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KPMG/AGMA SURVEY PROJECTS GLOBAL 'GRAY MARKET' OF $58 BILLION FOR INFORMATION TECHNOLOGY MANUFACTURERS

Sale of gray market products can lead to profit erosion, brand damage

SILICON VALLEY, December 11, 2008 – Information technology manufacturers are losing up to US$10 billion in profits annually to the gray market, with as much as $58 billion of technology products passing through the gray market each year, according to the results of a new study by audit, tax and advisory firm KPMG LLP and the Alliance for Gray Market and Counterfeit Abatement (AGMA).

According to KPMG's latest estimates, the projected gray market for IT products has increased by $18 billion over the Firm's 2002 projection of $40 billion. These estimates place the size of the gray market at about eight percent of total global IT sales. However, the gray market did not grow as much as the overall IT market. As compared to the 2002 project, the overall IT market increased 81 percent, while the gray market increased 45 percent.

Gray market products are branded products diverted from an authorized distribution channel or imported into another country without a manufacturer's consent. Gray market activity persists because of fraud and abuse of distribution agreements and incentive/discount programs, according to the KPMG study. In addition, the study results indicate that the Internet has impacted the gray market specifically in the areas of pricing policy, product availability, warranty, service and maintenance.

"The IT gray market is thriving, and the Internet has contributed greatly to the volume," said Tom Lamoureux, KPMG's Global Advisory Sector Leader, Electronics, Software and Services. "Manufacturers need to understand its impact on their profits and brand integrity, and scrutinize their internal and external controls. If they want to gain control over gray market activities and improve profits, they need to improve relationships at all levels of the distribution channel.

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Likewise, channel partners need to understand their role in allowing gray marketing to thrive, and take corrective actions to address this issue."

Key findings from the study include:

- Of the OEMs surveyed, 65 percent said gray market products are discounted –on average – more than 20 percent below list price.
- 38 percent of the OEMs said that they had identified instances of inappropriate discount claims.
- More than 60 percent of OEMs said the Internet has had a very significant impact on pricing policies, availability of product, and movement of product across borders.
- Despite the magnitude of the impact the gray market can have on an IT company, 42 percent of OEMs surveyed said they do not have a process in place to identify or monitor gray market activity.

Distributors

- Distributors see the risks of the gray market, too. Sixty-three percent indicated that availability of gray market products has increased over the last two years, and as a result, 67 percent claim it has become easier to source from the gray market.
- 67 percent of distributors surveyed say they have concerns about selling gray market products to their end customers. And more than 70 percent of the distributors said their chief concerns about gray market products are poor quality and poor technical support.
- 51 percent of distributors said that their competitive position would improve if all gray market activity were eliminated.

In addition to the financial costs, which are expected to continue to grow year over year, the study shows that products sold on the gray market may pose a risk to consumers, as well. Products that travel through the gray market may be sold to unwitting consumers. These buyers may believe they are buying new branded goods, but find out only after they have made the purchase that the product is damaged, remarked, obsolete or without warranty or support, or possibly counterfeit. This can hurt a manufacturer's reputation with its customers and investors.

The KPMG study, conducted in partnership with AGMA, and supported by data developed by MarkMonitor, surveyed high-ranking executives at 189 leading IT Original Equipment Manufacturers (OEMs), channel partners and brokers . MarkMonitor also reviewed internet data for a selection of IT products. The

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survey found that distributors and brokers may often violate distribution agreements, some by using deceit, including misrepresenting end users' identities in special discount programs, or using fraudulent documentation to acquire goods from authorized sources to sell to the gray market.

About KPMG

KPMG LLP, the audit, tax and advisory firm (www.us.kpmg.com), is the U.S. member firm of KPMG International. KPMG International's member firms have 123,000 professionals, including more than 7,100 partners, in 145 countries.

About AGMA

AGMA is a non-profit organization comprised of influential companies in the technology sector including founding members 3Com Corporation, Cisco Systems, Hewlett-Packard and Nortel. Incorporated in 2001, AGMA's mission is to address gray market fraud and counterfeiting of technology products around the globe. The organization's goals are to protect intellectual property and authorized distribution channels, improve customer satisfaction and preserve brand integrity.

AGMA welcomes any technology manufacturer that owns a branded IT product. Aiming to educate a wide audience about the growing IT counterfeit, gray market fraud and service abuse threats, AGMA uses a variety of avenues to cultivate change in the marketplace, including event speaking, educational initiatives, benchmark studies, industry guidelines, and, where appropriate, public policy advocacy in areas like law enforcement and customs. To learn more about AGMA's initiative or to become a member, please visit www.agmaglobal.org.

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