iPad Dominates Due To Apple's Supply Deals

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NEW YORK (AP) — Apple certainly has lots of buzz and corporate cache behind its products, but there's a hidden — almost mundane — reason its newest iPad is likely to dominate the competition: the advantageous deals the company cuts with components manufacturers.

Apple's size, and the fact that the iPad shares components with the highly popular iPhone, means that the company can buy crucial parts such as processing chips and display screens at lower prices. Any company that wants to make a tablet computer that matches the iPad's $499 starting price has to endure higher costs.

As a result, Apple's tablet-making competitors have flailed — and failed. And with the new iPad, Apple is expected to extend its 62 percent market share in the tablet computer category it created. IMS Research expects Apple to capture 70 percent of the market this year.

A year ago, scores of companies all thought they had a shot at emulating Apple's success. More than 100 tablet models were on display at the annual consumer electronics trade show in Las Vegas in January 2011. Many of them ran on the Android operating system, developed by Silicon Valley powerhouse Google.

As the year progressed, those dreams crumbled. The iPad 2, launched in March, proved nearly unassailable.

A big part of the reason was that Apple has priced the iPad aggressively. At just under $500 for the basic model, Apple's profit margin on the device is lower than on the iPhone, a smaller device for which it charges phone companies a wholesale rate of $600 or more.

On Wednesday, Apple stuck to that price point when it unveiled the new iPad model. It has a screen that displays sharper images and deeper, more vibrant colors to set it apart from the competition. The new tablet goes on sale March 16 in the U.S. and several other countries.

Apple has other advantages, too. The company sells about a third of all iPads in its own stores or from its website. By cutting out the middleman, Apple is able to keep more of the slim profit margin for itself.

Because it produces tens of millions of iPads and uses some of the same components as the highly popular iPhone, Apple can buy crucial components such as chips and displays at lower prices.

According to research firm IHS iSuppli, Apple is the world's largest buyer of the microprocessor chips that serve as the "brains" of various devices. In January 2011,

Apple said it had spent $3.9 billion on long-term contracts to secure supplies for two years of a "very strategic" component it wouldn't name. Few other companies are able to commit that much money.

Many suppliers are happy to sell to Apple, given the company's success in mobile products. ARM Holdings PLC, a British chip-maker that licenses the technology used in iPhone and iPad chips, for instance, saw its stock rise nearly 4 percent Thursday, a day after Apple unveiled iPads with faster processors. Other Apple suppliers, including Cirrus Logic Inc., Jabil Circuit Inc. and Skyworks Solutions, have all experienced healthy stock gains in recent months.

The iPad's pricing created an odd situation. Usually, the first gadget of its kind to hit the market is expensive. Competition then gradually brings prices down.

With the iPad, the reverse happened: Competing products from makers such as Samsung Electronics Co. and Motorola Mobility Holdings Inc. were more expensive, at least for the first year.

The most extreme example of a tablet failure comes from Research In Motion Ltd., the maker of the BlackBerry.

In late 2010, RIM's co-CEO at the time, Jim Balsillie, said interest in the planned PlayBook tablet was "really overwhelming," particularly from corporate customers, a key market for BlackBerry phones. In March, just before it launched, Balsillie said the PlayBook "may well be the most significant development for RIM since the launch of the first BlackBerry device back in 1999."

But the PlayBook was widely panned because of its software, which RIM had put together. It was also expensive. It cost the same as an entry-level iPad 2 despite being half as big.

When sales failed to materialize, RIM had to slash the price of the PlayBook from $500 to $200. It ended up taking a pre-tax charge of $485 million for the declining value of its inventory.

Other manufacturers slashed prices too, culminating in a "fire sale" during the recent holiday season, said Rhoda Alexander, an analyst who covers tablets for IHS iSuppli.

"Those price discounts have come out of the profit margin, to a large degree," she said.

Hewlett-Packard Co., meanwhile, left the market completely. In August, it decided to discontinue the fledging TouchPad tablet along with its line of smartphones, despite great reviews for the in-house software running them.

Samsung has been one of the survivors, selling 6.1 million tablets last year, according to IHS iSuppli. That makes it the second largest tablet maker after Apple, with a market share of 9 percent compared with Apple's 62 percent. Samsung is

also one of the world's leading makers of smartphones, chips and display screens. The company is, therefore, big enough to capture some of the advantages that Apple has as a buyer of components in bulk.

Samsung has put out a bevy of tablets in different screen sizes, hoping to capture buyers, who for one reason or another, want something other than the 9.7-inch screen of the iPad.

In November, another successful challenger appeared: Amazon.com Inc. The Internet retailer figured out that people would buy a device other than an iPad if the price was considerably lower. It put together a Spartan tablet with a minimum of frills and started selling it at $199. Amazon doesn't make a profit on its Kindle Fire, according to IHS iSuppli, but it hopes the device will help boost sales of movies, music and electronic books at its online store.

Analysts estimate that Amazon sold 3.9 million to 6 million Kindle Fires in the first six weeks, making it the third-largest seller of tablets last year. Looking solely at the last three months of 2011, Amazon beat Samsung as the second-largest seller of tablets.

Barnes & Noble Inc. adopted a similar strategy and was also successful, at least considering that it's a bookseller venturing into consumer electronics. It updated its Nook Color e-reader to make it more of a general-purpose device and called it the Nook Tablet. ISuppli estimates that it sold 3.3 million Nook tablets last year.

During this year's holiday shopping season, a new raft of challengers will appear: tablets powered by Microsoft Corp.'s Windows 8. Microsoft has provided software for PC-style tablets before, but they've never been more than a niche product. Now, the company is creating a version of Windows that runs on phone-style processors such as those used in the iPad. Reviews of the pre-production software have been positive. It will allow users to do some things they can't on an iPad, such as running two applications side by side on the same screen.

Still, analysts expect Apple to regain market share, after losing some because of the unsustainable discounting by competitors late last year. On Wednesday, Apple said it would keep the iPad 2 in production and cut the starting price to $399 — the same price as Samsung's Galaxy Note Tab 10.1.

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