

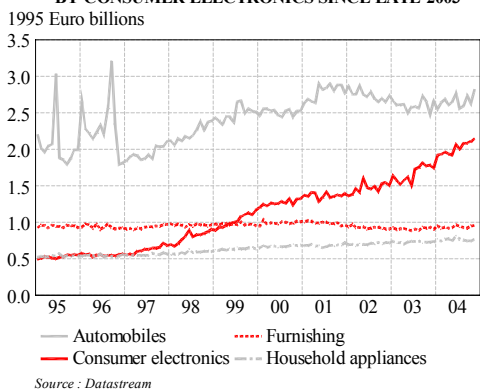
THE ELECTRONICS BOOM IS DRIVING CONSUMER SPENDING FORWARD

Consumer spending grew at an exceptional pace in the first half of the year, led by the remarkable strength of consumer electronics sales. The spread of digital technology has led to falling prices, upgrades and a broadening range of products, stimulating significant demand for "brown goods".

• The consumer electronics boom

The volume of consumer spending rose by a very healthy 1.8% in the first half of the year, thanks to a strong increase in expenditure on manufactured products (+3% over the period). This was led solely by durable goods expenditure, and indeed consumer electronics spending, which has been rising rapidly since spring 2003 (17% p.a. in the third quarter after 26% in the second). Sales of consumer electronics were still very brisk in October, growing 1%, and in November (+2,1 %, +20,9 % p.a). They currently represent 11.6% of manufactured goods purchases by volume (27% of total consumption) versus 9.2% in the first quarter of 2003 and 3.4% 10 years ago.

DURABLE GOODS CONSUMPTION HAS BEEN SPURED ON BY CONSUMER ELECTRONICS SINCE LATE-2003



The high-speed growth of sales in terms of volume in the consumer electronics sector is attributable to a few key products from the digital universe such as cameras (sales rose 68% in 2004 from 127% in 2003 and 30% of households will have one at the end of the year, according to the GFK Institute), camcorders, MP3 players and camera phones as well as flat screens and DVD players (60% of French households are likely to own a DVD player at end-2004 versus 42.6% at end-2003, according to GFK). These developments more than make up for the erosion of sales of "traditional" products such as film cameras, cathode televisions and video recorders. Products arising from digital technology currently represent two-thirds of sales to the detriment of analogue products.

• A technological departure and falling prices

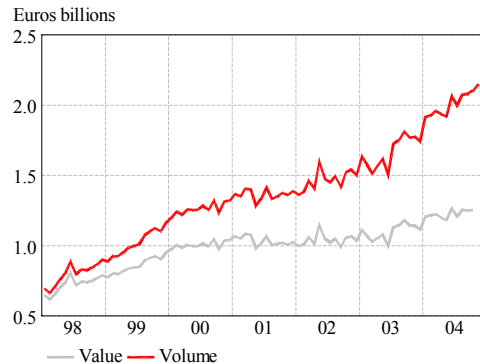
Apart from a traditional effect associated with the year's major sporting events, part of the strength of consumer spending on "brown goods" is connected to the housing boom. More fundamentally, however, it is the result of a major shift in technology, namely the transition from analogue to digital broadcasting – what might be dubbed the "technological big bang". Indeed, unlike previous breakthroughs, this shift encompasses all the domains of sound, image and content. It also provides a link between IT and electronics. As well as bringing new features to traditional products – the typical example being flat screens for television – digital technology is creating new products (such as the DVD recorder and the camera phone). Product expansion – which is bringing multiple technologies into the home – has been accompanied by an improvement in quality and product upgrading, which is further stimulating demand.

Added to this is a "price effect", hefty price falls are being observed in the sector. The price of "brown goods" fell some 4% in the first half of the year, after an average of 7% in 2003. Most importantly,

the fall in the price of key products has speeded up since early 2002. A digital camera with an optical quality three times greater than its 2003 predecessor sold for 20% less, while the price of flat screens has fallen an average of 30% p.a. since 2001.

Apart from the fall in the dollar (the majority of consumer electronics are imported), the acceleration of price falls is due to increasing competition in the sector. The convergence of sound, image and content has increased the number of players, while the disappearance of the boundaries between IT and consumer electronics has brought PC manufacturers into key products (e.g. Apple's iPod), generating furious competition. This encourages innovation of course, but also tends to bring down prices, especially since overcapacity has appeared a few specific sub-segments. At the same time, investment and R&D costs are constantly rising. The intensification of competition and the permanent need to innovate renders products commonplace more and more quickly and shortens their life span, which further stimulates demand and intensifies the fall in prices. As a consequence of lower prices, consumer electronics consumption is rising significantly less quickly in value terms than in volume: the value of spending rose a "mere" 7% in the first half of the year after an average of 5.6% in 2003. By way of example, "home cinema" sales grew 80.5% p.a. in volume between H1 2003 and H1 2004, whereas turnover grew "only" 13% over the same period.

CONSUMER ELECTRONICS CONSUMPTION



Manufactured goods consumption should continue to benefit from strong consumer electronics spending in the short term, especially since the end of the year is traditionally a boom period for these products. Furthermore, in late 2004/early 2005 "brown goods" consumption will benefit from the extra cash pumped into the economy by the "Sarkozy measures" (EUR 3.9 billion had been injected into the economy at end-October – EUR 3.9 billion by way of a one-off release of employee savings and EUR 3 billion in the form of gift tax exemptions).

Beyond that, the factors behind soaring consumer electronics spending should remain in play over the next few years. The fall in prices should accelerate. Digital technology has a rich potential to create new high-value-added products. Innovations such as interactive televisions, television as a multimedia centre supporting other digital equipment, or new types of telephony (UMTS) and product upgrades will continue to fuel demand. The household ownership rate of consumer electronics is still a long way from having reached its peak.

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