



Advisory Report

# The Importance of Functional Branding for Handsets

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## ■ Issue Summary

There has long been an unmet need for merging usable, basic personal information management (PIM) functionality with the common cellphone. The problem is that smartphones have been relatively expensive, bulky, productivity-oriented devices until just this past year. The march of Moore's Law – combined with the “thin” trend – has meant that there are finally attractive, super-thin smartphones from HTC, RIM, Motorola and Samsung that cost less than a PDA. Palm and Nokia also play in this space, though Palm needs to put its Treo on a stricter diet, and, improbably, getting a smartphone in the U.S. from the world's largest smartphone vendor is often impossible. Still, smartphones overall have gotten smarter, cheaper and better looking. So why is the percentage of smartphone sales stuck in the single digits?

## ■ Current Perspective

I'm a mobile devices analyst, and I test literally hundreds of gadgets a year. I change phones at least weekly and sometimes more frequently than that (playing with toys is a tough way to make a living, but someone has to do it). However, convincing my wife to “upgrade” is a lesson in how much of the real world works. There are segments of the market that can be lured by new multimedia features, or better design – even my wife succumbed to the lure of a pink RAZR – but at the end of the day, she uses her phone to make phone calls. It's certainly not that she couldn't adjust to new devices – she's considerably smarter than I am; her day job title is “Level IV Sr. Web/Database Programmer/Project Manager” or something like that. It's just that to her, a phone is a tool, and, as long as it is functioning properly, there is no need to replace it. So it's something of an event around here when I get something in that she's willing to try.

PDA sales are on the decline, but plenty of people still rely on them even for basic



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## Report:

**The Importance of Functional Branding for Handsets**

calendar and contact information management – my wife included. What were the convergence features that finally pushed her over the edge to agree to try a smartphone? The ability to synchronize the phone with Outlook, make phone calls directly from the complete contact list, and carry just a single device rather than the phone and PDA. Wow. Nothing fancy here – this has been core functionality of every smartphone for the last decade.

There has long been an unmet need for merging usable, basic PIM functionality with the common cellphone. The problem is that smartphones have been relatively expensive, bulky, productivity-oriented devices until just this past year. Consumers like my wife shunned them, and understandably so. But today's smartphones are smart, affordable and stylish. So why is the percentage of smartphone sales stuck in the single digits?

#### Distribution Channel Roadblocks

We thought the problem was one of technology, design and pricing. Pricing is still an issue – more on this in a minute – but it turns out that distribution is the major roadblock. Once we had nicely designed products like the HTC 3125 – a \$99 super-thin clamshell Windows Mobile smartphone that looks like a cross between a Motorola RAZR and a prop from Star Trek – we discovered that carriers simply can't sell them.

Part of the problem is still pricing. In order to get the price down below \$100 - \$200 with a two year contract, some carriers have tied the device's rebate to the sale of data plans. The structure of these data plans assumes that enterprise users will have their company reimburse them. This does not work for consumers buying for personal use who don't know up front if they'll ever need Web or email access, never mind know that they should be willing to pay \$20 - \$40 a month for the privilege.

But even if pricing issues are resolved, the distribution channel is still challenging for manufacturers, and the problem goes well beyond smartphones. A majority of U.S. consumers buy their handsets at carrier retail stores, where the employee helping you choose among some of the world's most complicated gadgets failed to master the Frialator at his previous job last week. Sure, that was a cheap shot, but the truth is that anyone who understands the intricacies of the voice, data and device landscape well enough to properly guide consumers through it can make more than \$8.50 an hour working retail. This is a structural issue, not an indictment of carriers per se, and of course there are exceptions.

If you're a handset vendor, the sales process itself also works against you. We've observed hundreds of retail sales sessions and they generally follow the same script:

- Consumer enters the store, looks confused (one minute or so).
- Consumer looks around at displays, picks up a handset here or there (length of time this lasts depends on how busy the store is; it can be endless or as short as 30 seconds).
- Once store employee is engaged, rate plans are discussed (five - 20 minutes).
- Consumer walks around store considering handsets, and picks handset (three minutes maximum – store employee is anxious to complete the sale and often hovers near the customer).
- Employee finishes paperwork, explains the basics of the plan. In rare instances (somewhat more often at Sprint), employee also hurriedly explains the bare basics of phone operation (three to ten minutes).

Some consumers have done research online, or know in advance that they want an advertised special or a specific product. But the majority appear to spend less than five minutes

**Report:**

**The Importance of Functional Branding for Handsets**

– sometimes much less – choosing their handset. We’ve even see salespeople actively push customers away from smartphones and multimedia-centric devices because they don’t want to open themselves up to questions that they can’t answer. There are approaches that carriers and vendors can take to help train sales staff, and syndicated research can certainly help (e.g., Current Analysis offers retail pricing tools and syndicated competitive handset analysis). However, even the best sales tools only help employees motivated enough to learn and use them. In this environment, vendors need to make products that sell themselves.

Vendors can make products that sell themselves by using brand expectations to clue consumers in to key functionality, using physical cues to help identify crucial features, and by working with carriers to implement some fairly basic – but often overlooked – retail tactics. Details for each of these strategies follow in the Recommended Actions section of this report.

Epilogue

Distribution is rarely an issue for spouses of mobile device analysts – kind public relations people FedEx devices to my door. However, my devices are often on tight loan return deadlines, and my wife is reluctant to be an unpaid mobile devices intern. Her new Palm Treo 680 in “Crimson” (red) was won in a raffle.

**Recommended Actions**

**Recommended Vendor Actions**

- One way to make products that sell themselves is to use brand expectations to clue consumers in to key functionality. Sony Ericsson has been extremely effective using Sony’s Walkman brand to sell music capabilities to consumers even on handsets that (at least at first glance) appear to be regular phones. In Europe, the company is doing the same thing with Sony’s Cyber-shot and Bravia brands.
- Similarly, devices that bear RIM’s BlackBerry brand can be assumed to do mobile email even without full QWERTY keyboards, which has helped sales of RIM’s Pearl, while Samsung’s t719 – which has the same key layout as the Pearl – has languished on the shelves. Palm’s brand is associated with electronic organizers, and if Palm were to ever launch a clamshell device, consumers might reasonably assume that it allows them to synchronize calendar and contact information even though it does not look like a PDA.
- When your brand doesn’t adequately convey the message, one approach is to create a new one, or co-opt someone else’s brand. Nokia does both with its Nseries sub-brand for high end multimedia handsets. For its imaging-centric Nseries “multimedia computers” (Nokia’s term, not mine), Nokia stamps “Carl Zeiss optics” on the case, in exclusive association with the lens maker.
- Another effective alternative is to make your product’s unique selling proposition (USP) visually obvious. Verizon Wireless asked LG to butcher its beautifully minimalist Chocolate design by putting a fake scroll wheel on the front, highlighting the product’s music capabilities. It was a hit. Similarly, QWERTY keyboards mean messaging. Motorola’s work-oriented iDEN handsets are big, clunky and look like they are built to withstand a beating. Nextel built an entire business on them.
- As you might expect, bribes work (they’re called “spiffs” or “sales promotions” at retail). Other retail strategies include helping customers help themselves. Every television set

## Report:

**The Importance of Functional Branding for Handsets**

comes with a sticker promoting its unique features in case it ends up as a floor model, but cellphones come with stickers that simply protect the screen. Vendor-created in-store signage is also usually absent. Keep messaging simple and benefit-oriented: “Smartphone” is basically meaningless; “Sync Contacts and Calendar with MS Outlook” means something.

**Recommended Carrier Actions**

- National carriers should look to MVNOs for consumer data pricing models, such as Virgin Mobile’s daily pay-as-you-go option. Carriers would be able to sell data-oriented devices and build up data usage over time, converting heavy users to unlimited plans in the same way they have successfully sold text messaging packages.
- Pay-as-you-go data plans must be measured in ways consumers can understand. “Unlimited for the day,” is ideal, but even “about three song downloads” is better than “5 MB.” When seasoned mobile device analysts cannot predict how much data will be used in a typical mobile email session (this one certainly can’t), consumers shouldn’t be faced with pricing for bits and bytes.
- Carriers can help the device sales process by grouping products together in functional areas. This is retail 101 – have you ever been in a sporting goods store where baseball, gymnastics and football gear was mixed together? – but is often lacking in the mobile world.
- Carrier retail stores choke on low volume, highly complex products, but it is worth stocking them because higher dollar sales almost always correlate to higher value customers. One way carriers can manage this conflict is to treat online channels separately from brick and mortar stores. Online stores can offer a greater variety of high end devices along with the information consumers need to educate themselves on a higher dollar purchase. This also helps lower inventory management costs by centralizing distribution of these slower volume devices.
- Carriers must display live devices in retail stores – there is no way for a consumer to explore the features of a block of inert colored plastic. If it is two faced device, dummy models on rotating stands or an equivalent demonstration video loop running on a flat panel monitor should also be placed at eye level to ensure consumers realize at a glance that they can get a phone/MP3 player, phone/camera, phone/TV, phone/sandwich, or whatever it is.