

Bloomberg

Nokia Betting on \$20 Handset as It Loses Ground on iPhone

By Adam Ewing - Apr 29, 2013

As [Nokia Oyj \(NOK1V\)](#) struggles to catch [Apple Inc. \(AAPL\)](#) and Samsung Electronics Co. in the market for smartphones costing \$500 or more, it's counting on a bare-bones handset that sells for just \$20 to give it an edge.

Priced 97 percent below the latest iPhone, the [Nokia 105](#) features preloaded games, a color screen, a radio, a speaking clock and a flashlight. The phone, Nokia's cheapest ever, has been available for a few weeks in India and [Indonesia](#) and will soon start selling in [Europe](#).

Even with its bargain-basement price, the 105 is critical to Nokia's entire handset business. Nokia reported April 18 that it sold about 11 million fewer mobile phones in the first quarter than analysts had projected, with sales of basic phones plunging 21 percent to 55.8 million units. A failure to revive the low-end business would leave Nokia without an important source of cash as it seeks to develop devices to challenge the iPhone and Samsung handsets running [Google Inc. \(GOOG\)](#)'s Android.

Falling sales of simpler phones are "definitely worrisome," said Mika Heikkinen, a fund manager at FIM Asset Management in Helsinki, who helps oversee some \$2.5 billion, including Nokia shares. "They have to get this under control."

Nokia Chief Executive Officer Stephen Elop, speaking to investors after the report, pointed to the 105 as a signal that the low-end business can recover after a "difficult" quarter.

Recovery Signal

While demand for the iPhone and Android devices have made smartphones the fastest-growing part of the market, basic handsets still make up more than half of units sold. That means hundreds of millions of phones each quarter -- a market Nokia dominated until Asian manufacturers such as [ZTE Corp. \(000063\)](#), Huawei Technologies Co. and Samsung started challenging it more aggressively. Nokia says the 105 will be profitable, but declined to provide any details. Liberum estimates Nokia will enjoy a margin of about 20 percent on the device.

Of the 336 million handsets Nokia sold last year, only about 10 percent were smartphones. Basic models accounted for 31 percent of Nokia's revenue, versus 18 percent for smartphones. Network equipment made up most of the balance.

Nokia had more than half of the mobile handset market before Apple introduced the iPhone in 2007. Nokia shares have fallen more than 80 percent since then, while Samsung has risen 154 percent and Apple has quadrupled. After five consecutive annual losses, Nokia is down 14 percent this year through April 26.

The stock rose 1 percent to close at 2.53 euros in Helsinki, valuing the company at 9.5 billion euros.

Developing Markets

Nokia, based in the Helsinki suburb of Espoo, is counting on cheaper phones like the 105 to build trust in the company's brand in growth markets such as [India](#) and [China](#). Customers who buy a 105 will stick with Nokia when moving to more expensive devices in the years ahead, the company reasons.

"The low-end, high-volume part of the mobile-phone market is a huge opportunity for [Nokia \(NOK1V\)](#) in developing countries," said Francisco Jeronimo, an analyst at IDC in London. "These users will be likely to upgrade to more expensive phones over time, so it's a good strategy to keep a high market share in this segment."

The 105 is "very competitive" and should help Nokia with its low-end recovery effort, said Neil Mawston, an analyst at researcher Strategy Analytics in [London](#). A predecessor to the 105, called the 1280, sold more than 100 million units over three years.

Simpler phones have "been the bedrock of Nokia's business for the past decade," Mawston said.

35 Days

Nokia's expertise in handset production makes it possible to turn a profit on a \$20 phone, Jeronimo said. For years the world's largest mobile-phone maker and now No. 2, Nokia makes more than 600,000 phones a day in seven [factories](#) around the world, using parts from suppliers it knows well. Chinese [rivals](#) may be able to make a device as cheap as the 105, but they lack the features and services from Nokia, Jeronimo said.

The candybar-shaped 105 is 25 percent cheaper than the Nokia 1280, yet its battery lasts 56 percent longer -- 35 days. The phone is resistant to water and dust and comes with text- message-based tools that teach English and provide basic health- care advice.

Despite such features, the company sought to simplify the phone's software, which in turn allowed it to use cheaper parts, said Dirk Didascalou, head of R&D for Nokia's [mobile-phone business](#).

Lumia Attention

"To be successful at the low end, one needs to explicitly do innovative work with a focus on delivering value," he said by phone from Nokia's research facility in Beijing. "If you don't, you get

in a cost spiral where you're always a bit too expensive compared to somebody else.”

Even as the slump in simple handsets has stolen investor attention, Nokia's main goal is to make a full recovery in smartphones, where profit margins are widest. [Apple \(AAPL\)](#)'s 32-gigabyte iPhone 5 sells for \$750, while Samsung's Galaxy S4 goes for \$640 and Nokia's flagship Lumia 920 is \$450.

Nokia sold 5.6 million Lumia phones, which run on [Microsoft Corp. \(MSFT\)](#)'s Windows, in the first quarter, up from 4.4 million in the previous three months. But the iPhone and Android control more than 90 percent of the smartphone market, while Nokia has just 3 percent, according to Strategy Analytics. So it's far from clear Nokia can break that dominance even if its low-end devices recover, said [Mikko Ervasti](#), an analyst at Evli Bank in Helsinki.

“Nokia may still be the second-biggest phone maker in the world,” Ervasti said. “But if it's going to have a chance at long-term success it needs to make sure it also has the right smartphones.”

To contact the reporter on this story: Adam Ewing in Stockholm at aewing5@bloomberg.net

To contact the editor responsible for this story: Kenneth Wong at kwong11@bloomberg.net

©2013 BLOOMBERG L.P. ALL RIGHTS RESERVED.