

Paris, 17 June 2014

New paradigm for the electronics industry in Asia: clear dynamism, increased risks

Innovation: driving growth, generating risk

Having passed from the stage of Global Production Networks to Global Innovation Networks (which include the development of products and research activities beyond geographical borders), the electronics industry should now experience annual growth of over 3% through to 2017. With emerging Asia the new epicentre of electronics innovation, local companies are now counting on the internalisation of production and research.

However, the dynamism of the sector faces new risks, which is confirmed by the gradual rise in unpaid invoices in the region noted by Coface. In 2013, close to 3 out of 4 companies in the electronics & IT sector in Asia-Pacific experienced overdue payments, mainly in the sub-sector of electronic components and consumer electronics goods distribution.

Three major risks threaten the electronics sector in Asia

Risk no. 1: the growing gap in R&D investment capacity between the sector's medium-sized and very large-scale companies

Innovation is situated at both ends of the market, with manufacturers of semiconductors offering increasingly complex products, and the giants creating new offers (such as Google with Android). The dominance of these very large-scale companies, whose market share continues to grow, has resulted in lower profitability and lower margins for companies of a more modest size. This impact is detrimental to manufacturers of semiconductors, at the heart of innovation, who have to invest more in R&D in the face of rapid change.

- **Risk no. 2:** increased risks in electronics in Mainland China

Mainland China produces more than a third of global electronics. However, Chinese companies in the sector are particularly affected by this pressure on costs and margins, which the Coface study on payment behaviour confirms. It appears that in Chinese electronics, the number of overdue days is increasing: in 2013, 44% of overdue payments exceeded 60 days (compared to 25% in 2012). Moreover, in electronics overdue payments exceeding 150 days reach double that observed for the average of all sectors. This deterioration is mainly due to business cash flow problems and the economic slowdown in China. Companies assembling products are at increased risk.

- **Risk no. 3:** competition from Mainland China is affecting the Asian players, particularly Hong Kong and Taiwan

Hong Kong and Taiwanese economies, which are dependent on China, are very vulnerable to the slowdown in their main commercial outlet.

In Hong Kong, this dependence is increased by the fact that the entire industry in Hong Kong is now outsourced to China; this is especially true in the electronics & IT sector. As for Taiwan, electronics companies are larger than their Hong Kong counterparts and further upstream in the production chain. They are very dependent on the activity level of their purchasers, themselves severely affected by the pace of domestic demand (China) and export (United States, Europe, and increasingly Asia).

Despite increased risks, there are growth drivers

To emerge from this bad patch, the Asian electronics industry must reinvent itself. It has numerous strengths. The emphasis on innovation in the face of increasingly rapid product obsolescence, the ability of medium-sized companies to adapt to changing consumer demand and to close the existing gap with large-scale groups, equip them to stay ahead of the pack.

In the medium term, the sector's growth will be driven by, among others, onboard electronics (automotive and aerospace), electronics for the medical sector, and meeting the demands of the aging population in developed countries. The Chinese government is also preparing to take measures to promote long-term investment and cooperation between Chinese and foreign companies.

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