schilling M., Jones G., *Strategic Management Theory: An Integrated Approach*, 12th edition, Cengage Learning, Boston 2016.
- How Stephen Elop killed Nokia: Two key lessons for your business*, Startup Smart, September 4 2013, <http://www.startupsmart.com.au/technology/how-stephen-elop-killed-nokia-two-key-lesson-for-your-business/>.
- Huxham C., Vangen S., *Managing to Collaborate: The theory and practice of collaborative advantage*, Routledge, New York 2005.
- Martin T., The Evolution of the smartphone, Pocketnow, July 28 2014, <http://pocketnow.com/2014/07/28/the-evolution-of-the-smartphone>.
- Microsoft ostaa Nokian matkapuhelimet*, Taloussanomat, September 3 2013, <http://www.iltasanomat.fi/taloussanomat/porssiuutiset/art-2000001808135.html>.
- Tengyuen N., *50 Things Your Smartphone Replaced [Or Will Replace In The Future]*, Gecko&Fly, November 19 2016.
- Vincent J., Four Reasons why Microsoft had to buy Nokia, Independent, September 3 2013, <http://www.independent.co.uk/life-style/gadgets-and-tech/features/four-reasons-why-microsoft-had-to-buy-nokia-8796638.html>.
- Vuori T., Huy Q., *Distributed Attention and Shared Emotions in the Innovation Process: How Nokia Lost the Smartphone Battle*, "Administrative Science Quarterly" 2015.
- What Is Mobile Ecosystem*, LearnDataModelling.com, August 31 2015.

Summary

Mobile phone industry is one of the most dynamic and competitive market in the world. For a decade Finnish mobile phone manufacturer Nokia was a market leader in mobile phone market. Since the early 2000s smartphones became increasingly popular segment inside the mobile phone industry. Mobile phone market leader Nokia underestimated the importance of smartphones, and although remaining as a market leader for entire mobile phone industry until the early 2010s, it was underachieving in the smartphone market in comparison to its main rivals Apple and Samsung. Nokia tried to gain a market leadership in the smartphone industry through strategic alliance with technology company Microsoft. Strategic alliance, however, failed to achieve this goal. This article attempts to explain through descriptive research method the main reasons that caused the downfall of Nokia from being the mobile phone market leader to becoming a former mobile phone manufacturer in less than 10 years. This article suggests that industry changes and company's decision making environment caused an irreversible decline in Nokia that resulted in acquisition of Nokia's Devices & Services unit to Microsoft.

Keywords: Nokia, Microsoft, Google, Apple, smartphone, mobile phone, strategic management, global strategic alliance, market positioning, market strategy, mergers and acquisitions

UPADEK NOKII

Streszczenie

Jednym z najbardziej dynamicznych i konkurencyjnych rynków na świecie jest branża telefonii komórkowej. Przez dekadę liderem w branży był fiński producent telefonów komórkowych – Nokia. Od początku XXI w. Jeden z segmentów rynku w sposób szczególnie zauważalny zyskiwał na popularności i powoli monopolizował rynek telefonów komórkowych – smartphony. Lider branży – Nokia – nie docenił rosnących w popularność smartphonów, i pomimo iż pozostał w czołówce firm produkujących telefony komórkowe, do roku 2010 technologicznie pozostawał w tyle w porównaniu do swoich głównych konkurentów, firm Apple i Samsung. Przy rosnącej sile popytu na smartphone, Nokia próbowała utrzymać pozycję lidera w branży przez strategiczny sojusz technologiczny z firmą Microsoft. Celu tego nie udało się osiągnąć i sojusz odniósł porażkę.

Artykuł ma na celu wyjaśnienie głównych powodów zawarcia tego strategicznego dla Nokii i Microsoftu sojuszu, oraz przybliżenie procesu przejęcia Nokii przez Microsoft. Kwestią badań jest to jakie czynniki kierujące branżą telefonii komórkowej zaważyły o zawarciu sojuszu między Nokią a Microsoftem, oraz które z czynników zadecydowały o jego niepowodzeniu. Literatura źródłowa użyta do napisania tego artykułu to dzieła poruszające temat fuzji i przejęć firm. Wykorzystana została również literatura z zakresu marketingu i zarządzania. Narzędziem analizy ostatnich zmian zachodzących na rynku telefonii komórkowej są analizy biznesowe znanych czasopism branżowych.