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# Cyber boom: Why tablet domination has only just begun

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## Cyber boom: Why tablet domination has only just begun

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## Tablet computers have disrupted markets and outperformed analyst predictions from the start – McKinsey research points to more surprises to come.

Bigger and brainier than a smartphone but sleeker and smaller than a netbook, the tablet computer has gained unexpected momentum since Apple created the market segment in 2010 with the iPad. Sales figures have consistently defied analyst expectations as hardware makers worldwide have launched arrays of competing offers. While device makers and application developers have been quick to benefit from the trend, tablets also offer substantial opportunities to other players further down the value chain, including mobile operators with dedicated data plans.

Significant amounts of research into how, why, where, and when people use tablets has already been undertaken, but findings are sometimes contradictory. Key insights often become buried beneath the sheer amount of data available. In an effort to cut through the clutter, McKinsey has examined the research, distilled the data, and identified a number of key market insights regarding tablets and their users. The following six take-aways can help telecoms, media, and high-tech players and other value chain participants capture more of this growing opportunity.

### Tablet market growth will continue to exceed analyst expectations

Attempts to predict the market uptake of disruptive innovations like tablet computers are inherently difficult; results are usually fraught with errors. That's why initial analyst forecasts for iPad sales were so overwhelmingly wrong, underestimating sales in the first six months after launch by up to a factor of seven. While predictions are rarely right on target – the number of new market entries, consumer interest levels, and the trend toward lower prices tend to throw

a monkey wrench into forecast models – recent McKinsey analysis indicates tablet sales levels that will again exceed analyst expectations. Even using conservative assumptions, tablets are likely to surpass 350 million units by 2016.

Regionally, Europe along with Russia and Turkey are expected to constitute the largest market – accounting for one third of tablet demand – followed by North America and Asia. The Middle East and Latin America will likely show the largest growth, representing around 50 million units by 2016.

Five main factors will drive tablet growth. First, affordability – with the introduction of low-end devices and the natural price decline curve – will shift demand, supporting uptake among new, less affluent customer segments. This will fuel around 60 percent of the total cumulative sales through 2016. Second, consumers will replace outdated tablets over time, contributing about 28 percent of expected growth. Third, 6 percent of the overall increase will stem from substituting conventional laptops and notebooks with tablets. The two remaining drivers are business adoption (4 percent) and education initiatives (3 percent).

Introducing new, smarter tablets with more extensive input capabilities or more countries launching government-driven initiatives could easily increase the base case scenario.

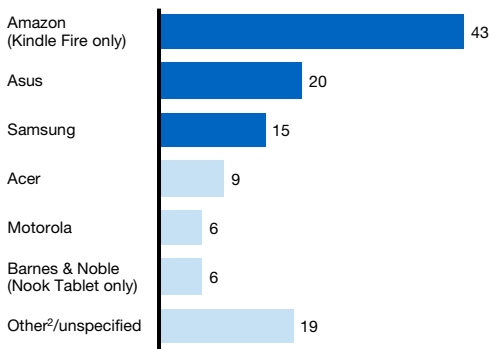
### Social media buzz sheds new light on product usages

The sales breakdown is certainly one indicator of current competition levels among tablet operating systems. By the end of 2011, Android powered from 35 to 40 percent of all tablets sold globally –

## Among Android-operated devices, the Kindle Fire generates the most positive user engagement buzz

### Level of social media buzz for Android tablets

Frequency mentioned, percent of posts<sup>1</sup> (multiple mentions possible)



<sup>1</sup> Based on a random selection of 200 relevant posts between August 2011 and January 2012

<sup>2</sup> E.g., Archos, Toshiba, HP, Sony, Dell

SOURCE: NM Incite; McKinsey

### Breakdown of social media buzz by type

Percent of posts<sup>1</sup>

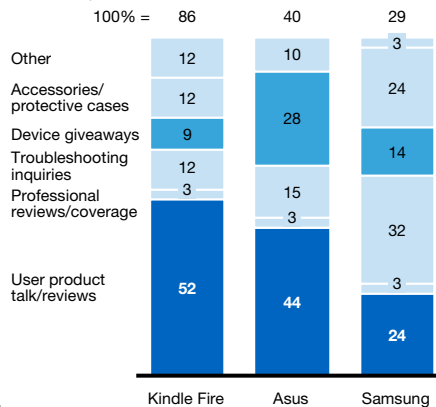


Exhibit 1

a major change from the prior year when Apple's OS was the only market player. The more complex indicator of social media buzz, however, points to how the market may evolve.

While Apple still accounts for about 90 percent of consumer commentary from forums, blogs, Facebook, Twitter, etc., one recent arrival to the Android scene is getting more buzz than the others. Amazon's Kindle Fire is generating nearly 43 percent of total Android buzz, making it the iPad's main competition in online consumer conversation (Exhibit 1). Delving deeper into buzz

*Amazon's Kindle Fire is getting lots of "king of Androids" buzz, indicating that it might become stiff competition for Apple's iPad*

analysis also indicates that the Kindle Fire generates the most actionable product talk with users recommending the device and telling their friends about it. For some other tablets, in comparison, a significant share of the

buzz is related to corporate contests and device giveaways – which is an indication of less genuine user engagement.

Another sign that the Kindle Fire is emerging as a key contender is that its buzz is relatively positive, despite some critical early reviews in the professional technology blogs. One user noted that although the Kindle Fire did not have all the bells and whistles of an iPad, it was an excellent book and document reader and Android app device – all delivered in brilliant HD color. Another user who bought the Kindle Fire as a gift for her daughter favorably mentioned the picture quality of the screen and the device's ease of use via the touch interface as compared to a laptop.

Where Apple scores higher than competitors is the brand loyalty of smartphone users. For instance, 77 percent of iPhone users said they would prefer an iPad to other tablets, perhaps revealing how invested these users are in their ecosystems. And while 59 percent of Android smartphone users said they preferred something other than an iPad, their loyalty to other specific brands was quite low.

## From the sidelines to the playing field: Tablets put seniors squarely in the high-tech game

Senior citizens have often been left out of the consumer technology equation. At best, simplified versions of popular devices and services – such as e-mail that does not require a PC and large-button, single-function mobile phones – have been launched as afterthoughts for the oldest consumers who tend to be farther behind the adoption curve. Tablets – whether by design or simply by nature – have changed the technology landscape for seniors.

**Usability.** For seniors, tablets address some of the biggest traditional barriers to technology. Arthritis and other impairments often limit a senior's fine motor skills – a disability is incompatible with mouse and keyboard requirements. Tablets deliver touch screen technology, facilitating usage and minimizing user frustration.

Tablets also offer an improvement over one of the most traditional form factors – books. For those with poorer vision, a once-enjoyed activity like reading could be a thing of the past. Not only can those with limited mobility avoid a difficult trip to a bookstore or library by downloading a book, they can also easily adjust the text size.

**Healthcare.** Tablets are also enabling greater independence for the elderly through remote evaluation and monitoring. From the diagnostic side, tablet-based mobile assessment tools provide a rapid assessment of a patient's ability to complete mobility-related tasks. Tablets also enable ongoing care. One example is Angela, a specialized tablet designed to give patients medication and appointment reminders as well as video access to family and caregivers.

### Tablets are conquering new user demographics

Even if younger, tech-savvy demographic segments initially powered the tablet's market rise, ownership is expanding to other age (and income) segments. Where early tablet adopters were mostly younger, affluent men, more women, older users, and middle-income households are becoming tablet owners today. This trend extends to both young children and senior citizens.

A Nielsen survey of 6- to 12-year-olds in the United States from October 2011 indicates the tablet's appeal among the youngest of users. Asked what electronic device they would be interested in purchasing in the next six months, 44 percent said an iPad – by far the highest re-

sponse rate for any device. A further 25 percent were interested in another type of tablet.

This preference should be no surprise, given the fact that one in five of the top 200 iPad apps targets kids. Beyond this, tablets also appeal to senior citizens, helping them boost their memory capacity. For older consumers, tablets make reading easier and can also provide specialized healthcare services (see text box).

The business world is likewise rapidly adopting tablets – especially for knowledge workers and executives. Both groups use them for work and personal activities. Among knowledge workers in Europe and North America, 5 percent (11 million) use their tablets at the office, and 20 percent of them purchased their tablets themselves.

## Apps are winning versus browser-based experiences

Tablet users often have a choice between using dedicated native apps (programmed for a specific OS) and accessing a Web site or HTML5 Web application. The latest tablet user research shows that consumers make distinctions regarding how they access content during different activities. For example, 48 percent of iPad users say they prefer apps when playing video games while 26 percent like to use the browser – 20 percent use both (7 percent say they don't know). When reading a book, newspaper, or magazine on a tablet, 32 percent use apps, 35 percent prefer the browser, 25 percent use both, and the rest don't know.

Recent research indicates that apps provide a much better customer experience – even for tasks where consumers are split fairly evenly between using an app or a browser. Users found reading the news, for example, more than twice as enjoyable on an app, thought the news was twice as worthwhile, and considered it much easier to learn new things. This has clear

*Apps provide a superior customer experience with tablet revenue potential three times higher than that of the smartphone*

implications for content and application providers, but is essentially positive. While smartphones have educated consumers about using (and paying for) apps, tablet users download even more apps and willingly pay significantly more for them. For instance, the annual app revenue potential of each iPad is USD 60, compared with an iPhone's USD 20. Based on current download metrics, app revenue for Android seems lower. These users download only half as many apps as those using Apple's iOS, and iOS users pay for apps (as opposed to seeking out free ones) three to four times more often.

## Good news for media companies: Tablets stimulate usage

Before the advent of tablets, publishers and media companies had long struggled to monetize their online offerings beyond advertising. When the tablet was first introduced, it sparked major excitement, and tablets started to be seen as a potential savior of news and magazine publishers. The hopes were that this new device category could persuade consumers to pay for content they had formerly obtained for free on the open Web.

Tablets might not have been a cure-all for media companies so far, but evidence supports reason for hope and points to tablets starting to make good on part of their initial promise: tablets are actually boosting news readership. The latest research indicates that 30 percent of tablet users actually spend more time reading news than they did before purchasing their device, while only 4 percent spend less. This is because most consumers find it more enjoyable to read newspapers and magazines on their tablets. One survey reveals that consumers who formerly spent about 45 minutes (per issue) reading a magazine "in print," boosted their time to 160 minutes on the tablet.

Beyond this, tablets are actually pulling in new users who had previously expressed no interest in the print products. One international news magazine developed an app for tablets and found that 25 percent of its app users were willing to pay for content, compared with only 5 percent of browser users. Amazon similarly found that customers who purchased the Kindle e-book reader tended to increase their book purchases more than threefold. As a result, sales of e-books in the US, the UK, and Germany are expected to increase 30, 59, and 77 percent respectively through 2015.

## Initially slow to act, mobile players have large upside potential

While media companies have been quick to benefit from the tablet opportunity, the experience among mobile operators has been more mixed so far.

## Operators are still experimenting – 3G tablet penetration and pricing vary considerably as a result

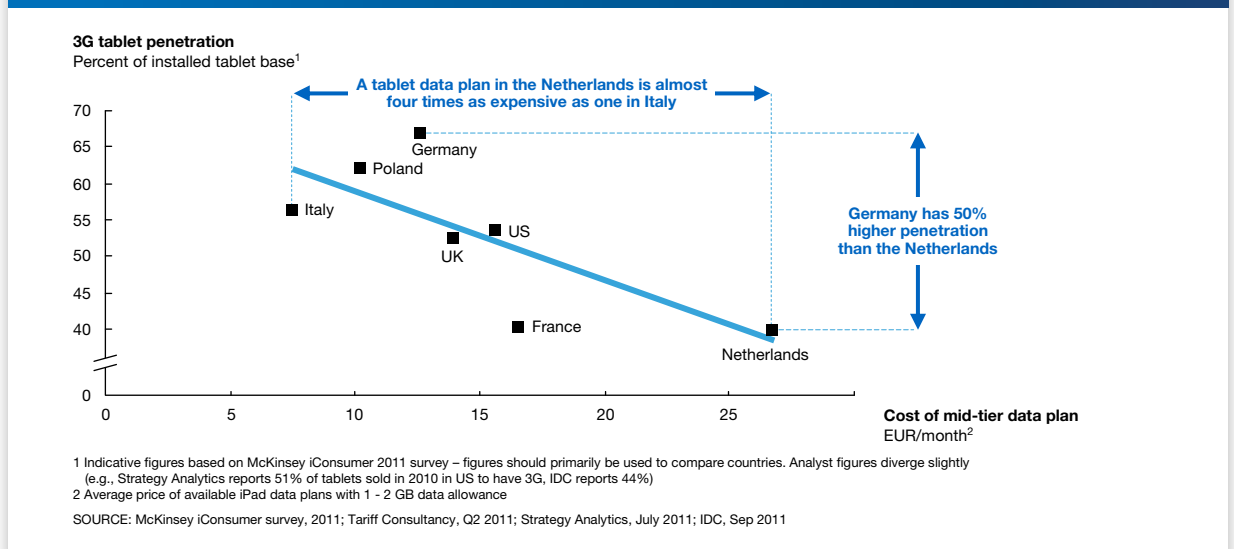


Exhibit 2

The expectation that tablets would transform the mobile operator's retail business into a major sales channel that could compete with Apple Store outlets or big box consumer electronics retailers such as Best Buy has largely failed to materialize.

In fact, McKinsey experts see two patterns across major developed markets. First, many mobile players lack clear strategies to deal with the tablet phenomenon. No real best-practice approaches to tablet data plans are apparent. Across and even within key countries, pricing and plans offered actually vary greatly from player to player. Second, many mobile operators play it safe when it comes to tablets, making few bold or innovative moves. From a pricing perspective, they usually treat tablets as separate devices similar to smartphones. One apparent fear: introducing novel approaches like multi-SIM could lead to plan cannibalization. Comparing prices for tablet data plans across markets helps underline the above points. In tablet data pricing, a lot of experimentation is still taking place. Price differences across major markets, for example, show significantly more variability than in traditional voice rate structures – tablet plans in

the most expensive countries cost 3.6 times more than in the least expensive ones – the difference is only 2.2 times for voice. As a consequence, the market uptake of 3G-enabled tablets correlates strongly with data pricing (Exhibit 2). High prices in the Netherlands appear to have constricted 3G tablet sales, for example, while Germany's lower prices have led to much higher penetration.

The relative lack of conformity in tablet data pricing across markets points to a clear upside opportunity based on the potential for sharing best-practice pricing strategies across markets. As an example, one innovative approach centers on multi-SIM offers that allow users to extend their current smartphone/voice contracts to include data access for their tablets. As a result, subscribers don't have to buy a second contract just for the tablet. Tele2 in Sweden, for instance, allows current mobile broadband customers to receive one extra SIM with a separate one gigabyte data allowance. Likewise, T-Mobile in Germany gives users the option to receive up to two extra SIMs for a one-time fee and no additional monthly charges. The data use is drawn from their current plans. Other operators

bundle tablets with 3G access and attractive content. Vodafone Italy, for example, links tablet plans with live streaming sports coverage and subscriptions to some of the leading national newspapers.



The tablet phenomenon is still on the rise, creating new opportunities for players across the telecoms, media, and high-tech value chain. The six trends described here should provide leaders interested in capturing more of this opportunity with a solid foundation regarding what to expect next from this vital new source of value.



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