

## Industry Report: Consumer Electronics Retailers

### Recent Trends

While overall consumer spending has risen steadily since the end of the economic recession, the rate of growth within discretionary sectors such as consumer electronics slowed during the first half of 2011. According to the Consumer Electronics Association, the average U.S. household spent over \$1,100 in the past 12 months on electronics, about \$200 less than the previous year. Price points for goods such as high-definition (HD) and 3D televisions, mobile/tablet computers and smartphones have fallen in recent years as the technology becomes increasingly accessible in the consumer marketplace.

Marketplace mainstays such as Best Buy and RadioShack reported comparative store sales declines of 1.7% and 0.6%, respectively, during the first quarter of 2011. Meanwhile, same store sales also fell during the first quarter at regional electronics retailers such as Conn's, Inc. (3.9%) and hgregg (10.8%). Big box discount chains (Wal-Mart, Target, Costco, etc.) continue to fragment the marketplace by offering competitive price points for HD televisions and Blu-ray players. On top of these challenges, brick-and-mortar electronics retail businesses have been increasingly plagued by the availability of comparable products on e-commerce sites such as Amazon.com. Apple, Inc., which has opened over 300 retail locations during the last decade, has withstood this challenge by operating its stores as multi-purpose showrooms and service centers that both promote the brand and allow consumers the option of buying in stores or online.

### Appraisal Factors

Based on liquidation data and appraisal experience, Tiger Valuation considers the following key consideration points when analyzing consumer electronics retailers:

- **New-in-box inventory** – A significant portion of inventory at electronics retailers often consists of out-of-box items used as floor models or as part of display demos. The relative proportion of new-in-box merchandise to floor model inventory should be closely monitored. Unopened goods generate the highest recovery values during liquidation sales.
- **Inventory aging** – Lenders should closely monitor inventory aging, particularly within core product departments such as high-definition televisions and home theater systems. The retail electronics marketplace is predicated on short product lifecycles, thus promoting the continuous development of new product features and concepts. Consequently, state-of-the-art goods produce higher recoveries in a GOB event.
- **Brand name supplier liens** – Well-known, top-selling brands typically generate strong recovery values during GOB sales. However, some suppliers hold liens on specific brand names, allowing them to pull merchandise from stores prior to a GOB event. Lenders should monitor the amount of brand name merchandise within stores that would be unavailable in a liquidation sale. It is unlikely that customers would substitute a sale with an alternative brand if they came into the store seeking a particular label that had been pulled from the inventory.
- **Additional services and installation options** – Revenue associated with extended warranties, installations, delivery, service activation and other non-merchandise transactions can artificially inflate achievable sales projections. In a typical liquidation scenario, the amounts generated from these activities would be negotiated in an agency agreement prior to a sale. Accordingly, these services should be excluded when analyzing the retail value of a company's inventory. However, liquidators often assume these services would continue throughout the sale term as discontinuing these services would have a negative impact on the projected return to the estate. A shortage of wiring, cable stock or other items critical to installation would also adversely affect recovery values.

### Outlook

Appraisal values within the consumer electronics industry increased steadily during the 2000s due primarily to the proliferation of home computers followed by HD technology. However, the majority of American households now own at least one HD television and the marketplace is approaching saturation level for these products. Sales have been bolstered by the increasing popularity and relative affordability of mobile devices (laptops, tablets, etc.) and gaming software that typically generate high sales margins. However, industry analysts caution that the demand for these products is cyclical by nature and susceptible to rapidly changing trends. Until the next wave of must-have technology is introduced into the marketplace, industry growth is expected to be modest and liquidation values for most electronics retailers are likely to remain close to their present levels.