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**NEW KPMG SURVEY PROJECTS GLOBAL ‘GRAY MARKET’ OF \$40 BILLION FOR
INFORMATION TECHNOLOGY MANUFACTURERS**

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

SILICON VALLEY, Feb. 20, 2003 – Information technology manufacturers are losing up to US\$5 billion annually to the gray market, with as much as \$40 billion of computer-related products passing through the gray market each year, according to the results of a new study by KPMG LLP, the accounting and tax firm.

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 discount programs, according to the KPMG study.

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 who find out

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only after they have made the purchase that the product is obsolete or without warranty or support. This can hurt a manufacturer's reputation with its customers and investors.

“Until now, this has been a largely unexamined problem, but clearly the gray market is thriving,” said Dale LeMasters, partner in charge of KPMG LLP's electronics practice. “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. Those that do stand to gain significantly.”

The KPMG study, conducted in partnership with the Anti-Gray Market Alliance (AGMA), surveyed high-ranking executives at 63 leading IT Original Equipment Manufacturers (OEMs), distributors and brokers. The 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.

Key findings from the study include:

- Of the OEMs surveyed, 62 percent identified situations where products that were discounted for a specific end user were never delivered to that end user. And 86 percent of the OEMs cited instances of inappropriate discount claims.
- Consumers don't benefit from the gray market. Survey respondents estimated that 60 percent of end users pay equally for products originating from the gray market versus products that originate from the legitimate market.
- Distributors see few benefits to the gray market, too. More than three-fourths of the distributors surveyed said they are concerned about selling gray market products because of poor quality and support issues, and 92 percent cited purchasing counterfeit products from the gray market as a main risk.

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- However, distributors and brokers are attracted to the gray market's price advantages and convenience. Of the distributors surveyed, 71 percent said they believe it's necessary to purchase gray market products to be competitive on pricing and fulfillment, yet 81 percent of distributors said that their competitive position would improve if all gray market activity were eliminated.
- Only 33 percent of OEMs surveyed have resources fully dedicated to the task of gray market issues.

About KPMG LLP

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