



market monitor

Focus on consumer electronics/ICT
performance and outlook

May 2013

The future is in consumers' hands

In the world of consumer electronics and information communication and technology (ICT), nothing stands still for long. The 'slimline' desktop computers of just a few years ago may already appear quaintly cumbersome to the ubiquitous users of smartphones and pocket-size tablet PCs who grace 'free WiFi' coffee bars across the globe.

And that perception is reflected to a large degree in the current state of the consumer electronics/ICT market. As our reports on the sector's performance show, demand for traditional desktop and even laptop PCs is falling, while sales of smartphones and tablets boom: a trend that is set to continue.

In France, sales of tablets rose 140% in the last quarter of 2012 while, in the US, unit sales of tablets are expected to reach 116 million this year. But, even within this segment, the picture is not entirely rosy everywhere. For instance, Japanese manufacturers are finding it hard to compete with market leaders like Apple and Samsung.

The story is the same in all the countries reviewed in this edition of Market Monitor – with smartphones and tablets bucking the trend of losses elsewhere in the sector. An important factor in this mix is the reduction in both government and company spending on large IT projects. For instance, the Dutch government has recently announced budget cuts and our report on the Belgian market highlights the reluctance of businesses to invest in IT while the economic outlook remains uncertain.

India is an exception in this respect, as its government is committed to improving India's low computer penetration, especially in its far-flung rural areas.

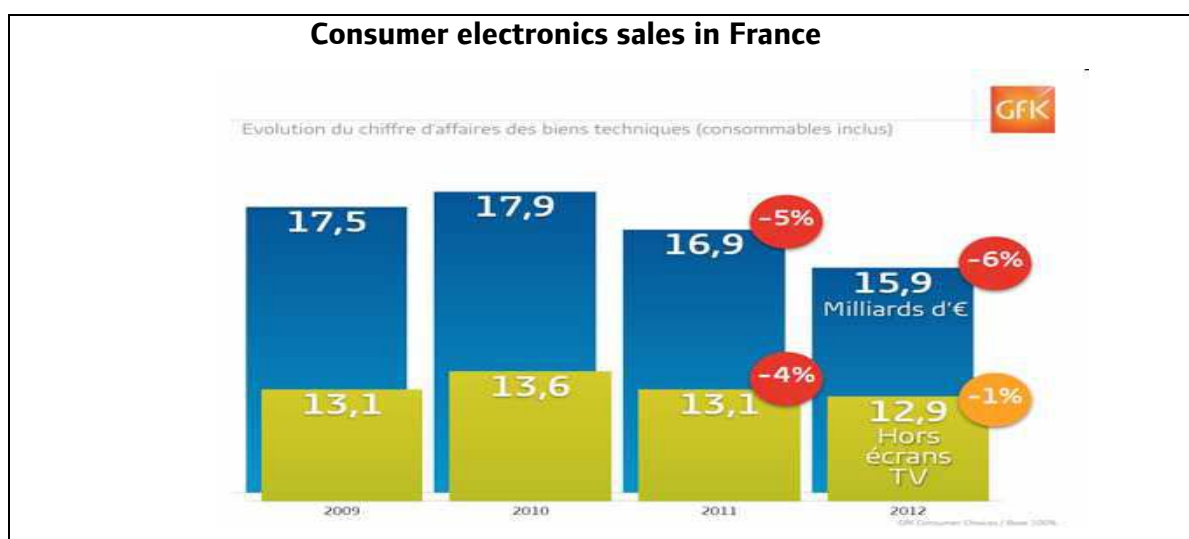
What is evident from our reports is that performance within this sector varies markedly from subsector to subsector. With smartphones and tablets the growth leaders, it is fair to say that the future of the sector is literally in consumers' hands.

France

More competition combined with lower sales



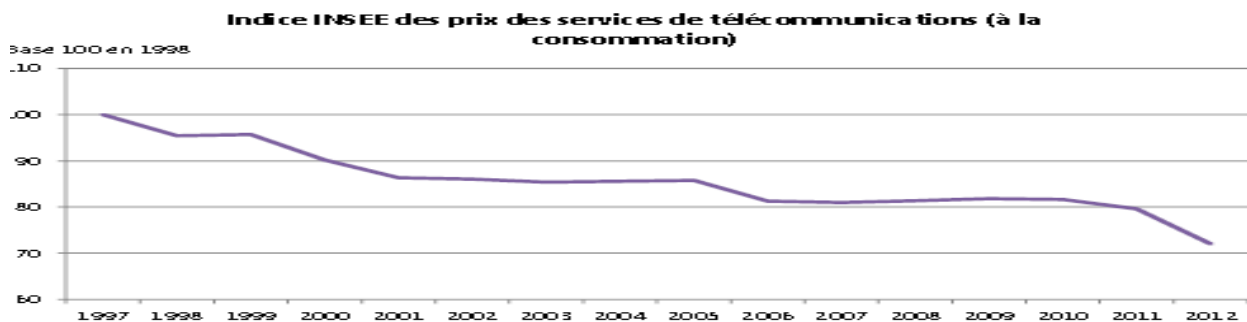
Both ICT and consumer electronics were hit by high profile bankruptcies in early 2012: for instance, those of IT service provider and hardware wholesaler Infolution and Ebizcuss.com, France's first and biggest Apple reseller. However, sales stabilised somewhat in the second half of the year and, according to the French statistics office INSEE, consumption of consumer durables increased 1.2% in Q4 while tablet PC sales even rose 140%. Nevertheless, the French IT market shrank 1% in 2012, and consumer electronics decreased 6% (down 1%, excluding TV sales - see chart below).



With both businesses and government IT budgets reduced, competition among service providers has grown while prices continue to fall. And, as IT expertise is in short supply, labour costs are becoming increasingly expensive. This combination of lower prices and higher input costs is putting pressure on companies in the IT service subsector and the market is expected to remain flat in 2013, with growth of just 1%.

Both IT and consumer electronics companies suffer from structurally tiny margins, as a result of which their equity is often no more than 15%. With this fragile solvency and weakening liquidity, the prudent management of working capital requirement is essential for survival.

In contrast to demand-driven consumer electronics and IT, the telecommunications subsector is mainly offer-driven. Mobile virtual network operators (MVNO) and distributors are seeing dramatic changes in their market environment. Faced with consumer-oriented regulation and fiercer competition now that low-cost operator Free has entered the market, every telecom player has had to reconsider its pricing and cost strategy. This has led to a massive price reduction in telephone lines (see chart overleaf), hitting operators' Earnings Before Interest, Taxes, Depreciation (EBIDTA) margins. According to the French telecommunications and posts regulator ARCEP, average margins decreased to 31.5% in 2012 from 34.3% in 2011.



Source: INSEE

However, with the expansion of voice, data, and sms traffic, companies are forced to invest in infrastructure and innovation such as 4G and fibre in order to support higher volumes and maintain their competitiveness. As a result, investments rose to EUR 9 billion in 2012 from EUR 8.2 billion in 2011 (up 9.7%), according to Arcep. That investment has required cost cutting elsewhere, and businesses have now begun to cancel their distribution arrangements with wholesalers so that they can streamline their own distribution channels and increase their share of internet sales. Their aim is to increase their own distribution revenues and avoid sharing their already tight margins. Despite this, telecommunications operators are still strong in comparison to other consumer electronics/ICT subsectors, as they have benefited from massive EBIDTA margins and cash flows in past years. Their size and level of capitalisation means they can absorb losses from the current market turbulence, although retail networks may be affected by lower consumption and weaker support from operators.

The economic environment for the rest of 2013 does not bode well for the consumer electronics subsector. Private consumption is expected to be flat this year, with unemployment forecast to remain above 10%. The French consumer electronics market will continue to shrink, although e-commerce and m-commerce (cell-phone purchases) are seen as high potential growth drivers that will buck the overall trend. In the long run, traditional retail cannot survive without online sales, and small independent shops will therefore see their sales fall dramatically in 2013. Larger businesses, such as Fnac and Darty, will also suffer from lower household consumption, but their current reorganisation plans are designed to achieve the right balance between online and bricks-and-mortar sales. Those larger players are far more resilient than smaller companies and have the capacity to overcome the current crisis.

In the IT subsector, B2C business will undoubtedly continue to benefit from the boom in sales of tablet PCs, which will compensate for the drop in sales of traditional laptops that usually generate higher margins. In addition, we see a trend of convergence between communication and consumer electronics products which will probably lead consumers to update their devices (eg: 'Phabett'= Phone+Tablets; or tablets with a removable keyboard). However, as far as B2B is concerned, budget restrictions and poor business expectations will lead to reduced or even cancelled IT investments - and the same goes for sales to public bodies. However, businesses are seeing the benefits of, and indeed the need to change to, cloud-computing and this will compensate to a degree for the drop in other IT investment. The software sub-market will therefore be sustained by the expansion of SaaS (i.e. Software as a Service). This year a slight increase of 0.7% in the French software market is expected while hardware sales will decrease. Software services should stay positive, with growth of 1%. In telecommunications, prices will continue to fall and operators' margins will decrease. However, to comply with the regulatory threshold regarding network coverage, and also to maintain market share, operators will continue to invest significantly in broadcasting infrastructure.

More payment delays and insolvencies in 2013

At year-end, it is common practice for suppliers to grant longer payment terms to their customers. During this period, the resulting boost to demand means that they need to hold higher stocks which they hope will be quickly converted to cash because of the increased sales. However, despite this strategy to boost sales, three factors have led to deterioration in the payment behaviour of the consumer electronics/ ICT sector in the last six months:

- consumers have waited until the very last moment before purchasing;
- unfavourable consumption conditions persist; and
- banks are often unwilling to be accommodating.

We expect payment delays to increase in the coming months, as the cash reserves of many ICT buyers have suffered from the erosion of both sales and margins. In addition, credit facilities (although currently at their cheapest level for years) are still subject to strict conditions imposed by the banks. As a result, there is little if any cash elasticity for most of the buyers in this sector. We also expect insolvencies in this sector to increase this year. Weaker sales and tighter margins mean that companies must be flexible enough to quickly adapt their product mix and their distribution channels to meet rapidly changing market conditions. If businesses cannot make those changes it is unlikely that they will stem the drop in sales and haemorrhage of cash.

Given these circumstances, our underwriting stance is cautious. When assessing buyers' creditworthiness, our main focus is on short-term cash availability, either owned or borrowed. It is also essential for us to thoroughly understand a buyer's business model, especially where they have high credit exposures. This means understanding how they manage their customer credit risk and their own supplier dependency, and also the accuracy of their information systems, i.e. the tools that enable them to manage in real time the two key factor in this industry: their stocks and orders. To maximise the cover that we can offer to our customers, we seek as much up-to-date financial information as possible from their buyers. That will allow us either to agree a realistic level of cover – even if that is subject to more stringent review – or at least to explain the reason that we have to restrict cover: either way, our aim is to protect our customer from unnecessary financial risk.

French consumer electronics/ICT sector

STRENGTHS	WEAKNESSES
Innovation drives consumption	Household consumption may continue to drop
Buyers are adapting their product mix	B2B activities are affected by budget reductions
Cross channel strategies can create synergies, develop sales and save costs	Small retailers are finding it hard to stay competitive

Japan

A downbeat picture



In 2012, and so far in 2013, the performance of Japanese consumer electronics manufacturers has been sluggish, as competition from Korea and other Asian countries intensifies. Sales of white goods have been stable but there has been a noticeable slump in the sale of digital appliances, with falling demand for digital TVs. The overall poorer performance has led major electronics manufacturers to begin downsizing their operations. In the area of ICT, the telecommunications subsector is seeing varying developments. The number of fixed-line phones has been falling since 2005 (down 8.9% year-on-year in 2012), while last year the number of IP and mobile phones increased 11.8% and 6.3% year-on-year respectively. Competition between telecom carriers in Japan is fierce, with the necessary increase in capital expenditure putting pressure on profit margins. In the communication devices subsector, Japanese mobile phone manufacturers are struggling despite the global proliferation of smart phones, as they lag behind foreign manufacturers such as Apple and Samsung. In information services, the business-to-business market remains sluggish while business-to-consumer - such as social networking services (SNS) - is growing, thanks to the increased use of tablet PCs and smart phones. While the software market is expanding to meet more sophisticated communication networks and hardware products, service charges have fallen in the last couple of years, reflecting the generally tighter budget of Japanese companies. Sales of PCs have decreased in recent years: in the second half of 2012 turnover fell 19% year-on-year.

The state of the Japanese electronics/ICT industry (2012 and early 2013)

	Turnover/production	Equity strength	Solvency/liquidity
Hardware (PC)	Decreasing	Average	Average
Communication Devices	Increasing	Average	Average
Software	Stable	Average	Average
Semiconductor	Decreasing	Average	Average
Electric parts	Increasing	Average	Average
Info Services (Database)	Decreasing	Average	Average
Info Services (Contents)	Increasing	Average	Average
Telecommunications (Fixed)	Decreasing	Average	Average
Telecommunications (Mobile)	Increasing	Average	Average
Consumer electronics (White)	Stable	Average	Average
Consumer electronics (Digital)	Decreasing	Average	Average

Source: Atradius

China to displace Japan as second largest ICT market

According to the Japanese Ministry of Internal Affairs and Communications, household consumption expenditure increased 3% in January and February 2013 compared to the previous three months. While at first sight this strong recovery in private consumption appears to be a good sign for the electronics/ICT sector, growth in private consumption is expected to slow in the coming months: with modest growth of 0.8% for the year compared to 2.4% in 2012. For that reason, the European Information Technology Observatory (EITO) expects subdued growth in the Japanese ICT market of 1.4% in 2013. This year China will displace Japan as the world's second largest ICT market.

The current downbeat trend in consumer electronics is expected to continue throughout 2013, although the depreciation of the yen and better than expected private consumption could prove positive factors for the sector. As long-term evolution (i.e. 4G LTE) services are expected to get into full swing in 2013, telecom carriers should be able to increase their revenues. In contrast, the development of Japan's mobile phone market probably peaked in 2012 and will start to shrink this year. In the information services subsector, a significant increase in demand for B2B services is expected, as many companies are changing their systems to Windows 8. The software market is expected to continue to thrive in 2013 in areas such as security and smart phone applications.

While the yen was appreciating, there was no major impact on the margins of manufacturers in this sector. However, as the yen began to depreciate in late 2012, this year ICT production costs will be hit by increases in the price of imported fuel: while its nuclear reactors remain switched off, Japan has to import large amounts of liquefied petroleum gas (LPG).

Our claims experience in Japan is of rapid insolvency following payment default as businesses, especially smaller ones, find it hard to survive for long after payment delay. We do not expect any significant increase in payment defaults by consumer electronics/ICT businesses this year, although more insolvencies are possible after the summer period, as the SME Financing Facilitation Act, which has helped to avert many bankruptcies, expired in March.

In view of the uncertain outlook for many subsectors, our underwriting stance for the Japanese consumer electronics/ICT sector remains generally cautious. As even the key players in the market have been struggling, we are especially cautious in the case of SMEs that are subcontractors of larger manufacturers: in the ICT subsector many SMEs have a short operating history, poor relations with their banks and a weak financial background.

Clearly, we require some financial information if we are to consider cover on a buyer. We check businesses' levels of debts and cash holdings, and the trend of their credit-to-cash cycle. For SMEs, accounting items such as loans and cash advances are carefully checked. If a buyer's performance is not in line with the market trend, we will investigate the reason. And our customers can be of great assistance in our underwriting process, as they can provide useful information about payment terms: especially if the terms have changed recently. To enable the approval of a credit limit, we can accept guarantees from parent companies, but only if the parent company is financially stable. While we can sometimes overcome difficulties in writing insurance cover simply by a visit to a customer's buyer, our Japanese customers are often unwilling to introduce us to their buyers, as they do not want to disclose the fact that they are credit insured.

Japanese consumer electronics/ICT sector

STRENGTHS	WEAKNESSES
Advanced technologies	A falling share of global markets as a result of fierce competition and the difficult market situation
Large manufacturers have strong ties with their main banks	Lagging behind in the smart phone market
Solid demand for white goods	Weak domestic demand for digital appliances
	SMEs tend to have high gearing

The Netherlands

ICT supports economic performance

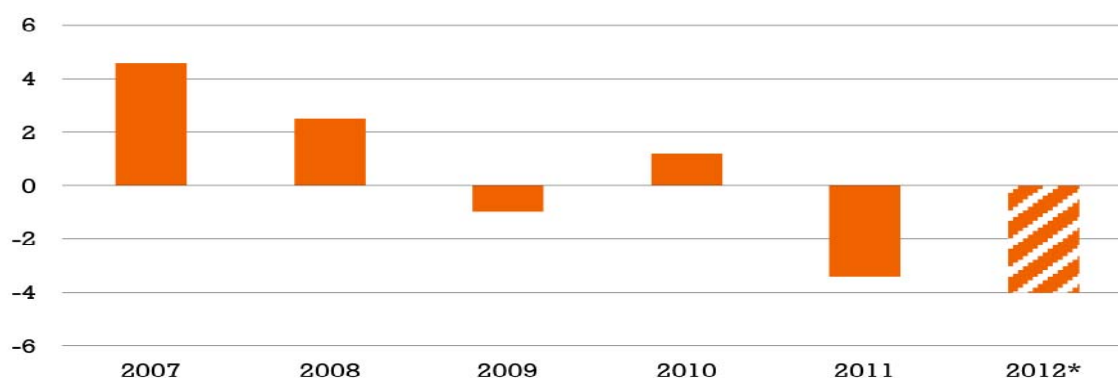


ICT is giving the Dutch economy a boost at a time of continuing economic slump, thanks to increasing mobile internet connectivity. The market for consumer electronics and ICT was worth EUR 29.8 billion in 2011, growing to EUR 30 billion in 2012. The trade association Nederland ICT now expects the market to grow slightly in 2013: by 0.3%. However, within the sector there are large variations in performance. Exports will again driver the Dutch economy this year, although the economy as a whole is again expected to shrink. Government cuts and the depressed housing market will deter consumer spending, which is forecast to decrease 1.4% - and this is bound to have an impact on the consumer electronics sector.

IT (hardware, software and services)

For the third consecutive year, the Dutch IT market achieved positive results in 2012, with revenue growth of 2.6% helped by a healthy increase in online sales. However, sales of hardware are still under pressure, with sales growth in hardware and office technology projected to decrease to just 0.4% this year as companies continue to invest in data storage and infrastructure but not in office technologies. Both public and private company spending on major IT projects is down because of the high cost and often disappointing results. As a result, leading international IT companies are feeling the effects through their falling revenue. In addition, there is considerable pressure on both prices and margins in the IT service segment. However, taken together with the Dutch government's recent announcement of forthcoming budget cuts, this will work to the benefit of small and medium-sized IT companies, which can offer an efficient and competitively priced service.

Price development within IT services (consultancy) compared to previous years (in %)



Source: CBS

Despite the rather negative outlook for hardware and IT services, there is more optimism in the software market, which saw sales increase 2.5% last year. Indeed, sales of software related to applications such as apps for tablets and smartphones rose 4% and this trend is expected to continue in 2013.

Demand for cloud services and standard applications also showed some growth. However, this has not been without a struggle, as there are still some barriers to acceptance such as safety (cybercrimes), stability, privacy and international jurisdiction. As a result, most revenues are still coming from software such as that used to manage service level agreements (SLAs).

Telecommunications (hardware, infrastructure and services)

Nederland ICT believes that telecommunication sales will increase 1.6% this year, driven by the rising popularity of smartphones. However, according to ABN AMRO, disappointing sales results in recent years, with sales falling 0.8% in 2011 and 0.5% in 2012, will continue this year, mainly in the sale of mobile phones.

Telecom companies turnover 2006 - 2012



Source: CBS

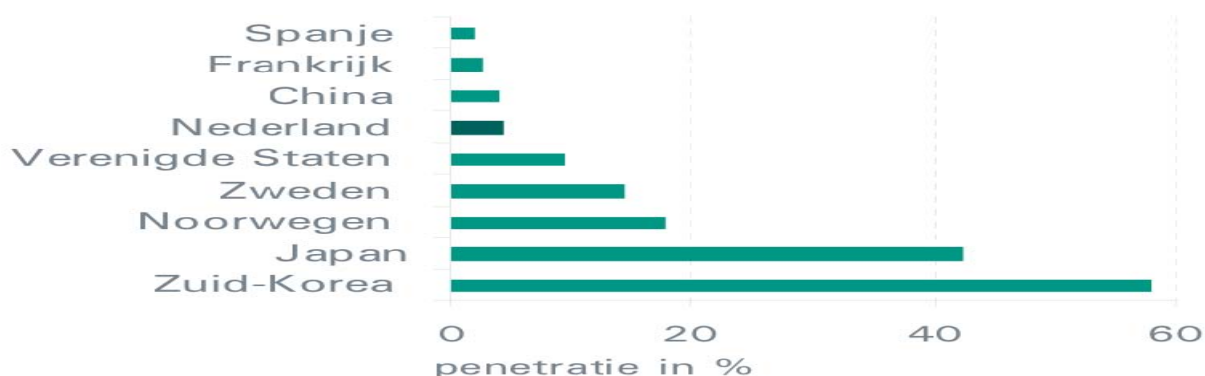
There is competitive price pressure on packet services for mobile data packages. Even though both turnover and the use of mobile data are rising, this does not compensate for the downward trend in the use of phone calls and SMS. This indicates the effect on customer behaviour of smartphones and mobile internet.

Apps such as Whatsapp and Skype are contributing to this negative effect. Providers are now trying to sell better priced mobile packages to maintain their turnover levels, while at the same time cautiously experimenting with new types of subscription: and occasionally succeeding in getting customers to change to more expensive subscriptions. Because of this, mobile services will probably continue to increase in size this year. In addition, telecom companies such as KPN, Vodafone and T-mobile have recently invested in the roll-out of the 4G network, which is expected to assist in the growth in the telecommunication market.

Fibre optic networks

The use of fibre optic networks in Dutch households is on the rise, if still at a modest level. Currently, 4.5% of households are connected to the internet through fibre optics, which is still low in comparison to other countries. A higher speed fibre optic network will not only improve connectivity but also create new possibilities such as e-commerce, just-in-time delivery, customer relationship management (CRM) and timely access to business intelligence.

Use of fibre optic networks: Netherlands vs other countries



Source: CBS

Consumer electronics

In 2012, sales of consumer electronics products totalled EUR 1.7 billion: a 15.4% decrease on 2011. Revenue from the sale of digital cameras decreased 8.3%, mainly because of competition from smartphones with their built-in digital cameras. The effect is particularly marked in the lower price segment. Sales of major household appliances also decreased slightly. However, sales of small household appliances grew for the third year running: by almost 2%. Nederland ICT expects television services to increase 2% this year, as larger screens and new features such as internet TV and 3D add to demand. In addition, growth in tablets and audio related products are an important category, which can benefit both retailers and e-tailers.

Slight increase in insolvencies expected

As already mentioned, performance differs widely across segments in the consumer electronics/ICT sector. While we have a generally cautious approach when underwriting the sector because of the overall economic picture, we acknowledge that this sector is performing better than many others. The number of insolvencies - mostly retailers - within the industry is much lower than, say, in construction and manufacturing. However, we expect a small increase in consumer electronics/ICT insolvencies this year. Our credit insurance customers and their buyers understand the value of transparency and two-way communication in helping us to underwrite risks accurately. So buyers respond positively to our requests for up-to-date information and, where we need additional information, to our requests for face-to-face meetings.

Dutch consumer electronics ICT sector

STRENGTHS	WEAKNESSES
Growth in the use of data	Double slump leading to a slow economic recovery
Increasing number of mobile phone applications	Consumer trust and business confidence remain low
Growing sales of tablets and smart TVs	

United Kingdom

A modest recovery last year



The UK is one of Europe's largest ICT markets, with the most consumer expenditure per head and an overall spend of £140 billion a year. This represents 12% of UK GDP of which the public sector contributes £18 billion. The UK also has the strongest ICT skills in Europe and the highest number of ICT graduates in the whole of Western Europe.

The ICT sector experienced a modest recovery through much of 2012, fuelled by the reinstatement of many IT projects after reduced IT capital expenditure during the previous three years. However, there is uncertainty about the strength of the recovery. The deteriorating economic situation in Europe is a major obstacle to the continued recovery of most sectors - and IT is no exception.

Telecommunications is a fairly stable subsector, dependent on a number of large Original Equipment Manufacturers (OEMs) in the UK and on capital expenditure. New infrastructure is limited and varies from region to region. Generally, the trend is towards system upgrading rather than on the installation of new infrastructure. 3G and 4G networks are due for substantial upgrades to keep pace with the growing use of smartphones, and local networking is also increasing as WiFi becomes more widely available.

Everywhere Everything (EE) is causing a stir in the market place with its monopoly over the 4G network. EE launched its 4G coverage in October 2012, 3 months ahead of the 4G auction for the remaining network providers. A similar situation was seen in the telecommunications sector when O2 had sole rights to the first Apple i-phone. Although its customer base increased when this happened, the effect was short-lived as consumers continue to be price-sensitive. It is expected that EE and its 4G coverage will follow a similar path.

Cloud services and data centres are growth segments. The annual market value of UK cloud computing is predicted to grow from £2.4 billion to £6.1 billion by 2014. Currently 18% of the UK's small to medium size enterprises (SMEs) use cloud solutions but a further 30% plan to within the next year. By 2015 half of all new IT spending by the public sector is predicted to be on public cloud services. The UK data centre market is the largest in Western Europe and the growth in the amount of data and new services such as cloud computing is creating new sources of demand. Some predictions put the rise in overall hosting and cloud services from £21.2 billion in 2008 to £70 billion in 2013.

Years of competition have led to aggressive price pressure driving down margins on hardware. Declining sales of PCs have continued to force down prices as OEMs shift excess stocks. However, the boom in tablet computing has helped to offset this. Apple has dominated this market but Samsung has an extensive offering and others will follow where these two lead. This will undoubtedly lead to price pressure on tablets and we are now starting to see this filter through.

From the perspective of their operating margins, many ICT businesses are flexible. Balance sheets do not contain properties, and most premises are leased, so that the largest operational cost remains that of the workforce. OEM support, through rebates on traditional hardware, remains as important as ever and it is often these rebates that

underpin a reseller's performance, so care must be taken when dealing with businesses that are dependent solely on such rebates for their survival.

General equity strength remains a major concern in the ICT industry: historically characterised by entrepreneurs that have sought 'get rich quick' schemes. While the channel is now far more mature, the industry is still dominated by a number of businesses whose shareholders consider it the norm to extract large dividends. This is of concern, as balance sheets remain modest compared to the scale of operations.

Despite the difficult trading environment and lower consumer confidence (see chart below) we have not seen any deterioration in payment trends in recent months. Businesses that have potential financial problems will tend to try and pay promptly to avoid 'red flags' being raised against their accounts. Business failures have tended to be driven by the withdrawal of funding and thus even prompt paying buyers can very quickly become insolvent. However, we have no reason to expect any significant change in payment practice over the next few months, unless the insolvency climate alters.



Sources: Global Insight; ICON

Retailers cause most concern

2012 was marked by the collapse of two retail giants in consumer electronics, namely Comet and Game, and we have seen an increase in insolvencies in the consumer electronics/ICT sector over the last couple of months. The post-Christmas period is when many of the weaker players in the market will fail, as company's financiers, be they shareholders or banks, will look to minimise their loss by calling in their funds at the point when liquidity is at its highest. We have therefore seen a small increase in credit insurance claims in this sector, although not of such a magnitude that would cause concern: our prudent underwriting approach is to steer our customers away from evident risk of buyer failure before it has happened.

Traditional retailers with sizeable store portfolios are experiencing the worst of the economic downturn. Many are tied into lengthy store leases, with landlords unwilling to renegotiate the terms of the lease. As a result, retailers have been unable to close loss-making stores and this has been the cause of numerous recent failures on the high street. Many other well known brands could fall victim to insolvency in the next 6 to 12 months.

Because of the muted growth prospects for the UK, our underwriters are monitoring the consumer electronics/ICT sector closely: identifying potentially risky buyers and seeking updated financial information to justify a realistic level of cover. Evidence of healthy cash flow and stock management is essential. By focusing on those buyers that show a negative trend, we can advise our customers on the best way forward for them.

We have built strong relationships with most of those buyers on whom we offer significant levels of cover, and this means we can react swiftly to any positive or negative developments.

British consumer electronics/ICT sector

STRENGTHS	WEAKNESSES
Ready availability of business information	Strong competition puts pressure on margins
Consolidation removes the weaker players	Dependent on OEMs
Cross channel strategies can create synergies, develop sales and save costs	Credit line constraints

United States

Smartphones and tablets lead the way



According to the Consumer Electronics Association (CEA), revenues for the US consumer electronics industry are expected to grow to a record US \$206.9 billion in 2013, up nearly 3% year-on-year. This follows 5% growth in 2012, to US \$204 billion. Manufacturers such as Apple and Samsung continue to lead the industry in both innovation and earnings.

As we have seen from the restructuring efforts of companies such as Best Buy and Radio Shack, the consumer electronics sector continues to see a product shift towards mobile devices including tablets and smartphones. This shift continues to mark a defined trend in consumer preference towards the portability of both devices and information. Smartphones are expected to continue to be the primary revenue driver within the industry in 2013: according to CEA, US unit sales of smartphones are expected to grow from 111 million to 130 million. In addition, tablet computing will continue to record double digit growth in 2013, with unit sales expected to reach 116 million. While the PC market continues to shrink, laptop/notebook computer sales are expected to rise in 2013. Manufacturers continue to capitalise on the success of specific products by each year releasing next generation models which provide only marginal improvements. This supports a short consumer product life cycle within the industry. The CEA expects US consumer electronics shipments to increase again in 2013 (see chart below)



Despite the pricing and margin pressure experienced within the flat screen television sector over the past few years, manufacturers continue to drive innovation. According to the CEA, a record 30.4 million LCD TVs are expected to be shipped to dealers in 2013, creating around 15 billion in revenues. Internet connected displays and 3D functionality are two of the primary differentiators within this subsector. In addition to tablets, smartphones and televisions, a number of other product categories continue to see significant innovation and to drive revenues within the consumer electronics sector, including headphones, soundbars, digital imaging products, and set-top boxes.

The low barriers to entry within the consumer electronics accessories market has led to significant competition. Many manufacturers are attempting to cash in on high margin accessories with their own take on smartphone and tablet

cases, headphones, and screen protectors. This has led to increased consumer choice - and retail competition. As can be expected, there is also a wide variation in quality.

Within the ICT segment, we continue to see consolidation efforts among the leading mobile operators, including Verizon, AT&T, Sprint and T-Mobile. While AT&T's 2011 bid for T-Mobile was blocked by regulatory issues, T-Mobile is now trying to acquire MetroPCS in order to expand its available spectrum and LTE coverage. Limited wireless spectrum continues to be a major concern in the ICT industry as wireless networks attempt to keep pace with demand. The US Congress has authorised the Federal Communications Commission (FCC) to hold voluntary incentive spectrum auctions. The FCC expects this type of auction to provide necessary financial support to television broadcasting companies and increased spectrum availability to mobile networks.

According to Gartner Inc, spending on IT will increase 4.1%, to US \$3.8 trillion, in 2013. While the US sequestration and the rise of Cyprus' debt burden are affecting discretionary spending, IT initiatives will continue. As can be seen from the chart below, global telecom services will continue to represent the largest IT spending market as firms continue to prioritise information storage and security. Gartner projects that declining spending on voice services will be offset by continued growth in spending related to mobile data services.

Worldwide IT spending forecast (billions of US dollars)

	2012 Spending	2012 Growth (%)	2013 Spending	2013 Growth (%)	2014 Spending	2014 Growth (%)
Devices	665	9.0	718	7.9	758	5.7
Data Center Systems	141	1.9	146	3.7	152	4.0
Enterprise Software	279	3.5	297	6.4	316	6.7
IT Services	878	1.5	918	4.5	963	4.9
Telecom Services	1,655	-0.4	1,688	2.0	1,728	2.4
Overall IT	3,618	2.1	3,766	4.1	3,917	4.0

Source: Gartner (March 2013)

In February 2013, the Semiconductor Industry Association (SIA), which represents US leadership in semiconductor manufacturing and design, announced worldwide semiconductor sales of US \$291.6 billion in 2012: down 2.7% from the record total of US \$299.5 billion in 2011. The industry was aided by the extension of the R&D tax credit through 2013 which was approved by Congress as part of the 'fiscal cliff' deal. The industry represents one of America's top exporters, employing nearly a quarter of a million workers and continuing to be a job creation leader in the US economy.

While the US semiconductor market shows signs of growth, there is ongoing economic and policy uncertainty surrounding possible future trade restrictions. The pending federal government budget cuts could also impact key semiconductor research programmes at federal agencies such as the National Science Foundation, the National Institute of Standards and Technology, the Defence Advanced Research Projects Agency, and the Department of Energy Office of Science. In addition, the significant trade in counterfeit semiconductors continues to be a concern from the standpoints of both the economy and national security.

While we did not see significant insolvencies in the electronics/ICT sector over the course of 2012, we continue to closely monitor several retailers that are dependent on the industry. The industry still suffers from considerable pricing pressure from increased competition and promotional activity.

Payment terms are generally between 30 and 90 days. When payment delays occur within the electronics sector, they generally relate to disputes over product pricing. Manufacturers often offer 'price protection' or discounts on products in order to move inventory ahead of the rapid innovation of technology experienced in the market. This can lead to disputes and ultimately an increase in non-payment until the issues can be resolved. Supply chain constraints, such as those experienced in 2011 following the natural disasters in Japan and Thailand, can also lead to increased disputes.

A cautious approach, as there are underlying problems

We maintain a cautious outlook and underwriting stance for the consumer electronics/ICT sector, despite the persistent growth rates mentioned above. While manufacturers continue to bring a steady stream of new products to market, many of these products are reiterations of previous innovations, as companies release next generation products with only marginal technological improvements. At the same time, the US economy is experiencing steep unemployment, stagnant wages, high gas prices, and rising taxes, putting increased pressure on discretionary spending. This has led to tougher price competition amongst consumer electronics/ICT retailers and more promotional activity, cutting margins and causing competing firms to reduce their expenses. The traditional brick-and-mortar retailers continue to be embattled by the growing e-commerce sector and the anticipated online sales tax legislation being reviewed in several states should be closely monitored. Our caution extends to the accessory market which, while offering a higher margin product mix, also has low barriers to entry and significant price competition. We will therefore continue to monitor closely the inventory management practices of firms in this sector.

US consumer electronics/ICT sector

STRENGTHS	WEAKNESSES
Semiconductors are used in many products, and the end users/markets are very diverse across a wide range of industries	US macroeconomic factors, such as high unemployment, stagnant wages, and high fuel prices, continue to affect consumer spending and enterprise IT expenditures, putting increased pressure on both manufacturers and retailers
There is a great deal of product innovation in the US, with Apple the strongest example, through products including the iPhone and iPad	Highly competitive industry leading to increased pricing pressures and promotional activity
Strong demand for mobile technology and network capacity has led to increased private, public, and government spending on network infrastructure and broadband capabilities	Capital intensive requiring heavy research and development to keep pace with the industry's technological advancements

Belgium

A flat business year expected



In 2012, computer sales in Belgium rose 5%, to EUR 1.6 billion, and in Q4 sales increased 9%, to EUR 460 million, due mainly to high demand for tablets and smart phones. In the B2B segment, we saw a 2% increase in sales of office supplies, while sales of radios, TVs and cameras fell 14% overall - and as much as 28% for cameras and 22% for flat screen TVs. Currently, the economic environment and rising unemployment are adversely affecting consumer confidence in Belgium. However, although consumer spending and retail sales are generally under pressure, sales of technological consumer goods have so far remained relatively stable. But, together with decreasing sales, falling prices of electronic mass consumer products is piling pressure on the margins of electronics retail stores. Last year, the sector suffered the bankruptcy of an important player, Photo Hall, which fell victim to the 'double whammy' of declining turnover and falling prices. Some of Photo Hall's stores have been taken over by the Krefel Group, but 47 stores closed with the loss of 230 jobs.

We expect sales in this sector to remain flat in 2013. In the current economic environment, most companies are delaying their investments: particularly in the field of IT hardware and maintenance. Sales of smartphones and tablets increased steeply in 2011 and 2012, making their outlook more optimistic. The games subsector is affected by the availability of downloads from the internet and the development of games on tablets. In 2012, Belgian consumers bought six million video games for a total of EUR 200 million, a 9.8% year-on-year decrease. This trend will continue in the coming years and may pose a real threat to this subsector.

On average, payments in the consumer electronics/ICT industry take between 60 and 90 days. We have seen no increase in payment delays during the last couple of months and expect payment behaviour to remain stable. Compared to other Belgian industries, the consumer electronics/ICT sector's default/insolvency rate is good and, despite the difficult business environment, we do not expect any significant increase in insolvencies in the industry. Our underwriting approach remains open and we always seek to provide cover that meets the needs of normal trade. However, for the reasons already explained, we are more cautious when underwriting the video games subsector.

As well as seeking annual accounts and interim figures from the companies whose creditworthiness we are asked to assess, we closely monitor their stock levels, trade creditors and debts, and if necessary the trading experience of our customers. If we have any doubts about the financial stability of a company that we are underwriting, or if we have a particularly high financial exposure on that company, a visit will be arranged to discuss their business development and to obtain the most recently available financial information.

Germany

Equity strength can be a concern



According to the German Federal Association for Information Technology, Telecommunications and New Media (BITKOM), overall consumer electronics/ICT sales will grow 1.4% in 2013, to EUR 153 billion, after 2.2% growth in 2012 (see chart below). All segments are expected to see increases, apart from consumer electronics (-3%), IT hardware (-0.3%) and telecommunication services (-1.6%). Consumer electronics is shrinking because of falling prices and shifting demand to smartphones and tablets, booming sales of which are set to continue. Cloud computing (an important trigger for growth of software and services) will increase 53 % to EUR 4.6 billion.

Consumer electronics/ ICT Germany	Market Volume (in billion EURO)				Growth Rates		
	2010	2011	2012	2013	11/10	12/11	13/12
Total ICT + CE	145.9	148.0	151.2	153.3	1.4%	2.2%	1.4%
Consumer Electronics	13.1	12.4	12.4	12.0	-5.8%	0.4%	-3.0%
ICT	132.8	135.7	138.8	141.2	2.1%	2.3%	1.8%
Information Technology	69.1	71.5	73.4	75.0	3.4%	2.7%	2.2%
IT-Hardware	20.5	21.0	21.4	21.3	2.4%	1.7%	-0.3%
Software	15.5	16.2	17.1	17.8	4.9%	5.1%	4.6%
IT-Services	33.1	34.2	34.9	35.8	3.4%	2.1%	2.5%
Telecommunication	63.7	64.2	65.4	66.3	0.8%	1.9%	1.3%
TC-Terminals	6.2	7.1	8.3	9.8	13.8%	17.3%	18.0%
TC-Infrastructure	5.7	5.9	6.0	6.1	2.7%	1.3%	2.2%
TC-Services	51.8	51.2	51.2	50.4	-1.0%	-0.1%	-1.6%

(Source: Bitkom, EITO, March 2013)

In general, businesses in all subsectors (information technology, telecommunications and consumer electronics) have below-average equity strength. Profit margins are tight because of fierce competition, particularly on price. The general solvency and liquidity position of ICT businesses varies from tight to sufficient, with companies often using factoring as a means of financing.

On average, payments in the consumer electronics/ICT industry take between 30 and 60 days. We have seen no increase in payment delays over the past couple of months and, with a positive outlook for 2013, we expect this to remain unchanged. According to Bitkom, in 2012 insolvencies in this sector decreased 1.1% year-on-year, after an 11.1% drop in 2011. We expect insolvencies to level off this year.

Consumer electronics/ICT is a very fast and innovative industry, with generally good growth prospects, but low margins, sharp price erosion and steep competition lead to an ongoing trend of consolidation. Unless they are well-established in niche products, smaller companies are - and will continue to be - the losers in this cut-throat competition.

Against this background, our underwriting approach is necessarily selective, and we require comprehensive information on each company we underwrite. If we are to agree cover we need to have the most recently available insight into the company's performance, including:

- annual accounts
- interim accounts (not older than 3 months)
- overview of liquidity status (including bank facilities provided)
- business forecasts.

To maximise our customers' insurance cover on buyers in this sector we obtain as much information as possible (e.g. quarterly reports, liquidity budgets, personal visits). If as a result we have to restrict cover, we explain the reason fully to our customer to help them plan their future sales strategy.

Generally, we limit our cover on companies that have operated for less than one year, unless they are part of, or a spin-off from, a larger group. Retention of title is mandatory as this adds a sensible level of protection to the sale of goods. Normally we will review our credit decisions annually, with additional reviews of problematic subsectors or in cases where we see difficulties. Because of the dynamic nature of this market, we need to react immediately to negativity in a company's creditworthiness or operating results.

India

More high growth in 2013



With a growth forecast of 13.9% in 2013 (according to the European Information Technology Observatory - EITO), India's consumer electronics/ICT sector is among the fastest growing in the world. IT spending is forecast to reach INR 1,064 billion (US \$19.52 billion) in 2013, up 12.8% on 2012, according to Business Monitor International. Government IT procurements at both state and federal level will help to generate spending and provide good market opportunities for vendors, while consumer spending is expected to remain the main PC market driver in 2013, accounting for 50% of sales. Indian consumer electronics spending will grow around 17% this year, to US \$37.5 billion, driven by rising incomes and growing affordability. In particular, there will also be strong growth opportunities in 200 to 400 of India's smaller cities, where vendors are expanding their retail and distribution presence. Mobile computing products, including notebooks, net books, tablets and hybrids, will continue to be the fastest growing segments this year. Realisation of the market's long-term potential depends on raising India's low computer penetration and on the government's ambitions to connect the vast rural areas to the outside world. The next layer of tier 3 and tier 4 towns, beyond the top 75 cities in India, is expected to be the major growth driver for the next few years, as PC penetration increases.

Overall, Indian consumer electronics/IT companies have reasonably healthy finances, while profit margins differ from business to business. Hardware/electronics manufacturers' or resellers' margins are typically lower but with high volumes, while in software/services the value proposition comes into play: i.e. niche product offerings to a smaller client base leading to better margins and healthy profitability. The biggest concern in this segment is currency fluctuation, as exports account for most of the revenue. The depreciation of the rupee against the US dollar has also been a problem for importers. All the major companies are either publicly listed, like TCS, Infosys and Wipro, or operate as private limited companies, with the parent company holding a majority shareholding, such as Sony India, LG and Samsung. Additionally, many Indian IT companies are listed on NASDAQ. Issues with liquidity and solvency typically arise with IT hardware resellers, which are mostly proprietorship/partnership companies working on very low margins. Multiple sourcing and tougher competition can lead to increased volatility in revenue growth for some IT companies, while margins are expected to decline slightly this year. The trend towards shorter length contracts will also lead to higher customer attrition rates and will impact margins, as will rising client acquisition costs. Nevertheless, an increase in resource utilisation levels and gains in higher value-added consulting segments are likely to contribute positively to margins. Our underwriting stance for this sector is generally relaxed and based mainly on financial strength and trading experience. Top buyers are national IT distributors or large software/hardware companies, which are either publicly listed or privately owned by strong groups. However, most buyers are IT resellers, which is where difficulties arise. These are often partnerships/proprietorships that are not obliged to file their annual accounts with the Registrar of Companies (ROC) and are usually unwilling to share that information with agencies or clients. Private limited companies file accounts with the ROC, but delays in filing are not uncommon and so we sometimes need to request financial information via our clients. IT resellers are therefore scrutinised more closely. If requested by a client, we may consider cover for more extended credit for a specific transaction or project with a large end-user. When we do need to take a more cautious approach, we look at the possibility of obtaining third party guarantees or escrow arrangements.

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