

The state of the smartphone market: Higher prices, lower sales, growing base

A year ago, consumer tech blogs were debating the pros and cons of smartphones priced at \$1,000 (£778). One commentator opined: "I can't just shake the feeling that paying \$1,000 for a smartphone is crazy" but added: "I ... honestly recommend you do it too".

Handset vendors appear to believe in the \$1,000 price point. Multiple smartphone models currently retail for over £778 in the UK market. Apple, Samsung, Huawei and Google all offer models priced at the equivalent of over \$1,000.

Over the last year consumers in the UK and abroad have bought tens of millions of smartphones at these prices. In Q4 2017, the iPhone X, which went on sale in November that year, sold an estimated 29 million units globally, according to Canalys. In Q1 2018 the iPhone X, which retails from £999 in the UK, was the bestselling phone in Europe, with 25 per cent share of shipments. The iPhone X also led global sales in that quarter, according to Strategy Analytics, with five per cent market share.

Higher-priced phones have had a material impact on smartphone revenues. In Q4 2017, sales value increased by 24 per cent in the UK, according to GfK, whose figures are based on aggregated point of sales data.

Higher prices, and strong sales at these price points, have however been balanced by a decline in overall sales units. GfK estimated that the UK market had declined by 11 per cent; Canalys' assessment was of an even steeper year-on-year fall, of 29.6 per cent.

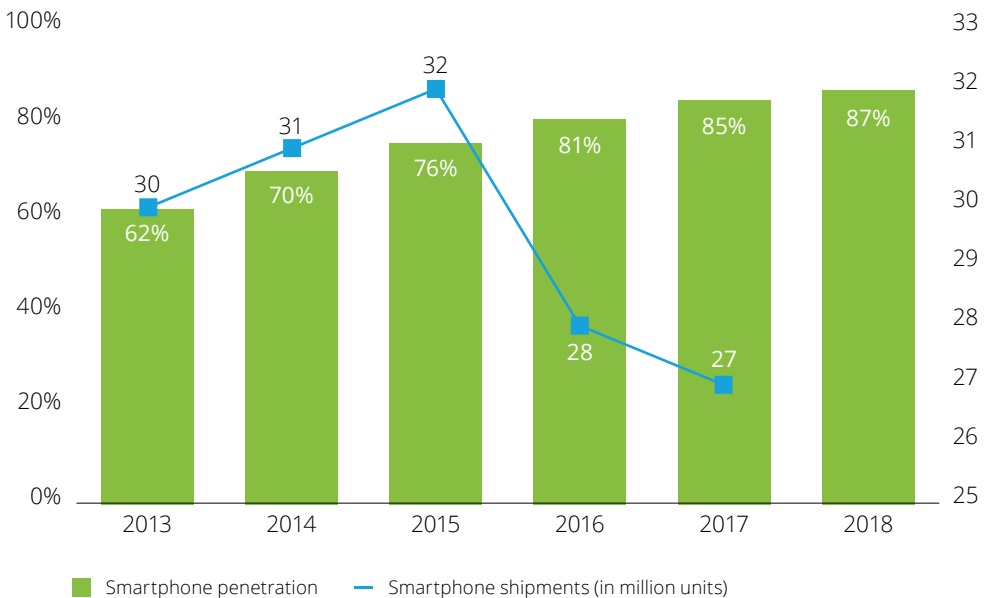
The smartphone market in the UK, and in other developed markets, has clearly rebalanced, even if the extent of the year-on-year decline in Q1 was a blip. Fewer smartphones are being sold, but the range of prices now extends to £1,000 and beyond.

The constraints on smartphone sales

The pattern of lower sales units, but higher average selling prices (ASPs), may remain in the UK in the near term, continuing the trend of the past two years (see Figure 1):

Figure 1. Smartphone penetration vs smartphone shipments (2013-2018)

Question: Which, if any, of the following devices do you own or have ready access to?



Weighted base (2013/2014/2015/2016/2017/2018): All respondents aged 18-75 years (4,020/4,000/4,000/4,003/4,002/4,000)

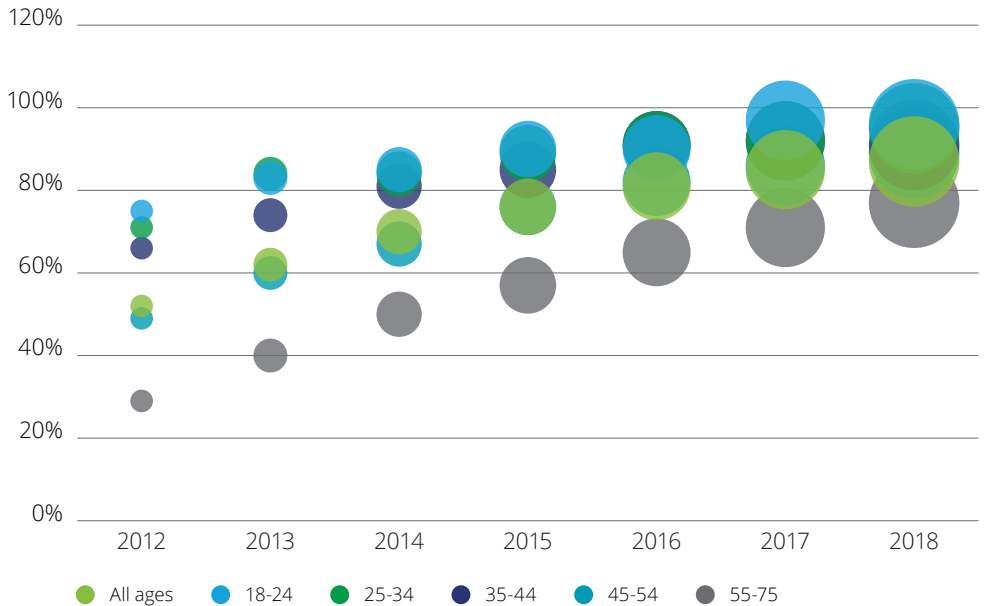
Source: for UK smartphone shipments (2013-17), Smartphone analysis, August 2018, Canalis; for smartphone penetration (2013-18), UK edition, Deloitte Global Mobile Consumer Survey, May-Jun 2012, May-Jun 2013, May-Jun 2014, May-Jun 2015, May-Jun 2016, May-Jun 2017, Jun 2018

This is partly because of the maturity of the smartphone market in the UK.

Historically, a principal driver of smartphone sales growth was upgrades from feature phones to smartphones. In 2012, according to Deloitte’s research, just over half of adults aged 18-75 had a smartphone. Now 87 per cent have one (see Figure 2). A mere eight per cent of respondents remains using solely a basic mobile phone, and some of these may refrain from upgrading out of principle.

Figure 2. Smartphone penetration by age group (2012-18)

Question: Which, if any, of the following devices do you own or have ready access to?



Weighted base (2012/2013/2014/2015/2016/2017/2018): All respondents aged 18-75 years (2,060/4,020/4,000/4,000/4,003/4,002/4,000)

Source: UK edition, Deloitte Global Mobile Consumer Survey, May-Jun 2012, May-Jun 2013, May-Jun 2014, May-Jun 2015, May-Jun 2016, May-Jun 2017, Jun 2018

A further factor is the surge, in recent years, in SIM-only contracts in the UK. Pre-pay users have opted to move to monthly payments. Some who were previously on a bundled contract have chosen an airtime only contract with operators.

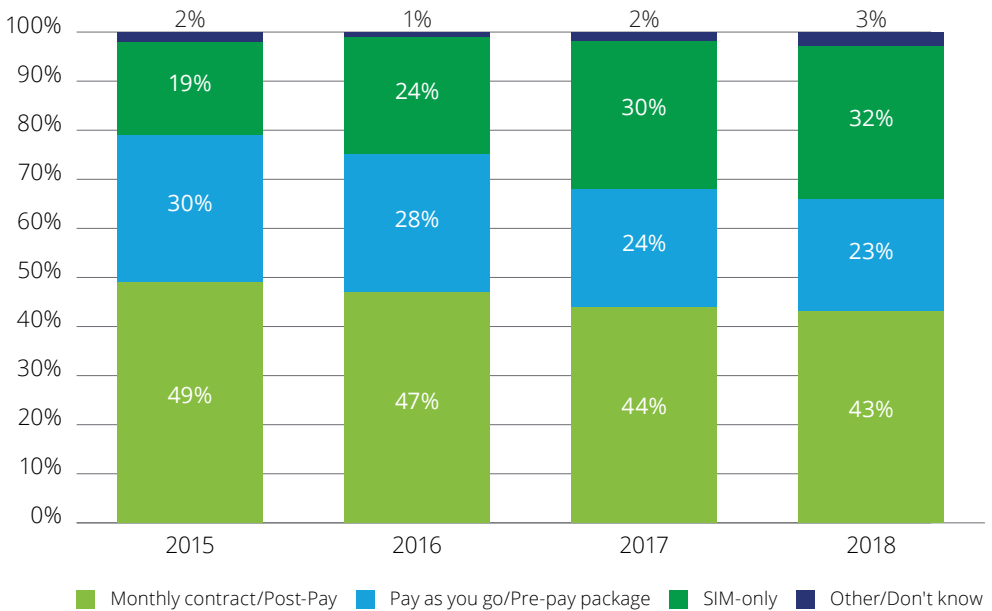
SIM-only implicitly severs the link between operator contract renewals and handset upgrades. A decade ago, new smartphones were typically bundled with a new two-year airtime contract, leading to a predictable rhythm of biennial smartphone upgrades.

A third of smartphone owners are now on a SIM-only contract. In 2015, only 19 per cent were (see Figure 3). SIM-only enables users to upgrade their airtime without upgrading their phone.

The rise of SIM-only is contributing to the slowing of the smartphone replacement cycle. Overall, smartphone owners in the UK are holding onto their phones ever longer. In this year's survey, 59 per cent of smartphone owners had acquired their device in the prior 18 months. In 2017, the proportion was 62 per cent; in 2016 it was 66 per cent.

Figure 3. Type of subscription of overall base (2015-2018)

Question: Is your phone on...?



Weighted base (2015/2016/2017/2018): All phone owners aged 18-75 years (3,682/3,712/3,794/3,795))

Source: UK edition, Deloitte Global Mobile Consumer Survey, May-Jun 2015, May-Jun 2016, May-Jun 2017, Jun 2018

A further constraint on sales of new phones has been the continuing growth in second-hand smartphones. In 2018, used or refurbished smartphones accounted for 15 per cent of the smartphone base in the UK, a two-percentage point rise over the prior year.

With every year, the second-hand smartphone market becomes more professionalised. The market has migrated from personal ads in online marketplaces to high street stores. Used phones are now available graded, boxed and warranted.

The lack of visual differentiation between different generations of smartphone may also encourage some people to settle for a three-year old, second-hand smartphone rather than a brand new one. Some may trade off a larger data SIM-only data plan for an older model of phone. And the cycle of hand-me downs between generations of family and friends continues.

Levers of growth

Smartphone sales are not fated to decline forever. There are several trends that could drive a growth in sales units in the UK market. In this section we discuss three possible drivers.

Buenas notches

A near-term driver may be the notch. This is a space at the front of the phone that houses an array of sensors and cameras. Over the course of the next 12-24 months, the notch is likely to be a factor in driving upgrades for millions of smartphone users

A lack of visual differentiation is one of the factors that may have slowed smartphone replacement cycles over prior years. Visual signifiers are a superficial but significant driver of handset replacement – owners want their new purchases to be noticed. Apple's iPhone 8, 7, 6s and 6 have a similar visual design, as do Samsung's Galaxy S9 and S8.

The iPhone X, launched in November 2017, was the first model with a notch to sell in the tens of millions of units globally. Since then dozens of new models with a similar design have launched, including the Huawei P20 Pro, the Nokia X6 and the OnePlus 6.

A benefit of the notch is that it signifies, at a glance, that the device is ne, high-end, and covetable. The notch also offers better functionality.

A camera placed at the top of the screen is preferable for selfies. While these may not be everyone's cup of tea, the calibre of front-facing cameras remains a core differentiator for millions of smartphone owners in the UK.

For higher-end phones, the notch may house the sensors used for depth facial recognition. This functionality authenticates the user by scanning the contours of the user's face, rather than just taking a two-dimensional photo. Depth facial recognition can have a far higher accuracy rate than fingerprint sensors. The ratio of false positives using the former can be one in a million, versus one in 50,000 for the latter. Further, depth facial recognition is not subject to some of the limitations of fingerprint recognition, such as struggling to authenticate moist fingers (such as after washing hands, or post exercise).

A notch is not enough. In the medium term new form factors may be required to sustain sales driven by visual differentiation. One possibility is foldable or bendable screens.

Business class smartphones

Eighty-seven per cent of 16-75 year olds use a smartphone in the UK: most of these are used for consumer applications. Yet a mere 34 per cent of the UK's 32.3 million strong work force uses a smartphone for work tasks.

The smartphone revolution has benefited the consumer, but its impact has yet to be felt at the worker level, particularly at the application level. There are apps, such as Words with Friends, that have successfully resized a board game to fit into a five-inch screen. But there are, as yet, no mainstream apps, that have been downloaded hundreds of millions of times, for every day work tasks such as task allocation, invoicing or ordering. Instead consumer apps, such as WhatsApp or even basic text messaging are co-opted for use by builders, bakers and hairdressers alike to communicate with their clients.

Workforce technology focuses on the PC, even though half of the workforce spends some or all their time away from a desk. Historically the PC was the default device for most computing tasks. Over the next year, and years to come, we would expect that the proportion of work tasks migrating in part or in whole over to a smartphone will continue to grow. And in doing so, this may require employers to issue upgraded smartphones or the self-employed to acquire higher-specification devices.

Upgrading smartphones can improve productivity, for example by distributing devices with superior camera functionality and the best connectivity. High-end smartphones' photo applications work better in low light conditions: workers that use photos or video when consulting or collaborating with other workers would benefit from having the sharpest images. Image and video based communication works best with devices that work with the fastest mobile and fixed connections.

Using smartphones or tablets can deliver benefits for more mainstream applications too. More than five million workers in the UK (15 per cent of the workforce) fill out forms on paper before copying onto a digital format; migrating these applications to a digital platform, such as a smartphone or tablet, could improve the pace, accuracy and value of the data collection.

Another reason for a company to upgrade its employees' smartphones may simply be to manage mobile devices better. While PCs are typically procured, managed, secured and maintained centrally, this is not yet the case for smartphones. According to Deloitte's research, only 16 per cent of the UK workforce's smartphones were provided by their employers. Issuing a standard device across a company's entire workforce can streamline business application rollout, centralise security updates and lower maintenance costs.

Coaching

The first smartphones appealed partly because of the intuitiveness of use. But the first smartphones also had very limited capabilities. A decade back, some models were effectively feature phones with a larger screen, and still used mostly to make calls, play stored songs and receive email.

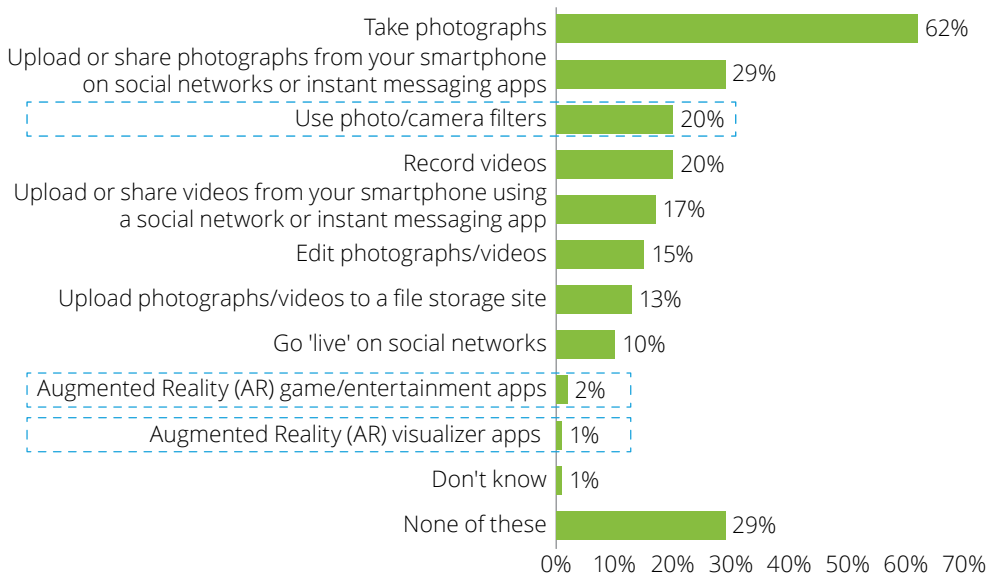
Today's smartphones are far more capable and sophisticated. High-end smartphones pack an array of functionality that may overwhelm users of all ages.

As an example, smartphone photography used to be point-and-shoot; the latest models have multiple lenses and modes. They can shoot stills and video, and hybrids of the two. They can shoot in colour and black and white. Photography on a high-end smartphone can be intuitive, for pointing and shooting. But to get the most out of it, guidance, ideally from a person who can provide step-by-step assistance, may be preferable.

Taking photos is one of the most used applications on a phone: 62 per cent of smartphone owners take photos on a weekly basis. But only a minority use the advanced functionality available. Of the weekly snappers, a fifth apply filters (which requires just a single additional click to effect), and just 15 per cent edit at all.

Figure 4. Activities performed on smartphones at least once a week

Question: Below is a list of activities that you may use your smartphone to do. Which, if any, of these do you do at least once a week?



Weighted base: All smartphone owners aged 16-75 years (3,637)

Source: UK edition, Deloitte Global Mobile Consumer Survey, Jun 2018

There are about 2,000 outlets in the UK where smartphones are sold. Few offer any guidance on how to get the most out of their phones. If more people edited their photos, this could lead to more sharing of content, and generate more network traffic as a result.

Bottom line

The smartphone sale has become more challenging. The device is more sophisticated than ever. Year-on-year upgrades are less obvious, and less tangible. All major forthcoming innovations – 5G, artificial intelligence, new generations of process – are invisible.

The industry will need to adjust to selling more on capability: appearances will still matter, but less so.

More powerful processors and faster connectivity enable a host of new applications. Some of these may take years to become useful to mainstream users.

For example, in the future smartphones should become absolutely indispensable assistants that are able to predict most actions we would want to take. They would anticipate, with a high degree of precision, not just what text we would want to write, but prior to this, would suggest whom we should communicate with, and via which communications app. The phone may also suggest, accurately, what should be attached to a photo.

In business environments, workers will depend to an increasing degree on their smartphones. Calendars will be programmed to become increasingly pro-active: suggesting how and when to travel to the next meeting; prompting when and to whom to send messages to; drafting components of each message, with writing styles customised to the preferences of the recipient; advising people when to switch their phones off.

The future of the smartphone is bright; the near-term outlook in the UK appears a little challenging. But globally demand remains strong, with over 1.5 billion shipments forecast this year. Smartphone innovation will remain unrelenting, regardless of the possible softness in the UK market.

1. Is any phone actually worth \$1000?, Android Central, 14 October 2017: <https://www.androidcentral.com/any-phone-worth-1000>
2. Media alert: Apple ships 29 million iPhone Xs in Q4 2017, Canalys, 23 January 2018: <https://www.canalys.com/newsroom/media-alert-apple-ships-29-million-iphone-xs-q4-2017>; iPhone, iPad, Siri and Apple Pay are trademarks of Apple Inc., registered in U.S. and other countries. Deloitte's Mobile Consumer Survey report is an independent publication and has not been authorised, supported, or otherwise approved by Apple Inc.
3. iPhone X remained 'comfortably' the most popular smartphone in Europe in Q1, 9to5Mac, 9 May 2018: <https://9to5mac.com/2018/05/09/iphone-x-sales-europe/>
4. iPhone X the world's best-selling smartphone in Q1 – Strategy Analytics, 9to5Mac, 4 May 2018: <https://9to5mac.com/2018/05/04/iphone-x-worlds-best-selling-smartphone/>
5. Global smartphone average sales price sees record year-on-year growth in 4Q17, Gfk, 24 January 2018: <https://www.gfk.com/en-gb/insights/press-release/global-smartphone-average-sales-price-sees-record-year-on-year-growth-in-4q17-1/>
6. Smartphone shipments fall 6.3% in Europe in Q1 2018, Canalys, 9 May 2018: https://www.canalys.com/static/press_release/2018/press-release-090518-smartphone-shipments-fall-63-europe-q1-2018_0.pdf
7. Source: Deloitte Global Mobile Consumer Survey, UK cut, May-Jun 2012, base: all 2,060 respondents aged 18-75
8. Source: Deloitte Global Mobile Consumer Survey, UK cut, Jun 2018, base: all 4,000 respondents aged 18-75
9. For more information see Deloitte member firms' Mobile Readiness for Work 2018, Deloitte Touche Tohmatsu Limited, as accessed on 7 September 2018: https://www.deloitte.co.uk/mobileuk/work/?_ga=2.50067750.1059198591.1536309704-412977467.1529667116
10. There are 57 million people playing Words with Friends at any moment, according to its publishers. For more information see Everything you need to know about Words with Friends 2, Time, 8 November 2017: <http://time.com/5013838/words-with-friends-2-review/>