

Industry Outlook:

Key Points

- 1** Euler Hermes forecasts that revenues in the U.S. Consumer Electronics industry will grow by more than +1.5% in 2016 (after +1.0% in 2015) and reach USD 224bn.
- 2** Growth will be sustained by the increase in disposable personal income on the demand side and by waves of innovation on the supply side.
- 3** The market is boosted by the new products and services launched every year, the increasing convergence between current products and the rise of the Internet of Things (the interconnectivity of objects).
- 4** However, competition remains high – as does the level of risks within the sector – as innovation in itself is not always sufficient to support prices (-0.5% y/y as of October 2015) while it continues to require huge investments.
- 5** Nevertheless, we expect that new challenges will support an industry accustomed to technological leaps. In particular the digital revolution and disruption are important factors. Big changes have a massive impact on the business environment, but they also offer significant opportunities, especially in the U.S. which will boast 177 million mobile shoppers in 2016.



Consumer Electronics

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Overview – U.S. Consumer Electronics, a sector on the move

As we reflect on the highs of the annual Consumer Electronics Show (CES), an event where driverless cars, virtual reality headsets and smarter-than-smart drones were feted with much fanfare, we offer a look at realities on the ground. Consumer Electronics (CE) is a huge industry where exciting innovation, deep disruption and, alas, passing fads cohabit. The crucial point is to see where risks lurk, and what opportunities might be on offer.

2015: A slight pause

In 2015, the U.S. CE market was still growing, but not as fast as hoped. A modest +1.0% growth was due to the two main categories of products – tablets and desktops – maturing and losing steam. After a few years of robust growth, tablet sales have decreased by -9% in volume.

2016: Innovation forges on

In 2016, the market will be boosted by new and ever more connected products. Despite the dazzling and sometimes confusing visions and concepts on offer in Las Vegas, the trade show made one thing very clear: the sector will continue to be driven by innovative products. Some of them are conceptual and will never move to the industrial stage, but others are success stories, like drones (+145% in units sold forecast in 2016) or 3D printing (+64% units sold expected in 2016).

The future: Digital disruption paves the way

The age of digital disruption leads companies to focus on customers – and how they use and interact with technology. As the emphasis changes, barriers fall and new alliances are forged between companies from different backgrounds. The CE business is deeply affected by the shift. But companies also proactively facilitate the digital revolution. Revolutionary products like 3D printers redefine the relation between manufacturer, marketer and end-user.

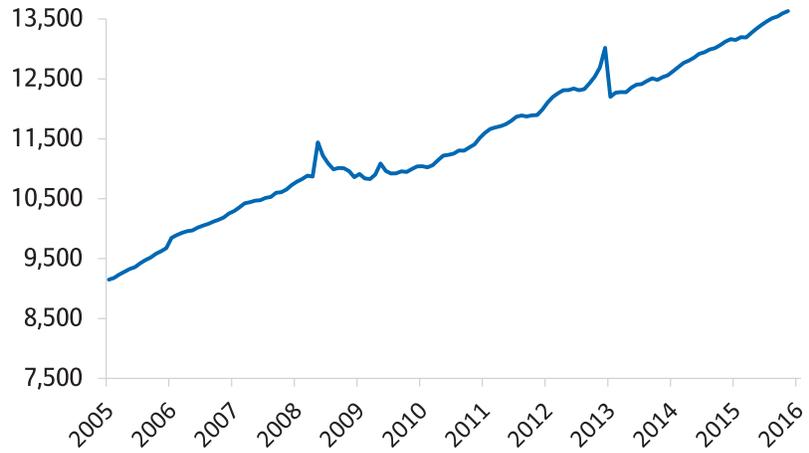
Current Environment – Rising disposable personal income vs. price pressures

Purchases benefit from a rather steady rise in disposable personal income

Since CE purchases are often discretionary, industry performance is tied to per capita disposable income. From 2005 to 2014, disposable personal income increased by +4% per year on average and they were still registering a +3.9% y/y rise in 2015 as of end of November. This important driver is expected to continue to grow more or less steadily, as the increase in salaries should remain subdued by the low inflation rate, reaching USD 13.6tn in 2016 (after USD 13.0tn in 2015) (see chart on next page).



Disposable Personal Income (in USD bn)

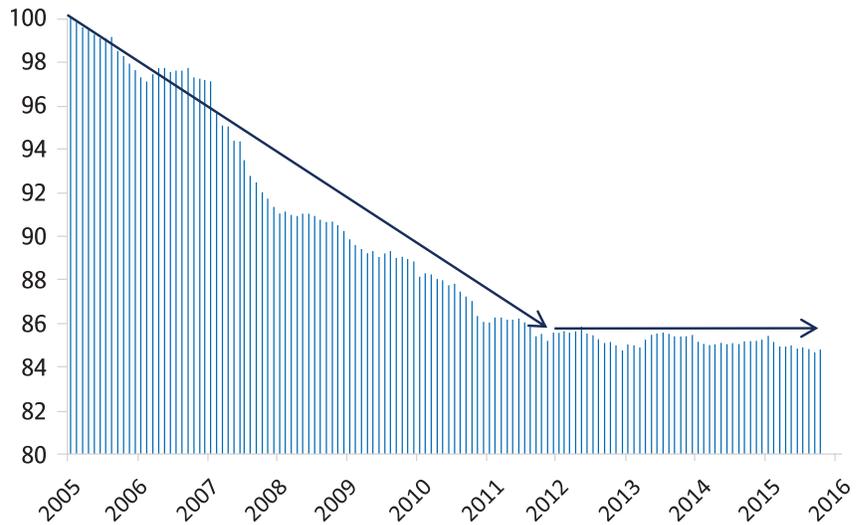


Sources: Bureau of Economic Analysis, Euler Hermes

Price pressures remain high

Despite the industry's efforts to introduce innovative products with higher added value, prices collapsed and then stagnated at a low level for several years (see chart below). This trend was due to the pressure of competition from countries with low manufacturing costs. From 2005 to 2011, the price index for computers and other electronic products dropped by -15%. Since December 2012, it has been stable and low (at a value of 84.8). In this context, the pressure on margins remains high due to fierce competition. Yet the net income/revenue ratio for the sector overall is high (7.5% in 2014). However, this is due mainly to the performance of market leaders - the most innovative companies. Those who cannot or will not innovate pay the price: fierce competition takes its toll and limits their net income/revenue ratio.

Price Index - U.S. Computer and Electronic Product Manufacturing (basis 100 in 2005)



Sources: Bureau of Economic Analysis, Euler Hermes



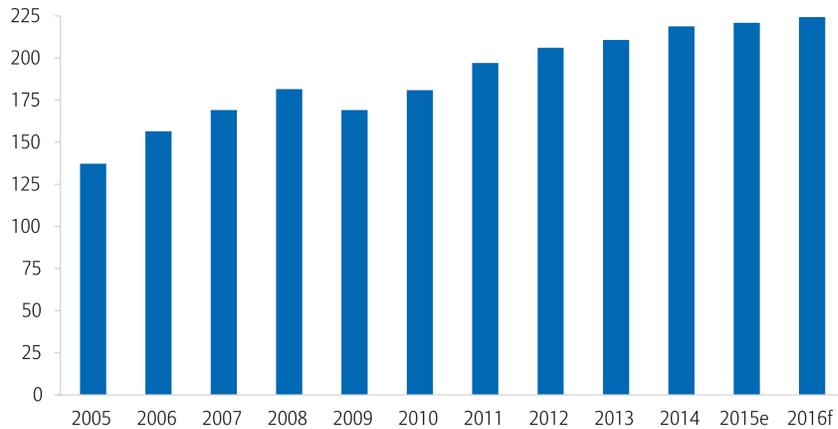
Outlook – Growth will continue for the next years

Industry revenues forecast to increase by USD 3.5bn in 2016 and reach USD 224bn

Although the U.S. economy is likely to grow by the same disappointing +2.5% pace as in 2015, the outlook for CE sales remains positive thanks to low interest rates, low unemployment and a new set of innovations.

Industry revenue is forecast to increase by +1.5% in 2016 to USD 224.3bn, after a +0.9% rise in 2015 to USD 220.9bn. However, this positive trend reflects a slower growth rate after five years of increase: +23% from 2009 to 2014 (see chart below).

Total U.S. Consumer Electronics Shipments – Revenues (in USD bn)

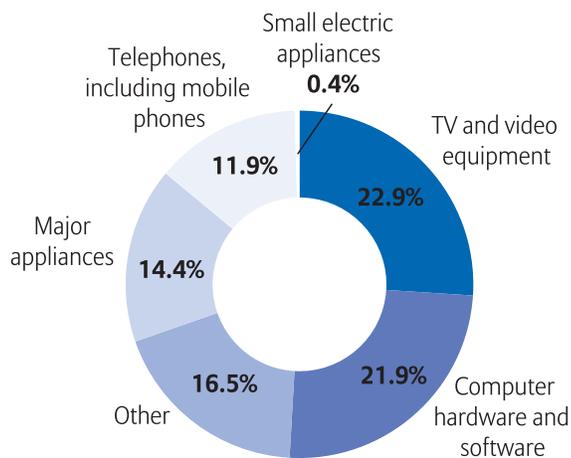


Sources: Consumer Electronics Association, Euler Hermes

From big ticket purchases to smaller, less expensive products

As an industry, CE offers a wide array of products which vary not only in price, but also in their impact. Innovation drives the market in unexpected ways. New products, like those presented at the CES, can cannibalize and dethrone a current leader and the market share of each category of products can change quickly (see chart below).

Consumer Electronics Products and Services Segmentation in 2015 (in %)



Sources: Ibisworld, Euler Hermes



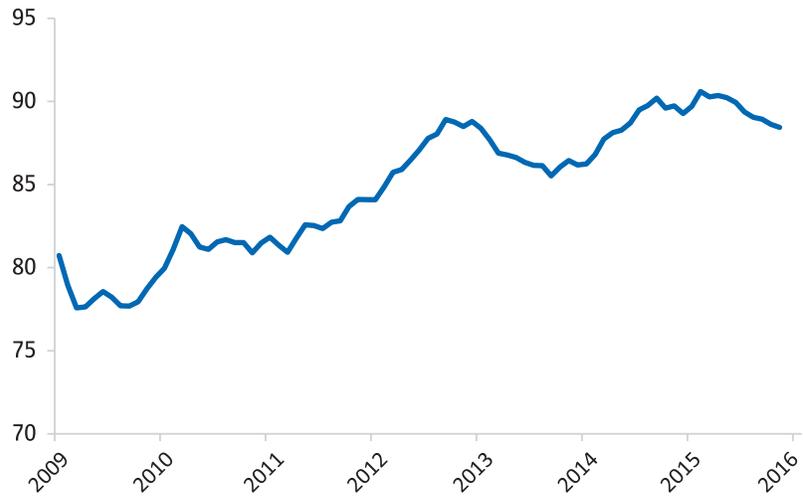
Opportunities – Consumer sentiment indexes are stabilizing at a high level

Expectations stabilizing at a high level for consumers electronics

Innovation will continue to drive the market — it is the way to attract consumers from early adopters to the masses. Moreover, it boosts customer expectations, hence their appetite for spending on new technology.

The Index of Consumer Technology Expectations (ICTE), which measures consumer expectations about technology spending, reached an historical peak in February 2015 (90.6). Since then it decreased slightly by -1.4% over the last twelve months until November 2015 (88.4 in annual average). However, the ICTE remains well above its long-term average (+4.9%) and its latest low level (+3.4% above September 2013) (see chart below).

Index of Consumer Technology Expectations – Consumer Expectations About Technology Spending



Sources: Consumer Electronics Association, Euler Hermes

What this means for your business

Favorable economic conditions including declining unemployment, improving consumer confidence, low interest rates and increases in disposable income will continue to drive demand and growth in largely discretionary consumer electronics purchases. For businesses, this favorable environment does not exclude risks. They must constantly innovate without certainty of success in a highly competitive industry, which penalize their profitability.

About Euler Hermes

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