



# Consumer Electronics Industry Outlook

OUTLOOK:  Signs of Weakness

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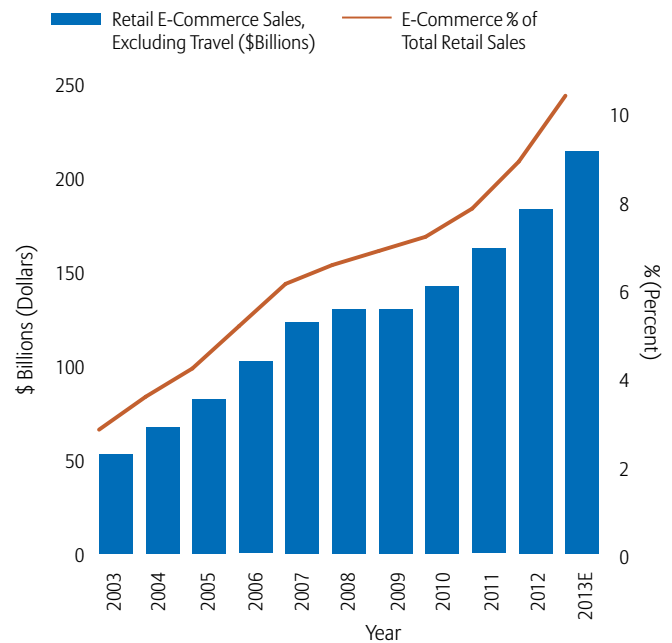
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# Overview

The outlook for the U.S. consumer electronics industry is considered neutral with some signs of weakness, based on the following:

- Euler Hermes forecasts 2013 U.S. GDP to grow 1.9% following a 2.1% increase in 2012.
- Subdued consumer spending and a lack of revolutionary products will result in low single-digit sales growth in 2013.
- The launch of Windows 8, more ultrabooks, and hybrid PC-tablets, offer potential for a rebound in PCs, but smartphones and tablets are expected to continue taking share.
- Manufacturer and retailer margins will continue to be pressured by product commoditization and value oriented consumers.
- Within the retail environment, online retailers will continue to challenge the brick and mortar players.

## Online Sales Penetration



Source: ComScore, U.S. Census Bureau

Note: eCommerce share is shown as % of U.S. Department of Commerce's Total Retail Sales excluding Food Service & Drinking, Food & Bev. Stores, Motor Vehicle & Parts, Gasoline Stations and Health & Personal Care Stores



# Current Situation

The U.S. economy continued its weak recovery in 2012 but high unemployment and weak housing markets kept a lid on consumer discretionary spending. Consumer electronics industry performance from manufacturers and consumer electronics retailers was generally negative, as competition remained fierce and frugal consumers remain focused on value.

According to the Consumer Electronics Association (CEA), preliminary results indicate that growth in industry revenues slowed to 4.7% in 2012 from 7.7% in 2011.

In 2012, the mass adoption of tablets resulted in significant deterioration in demand for laptop and notebook PCs. Unit shipments of tablets totaled 80 million and increased to 66% of total shipments of PCs, notebooks and tablets in 2012. Sales increased 93% to almost \$31 billion. Despite the much anticipated release of Windows 8, the U.S. PC market struggled in the fourth quarter of 2012 as limited product offerings led consumers to continue putting off purchases.

The continued rise of smartphones has been accelerating the demise of digital cameras, GPS, and audio devices. Tablets are also likely to replace the need for DVD players. TVs with larger screen sizes and more features kept volumes steady but required much lower prices to move them. The rapid growth in smartphones has facilitated consumers' ability to price compare while shopping, resulting in the show room effect that negatively impacted many consumer electronics retailers during the year.

Even as consumers gravitated to larger screens, prices for flat panel TVs continued falling, making them much more affordable to the average consumer and may have reached saturation as evidenced by relatively weak sales. In addition, there has been little interest in the latest technologies such as ultra HD, 3D and OLED.

The continued rise of smartphones has led to declines in sales of digital cameras, camcorders, MP3 players, and GPS navigators due to the convergence of functions offered by these devices into the smartphones.

## Top 10 Consumer Electronics Retailers

Rank		Consumer Electronics Retailer	CE Sales		% Change
2011	2010		2011	2010	
1	1	Best Buy	32,470	32,397	0.2%
2	2	Walmart	20,532	19,569	4.9%
3	4	Amazon.com	12,017	7,930	51.5%
4	3	Apple Retail Stores	11,173	8,655	29.1%
5	5	Target	6,486	6,490	-0.1%
6	6	Costco Wholesale	5,051	4,978	1.5%
7	7	Gamestop	4,816	4,939	-2.5%
8	8	Dell	3,451	4,260	-19.0%
9	9	RadioShack	3,389	3,513	-3.5%
10	10	Sam's Club	2,624	2,745	-4.4%

Source: This Week in Consumer Electronics

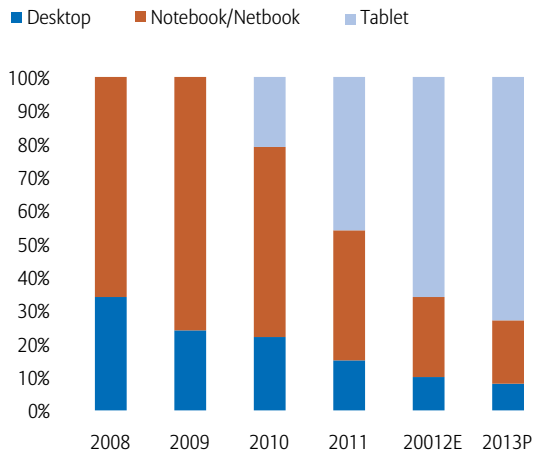
## Total TV Sets and Displays Sales to Dealers

	Unit Sales (Thousands)	Dollar Sales (Millions)	Average Unit Price
2008	31,153	\$25,827	\$829
2009	34,799	\$22,407	\$644
2010	34,659	\$20,120	\$581
2011	33,781	\$18,150	\$537
2012E	33,981	\$17,839	\$525
2013P	33,538	\$17,432	\$520

Source: Consumer Electronics Association

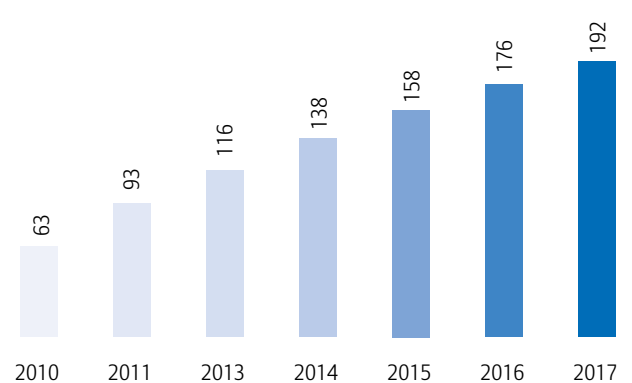


## Unit Composition of Personal Computer Volume Shipments



Source: Consumer Electronics Association

## U.S. Smartphone Users (Millions)



Source: International Data Corporation

In terms of the competitive environment, pure play consumer electronics retailers continue to feel the pressure from the general big box discounters like Walmart and Target, as well as online competitors such as Amazon.com. In fact, wide product availability of increasingly commoditized offerings, increasing online price transparency and the customers' focus on price has enabled the online channel to take share from traditional consumer electronics retailers. Many consumers have migrated to shopping on mobile devices, a trend that is expected to continue. According to TWICE's (This Week in Consumer Electronics) Top 10 CE Retailers Report, Amazon's consumer electronics sales increased nearly 52% in 2011 to \$12 billion. This performance catapulted Amazon to the number three spot ahead of RadioShack, Costco, Target and Apple, and behind only Best Buy and Walmart.

For many consumers, Best Buy and other big box retailers have become "showrooms" for Amazon.com and other online retailers. That is, consumers go to Best Buy to touch, feel and generally test the consumer electronics product and then go online to buy it at a cheaper price. In addition, new pricing applications on smartphones have made it easier for consumers to compare prices while "in the showroom".

## Outlook

Consumer electronics continues to face a number of headwinds that pressure our near-term outlook. Weak consumer spending and a lack of revolutionary products will lead to low single-digit sales increases for 2013. Demand for consumer electronics products should remain steady, driven by tablets and smartphones. Despite the growing influence of mobile based video games, sales of video game consoles should increase modestly following new console launches. Most other major categories are expected to decline.



The Consumer Electronics Association is forecasting that American consumer electronics shipment revenues will increase 2.7% in 2013 to \$209.6 billion and will be primarily driven by growth in smartphones, tablets and accessories, assuming consumers' purchasing power is not reduced.

Tablet sales are expected to increase in double digits in 2013 even though prices are expected to decline throughout the year. Shipments are expected to increase 45% to 116 million units. The popularity of tablets has at some extent replaced the need for laptops and notebooks, resulting in sluggish growth. However, with the introduction of Windows 8, more ultrabooks and hybrids, laptops are expected to perform well in 2013 with an estimated 26 million units shipping in 2013. Revenues for the overall mobile computing category (laptops and tablets) are still expected to increase 15%.

Tablet shipments, part of the Information Technology category, are the fastest growing category and are expected to sustain double digit growth through 2013 even as prices continue to decline, in part due to increased penetration of smaller screen sizes.

Within the Communications Devices category, smartphone shipments are expected to total 130 million units and sales are expected to increase 12.3% to \$37.3 billion and make up 90% of the total category.

This growing demand for mobile devices is also having a knock-on effect for accessories such as headphones, wireless speakers and sound bars. Shipments of sound bars alone are expected to rise 22% to 2.2 million units in 2013. In a December 2012 report from NPD Group, it was noted that audio accessories had seen a huge sales spike over the U.S.

holiday season. Headphone sales were up 15% and sound bars and streaming-capable speakers were also extremely popular. Sales dollars rose in those categories by 47% and 276%, respectively.

While TV sets and displays remain a crucial driver of the industry, display revenues are projected to decrease 2.2% to \$17.4 billion in 2013 as lower average selling prices more than offset the trend to larger screens and the relatively limited adoption of the latest technologies such as ultra HD and OLED. Internet-enabled TVs and streaming devices should gain traction as consumers want to enjoy streaming their favorite movies and TV shows.

In the longer term, TVs, computers, cameras and phones are all expected to converge into a mobile connected world.

As always, the key uncertainty for manufacturers and vendors are the margin opportunities given the competition. For example, 2012 saw a flood of new tablets that vendors had compete for store shelf space; 2013 is expected to see more of the same.

Consumer electronics retailers are shifting focus to capitalize on the connected device trend (smartphones, tablets, e-readers and related service plans and accessories). The online channel will also continue to grow. Research firm, eMarketer, forecasts that online sales of consumer electronics products will increase from \$48.6 billion in 2012 to \$80.2 billion in 2016. Traditional brick-and-mortar consumer electronics retailers will have to develop successful multi-channel offerings. Otherwise, they will continue to struggle to maintain sales, margins and profitability.

## CEA Sales Forecast

Factory-Level, \$ Sales, in Millions	2010	2011	% Growth	2012e	% Growth	2013p	% Growth
Video Technology	34,929	31,893	-8.7%	28,567	-10.4%	26,575	-7.0%
Information Technology	49,326	59,439	20.5%	72,868	22.6%	79,154	8.6%
Audio Technology	11,644	10,166	-12.7%	8,392	-17.5%	7,761	-7.5%
Communication Devices	26,999	35,697	32.2%	38,981	9.2%	41,595	6.7%
Electronic Gaming	23,827	23,577	-1.0%	19,834	-15.9%	17,793	-10.3%
Automotive Electronics	9,052	9,391	3.7%	10,557	12.4%	11,673	10.6%
CE Accessories and Media	19,591	19,236	-1.8%	19,367	0.7%	19,515	0.8%
Home Technology	5,463	5,369	-1.7%	5,429	1.1%	5,526	1.8%
<b>TOTAL</b>	<b>\$180,831</b>	<b>\$194,768</b>	<b>7.7%</b>	<b>\$203,995</b>	<b>4.7%</b>	<b>\$209,592</b>	<b>2.7%</b>





Source: Consumer Electronics Association - Jan 2013

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KEYS TO SYMBOLS

 Positive fundamentals & outlook	 Structural weaknesses
 Signs of weaknesses	 Imminent or recognised crisis