

**WARRANTY WEEK®**

The Newsletter for Warranty Management Professionals

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October 9, 2014

## Mid-Year Service Contract Report:

**Consumers will pay nearly \$40 billion this year for product protection plans, despite the best efforts of the watchdogs who tell them not to. It's mostly for smartphones and passenger cars, though, because everything else is perceived to be disposable and not worth fixing.**

The service contract industry is huge and growing in the U.S., despite the best efforts of critics who, right around this time of year, repeat their outdated "[don't buy extended warranties](#)" message to consumers.

Even our incomplete accounting of the various consumer-facing segments of the service contract industry suggests a market worth almost \$40 billion this year, assuming that no polar vortex arrives before Santa. We've counted up the total premiums paid by consumers in the vehicle service contract segment, the home warranty segment, the retail brown and white goods segments, and the mobile phone insurance segment, and the total market estimate we come up with for this year is \$39.5 billion to be paid by U.S. consumers for what we'll call product protection plans.

And that's not counting the jewelry, furniture, and sports equipment sectors, which we'll get around to sizing in 2015, we hope. And that's also not counting the purely business-to-business service contract sector, which covers everything from truck fleets to jet engines, not to mention printers, copiers and coffee machines. And that's only the U.S. Then there's the European market, and some Asian, African and South American markets that are just getting it together. They need to be counted too.

### Bad Marks on Report Card?

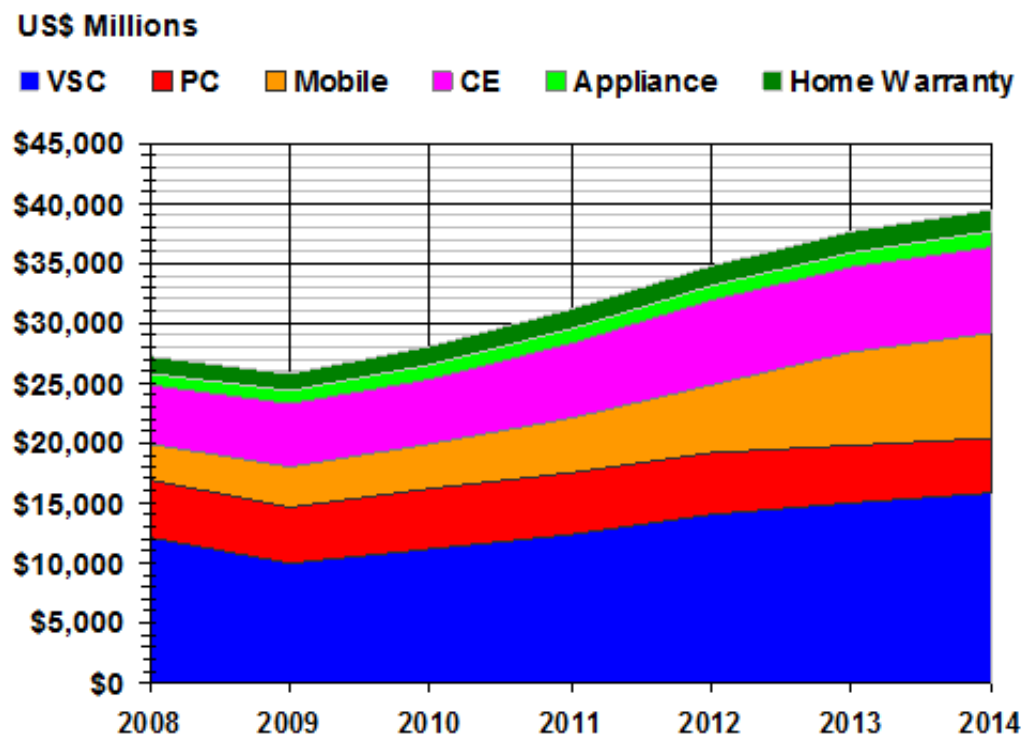
Despite the best efforts of [Consumer Reports](#) and its allies, more protection plans are being sold now than ever before. If we were to give out ratings like they do, we'd have to give them a little black circle on their report card. For while they might take credit for some of the extended warranty industry downturn from 2006 to 2009, it just as easily could have been caused by the then-brewing recession, the commoditization of major home electronics and home computer product lines, or the shift to online

shopping, where it's quite easy to say no to a click box offering you a protection plan.

Since 2009, we don't think there's been a down year for the market. Then again, unlike with our product warranty expense data, with service contracts we're making estimates based on confidential assistance from industry experts and occasional confirmations from the financial statements of some of the publicly-held players.

Readers are urged to take a look at the data in Figure 1 and compare it to your own internal estimates. Behind this data stands an array of charts and tables dissecting these various markets by underwriter, administrator, and seller. We won't include all that information here, but rest assured that the \$39.5 billion total is built from the bottom up.

**Figure 1**  
**U.S. Consumer Service Contract Market**  
**Premiums Paid by U.S. Consumers, 2008 to 2014**  
**(estimates in U.S. dollars)**



Source: Warranty Week estimates

Notice that the trough came in 2009, when these six segments declined to about \$25.8 billion in premiums paid, thanks to a massive decline in VSC sales that year. But even that recession-pounded segment was back in growth mode by 2010, as it has been ever since. Maybe it would have grown even more had *Consumer Reports* not launched its extended warranty buying guide. Or maybe it really didn't have much effect.

## Slice by Slice

We should explain what's included in each of these segments. From the top, the home warranty segment, in dark green, is the one where American Home Shield dominates -- typically, the seller of an existing home buys a home warranty to protect the heating/cooling, kitchen and laundry appliances, and passes it on to the home buyer as a deal sweetener.

The appliance segment, in bright green, is the slice of the pie that includes service contracts sold by retailers such as Sears, Lowe's, or Home Depot, in conjunction with a new product sale. We detailed the home warranty market shares in the [December 22, 2009 newsletter](#), and we covered the retail appliance protection market segment about a year ago in the [October 10, 2013 newsletter](#).

The CE segment is a service contract sold by a retailer such as Best Buy, Target, or Radio Shack, in conjunction with the sale of an electronics product. Their mobile phone protection plans are included here, as are Apple's. Also included here are protection plans covering laptops and other computers.

The mobile segment, in orange, includes protection plans sold by the cellular carriers themselves, billed monthly and bundled into their bills. We covered this market segment in depth in the [November 14, 2013 newsletter](#), where we pegged the 2013 market at \$7.8 billion.

Until recently, the phone companies had a tremendous advantage in terms of being able to include loss and theft coverage in addition to covering defect, malfunction and damage, while the retail CE plans covered only defect, malfunction and sometimes damage. But some of the retail CE plan providers have now found a way to bundle these insurance-like coverages into their plans, and more importantly, to sell them without having to send their cashiers to insurance school.

The PC segment, in red, includes the service contract programs of computer manufacturers such as Dell, HP, and Lenovo. In other words, it's a category that's specific to the type of seller, rather than to the type of product being sold. It's the same way we slice up the mobile segment: by channel rather than by object. And that means there is also some laptop coverage in the CE segment, when the plan is for a PC sold by Best Buy, Staples, or another of their competitors.

And finally, there's the vehicle service contract segment, in blue, which is and always has been the largest segment of the service contract industry ever since Pat Ryan thought of it 50 years ago. We covered this segment of the market in a series of newsletters that concluded with the [September 9, 2010 edition](#).

The VSC segment is primarily attached to new cars, and primarily to franchised dealers, though there is some coverage of used cars and sales by both independent dealers and direct marketers. But as we shall see, this entire category is being challenged for supremacy by the smartphone segment, whose growth shows no sign of slowing down.

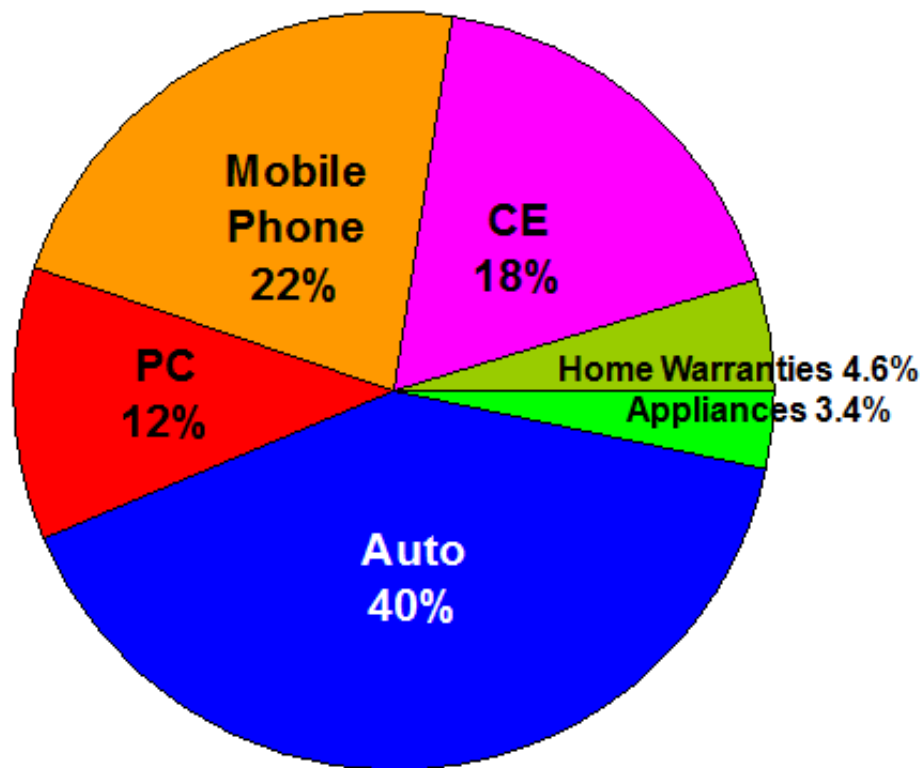
## Service Contract Market Shares

Here's what we expect in terms of market shares for each of these segments this year. Again, some of the plans sold in the CE segment cover smartphones, and some cover laptops. But there's no double-counting.

Likewise, both the home warranty and the appliance segments protect major appliances, using different approaches. One covers all the appliances no matter how old they are, and the other covers them one by one as they're purchased. And the VSC segment covers primarily passenger cars and light trucks driven

by consumers, but also some of their big toys: motorcycles, ATVs, recreational vehicles, boats and jet skis.

**Figure 2**  
**U.S. Consumer Service Contract Market**  
**Premiums Paid by U.S. Consumers, 2014**  
**(estimates as a percent of \$39.5 billion)**



Source: Warranty Week estimates

Figure 2 is a bit misleading in the sense that the mobile phone's share of the pie is actually much larger than 22%. Almost a third of the CE segment is AppleCare for iPhones. Another third represents smartphone protection plans sold by other retailers. So that's almost two-thirds of the 18% assigned to CE protection plans. The 22% in Figure 2 includes just the segment sold by the phone companies. Add those all together, and the total market share of the mobile phone protection plans grows to fully 34% of the \$39.5 billion total for all types of consumer service contracts.

Here's a little more detail. Let's say there are three ways to buy a mobile phone protection plan. First, you can buy an iPhone from Apple and protect it with an AppleCare plan. Second, you can buy a smartphone from Best Buy or Radio Shack and protect it with the house plan. Third, you can pay your phone company an extra \$8.00 to \$13.00 per month for a mobile phone insurance plan.

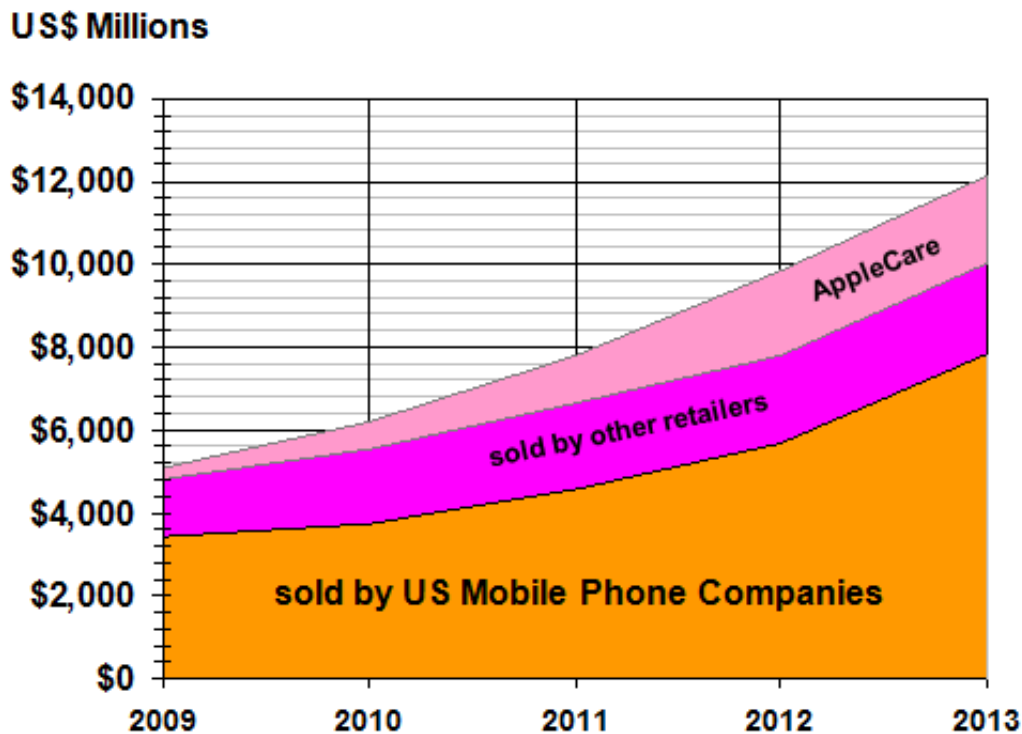
## AppleCare Worldwide

In 2013, we estimate the U.S. portion of the AppleCare program, covering just iPhones and iPads but not iPods or Macs, to have collected about \$2.1 billion in premiums from consumers. That's about 40% of the \$5.25 billion the AppleCare program took in worldwide that year for all products, which by the way, we believe, makes it the world's largest extended warranty program for any consumer product, by any company. Does anyone know of anything larger?

We estimate that other smartphone protection plans sold by other retailers brought in an additional \$2.2 billion last year. We expect that by the time the ball drops on New Year's Eve this year, these retailers will have seen that total grow by about five percent. And we're predicting about nine percent growth for AppleCare U.S., iPhone/iPad-only premiums paid.

The phone company plans, we believe, are growing even faster. Though they're losing the advantage they once had to retailers who can now cover loss and theft in addition to damage, defect and malfunction, and though consumers are beginning to realize that the convenience of monthly billing ends up costing more in the long run than yearly or two-year plans, we think they'll still be able to bring in about \$8.6 billion this year.

**Figure 3**  
**U.S. Mobile Phone Protection Plans**  
**Premiums Paid by U.S. Consumers, 2009 to 2014**  
**(estimates in U.S. dollars)**



Source: Warranty Week estimates

Add to that \$8.6 billion the \$2.3 billion in protection plans sold by Apple, and the \$2.3 billion sold by Best Buy, Radio Shack and other retailers, and you're looking at a \$13.2 U.S. market for mobile phone protection, up over nine percent from 2013. And you're looking at a product type -- the smartphone -- that will soon account for fully 34% of the entire service contract ecosystem.

Like we said, we think *Consumer Reports* is doing a rotten job of talking consumers out of buying extended warranties. Perhaps that has a lot to do with their antiquated mode of attack. First, they seem to believe that all extended warranties are priced the same, with identical coverages, deductibles, and exclusions. If only that were true!

Second, they compare that single price to the cost of a single repair. And because of allegedly high-quality manufacturing, they assign a low probability to the need for such a repair. One can only wonder what they'd discover if they applied such a methodology to fire insurance or term life insurance.

## No More Extended Warranties?

However, that's not how extended warranties are sold. In fact, does anyone but *Consumer Reports* still call them extended warranties? We see producers offering smartphone insurance, mobile protection insurance, protection plans, extended service contracts, vehicle service contracts, and extended service plans, but not so much extended warranties. That phrase seems to have gone out of style. In fact, many industry experts say that term is misleading and should be avoided.

But even the very concept of playing the odds on defects and malfunctions is a bit outdated. Now, when we sell a service contract, what we're really selling is a solution for a dropped phone with a cracked screen. We're selling the convenience of someone stopping by to take your big screen off the wall and pack it into one of those taco shells for shipping. We're selling an auto mechanic you can trust, who will not rip you off when you need a routine repair. We're selling a Maytag repairman who answers the phone and shows up when he promised, and doesn't steal your watches or ask your daughter out for a date while he's inside your home.

They call it peace of mind, but it's really a series of reassurances that you're protected from harm when the time comes. And like fire insurance or life insurance, it's there though you hope you never need it. But unlike those protection plans, the administrator of a service contract has the opportunity to delight the consumer and make the process of getting a product repaired as hassle-free as possible. You can't put a price on that.

We buy VSCs because we know our cars break down, even when they're young. We cover our appliances because then we know who to call if they malfunction. And we cover our smartphones because we all know somebody who has a spider-web crack on their screen, who wishes they'd bought the protection plan.

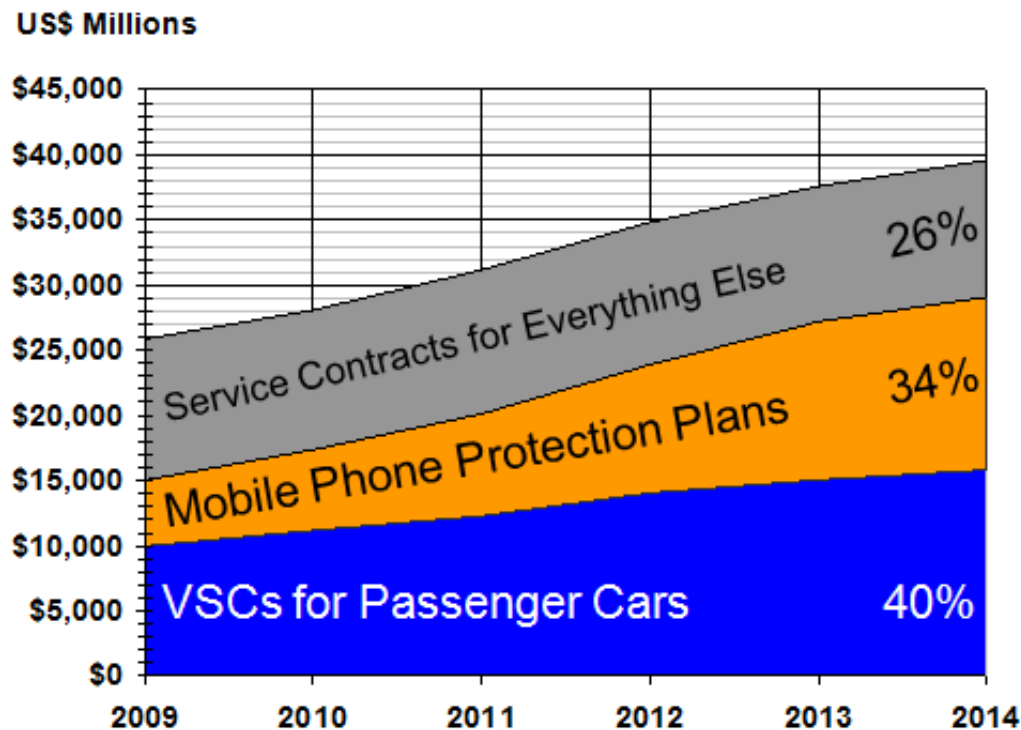
## No More Repairs?

With small and inexpensive electrical appliances, radios, televisions, digital cameras, and maybe even some laptops, consumers have learned that perhaps *Consumer Reports* is right: they're no longer worth protecting. But it's not because they never break or because repairs are inexpensive. It's because when they do break, they'll typically be replaced, not repaired. Besides, by the time they wear out, the new models will be twice as good and cost half as much.

In Figure 4, we've taken the data from Figure 1 and reorganized it a bit to put all the smartphone protection plan premiums into one bucket. All the VSC revenue is in another bucket. And then protection

plans for everything else, from pool pumps to printers, is in a third bucket (except for the furniture, jewelry and sports equipment service contracts that we've yet to count).

**Figure 4**  
**U.S. Consumer Service Contract Market**  
**Premiums Paid by U.S. Consumers, 2009 to 2014**  
**(estimates in U.S. dollars)**



Source: Warranty Week estimates

It's pretty obvious that the current market for service contracts basically comes down to this: VSCs, smartphones, and everything else. And everything else is now down to only 26% of the total, declining from a 42% share of the pie way back in 2009. But it's not that they've stopped selling, as much as that they stopped growing.

The VSC total has always been close to 40%, so what we're seeing is the smartphone segment growing faster than the average and turning into one of the few types of electronics that the typical consumer feels is still worth protecting. And that's a combination of the perceived value and vulnerability of the product. Smartphones are perceived to be expensive, sophisticated, and very fragile, like an [antique porcelain tea cup from the Ming dynasty](#). It's the perfect storm of peril versus peace of mind.

## Black Circles for Poor Performance

So we're going to give *Consumer Reports* a [black circle](#) for their poor rate of success when it comes to



talking U.S. consumers out of buying protection plans for their cars and smartphones. We expect the total market to grow more than five percent this year to more than \$39.5 billion, in spite of the magazine's [often-repeated negative advice](#). Keep screaming. Nobody's listening.

Perhaps the magazine's staff doesn't understand all the emotion tied up in the ownership of those products, or the value some people attach to the peace-of-mind they get from protecting them. And perhaps they haven't realized that their readers are the type who buy the best and never expect it to break -- they've never bought a service contract, and never will, because they believe they'll never need a repair if they stick to the brands that get the red circles and the full and half-moons. In other words, they're preaching to the choir, and the pews are empty.



[Mid-Year Warranty Expense Report: By comparing each company to itself over time, and then comparing the size of the changes, we can spot the companies with the most improved warranty costs and those in the most trouble.](#)[October 2, 2014 Extended Warranty Conferences: As the old saying goes, two's company, but three's a crowd. With the Warranty Chain Management Conference a fixture in the spring, two conferences are competing to become the industry's preferred event in the early fall. This year, they were three weeks apart, but next year, there's only three days between them.](#)[October 16, 2014](#)

An advertisement for Assurant Solutions. At the top is a blue-outlined graphic of a smartphone. Below it, on a dark grey background, is the text 'THE MOST IMPORTANT PART OF A CUSTOMER'S EXPERIENCE COMES AFTER THE SALE.' in white, all-caps font. At the bottom of the grey area is a blue button with the text 'CLICK TO LEARN MORE' and a white play button icon. Below the grey area is a white bar containing the Assurant Solutions logo (a colorful globe icon) and the text 'ASSURANT Solutions®'.





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- [Asurion develops new phone protection plans for Wind Mobile.](#)  
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- [Tesla is developing a certified pre-owned program for the Model S.](#)  
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- [South Carolina DMV reports telemarketing scam involving extended warranties.](#)  
WLTX-TV Columbia SC, October 6, 2014
- [James Rushton launches new consultancy called After Sales Solutions LLC.](#)  
Press Release, October 5, 2014 (PDF file)
- [Best warranty options for your new iPhone.](#)  
Cult of Mac, October 3, 2014
- [WMS Group call center to stay open for 24 hours a day, 365 days a year.](#)  
Press Release, October 2, 2014
- [Working through all the smartphone insurance and extended warranty options.](#)  
Chicago Tribune, October 2, 2014
- [Serra Nissan employees indicted on federal loan fraud conspiracy charges.](#)  
Birmingham Business Journal, October 2, 2014
- [Without receipts for oil changes, extended warranty claim denied.](#)  
KGTV-TV San Diego, October 2, 2014
- [GM's Vauxhall pulls the plug on its Lifetime Warranty in the UK.](#)  
Business Car Manager, October 2, 2014
- [Company doing business as the Motor Vehicle Division sends out expiring warranty letters.](#)  
Kent County (MD) News, October 2, 2014
- [Marketing Insight study finds car imports in Korea score low for warranty service.](#)  
Korea Bizwire, October 1, 2014
- [Kia Australia lengthens warranties from 5 to 7 years.](#)  
Motor Report, October 1, 2014
- [Modem that caused SkyTrain delays still under warranty.](#)  
Vancouver Sun, September 30, 2014
- [EFG Companies launches Simplicity Home Protection warranty program.](#)  
Press Release, September 30, 2014 (PDF file)
- [Apple begins sending out checks from liquid damage indicator lawsuit.](#)  
Mac Rumors, September 30, 2014
- [Reader survey finds 2% of Apple iPads and 3% of Samsung tablets failed.](#)  
Consumer Reports, September 30, 2014
- [Does your car have a hidden warranty?](#)  
WLS-TV Chicago, September 30, 2014
- [More details on "secret warranties."](#)  
Consumer Reports, September 30, 2014
- [Consumer Reports calls on Nissan to extend Juke and Maxima warranties.](#)  
Consumer Reports, September 29, 2014
- [Ford expects higher warranty costs, including recalls, in North America.](#)  
Press Release, September 29, 2014
- [MG, Rover & Daewoo cars most likely to experience head gasket failure, survey finds.](#)  
Car Dealer, September 29, 2014
- [Nevada regulators seek victims of Sensible Home Warranty's bankruptcy.](#)  
Reno Gazette-Journal, September 29, 2014
- [Limitations of the Victorinox "lifetime" warranty.](#)  
Los Angeles Times, September 29, 2014

- [Daniel Garcia of Danny's Auto World in Hartford accused of pocketing VSC premiums.](#)  
WTIC-TV Hartford CT, September 29, 2014
- [Cross Country Home Services wins two 2014 Golden Bridge Awards.](#)  
Press Release, September 25, 2014
- [SaskTel customers angry about disappearance of the Global Warranty Group.](#)  
Global News, September 25, 2014
- [Global Warranty Group goes out of business, customers kept in the dark.](#)  
CBC News Saskatchewan, September 25, 2014
- [The latest iPhone scandal: "Bendghazi."](#)  
Slate, September 25, 2014
- [Apple says it has received only 9 complaints of bent iPhone 6 Plus devices.](#)  
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**How to Buy Extended Warranties:** Step One: Read the contract. Research the terms and conditions of the service contract while you compare the prices and features of the products themselves. Then use your common sense and Google to decide if the extended warranty offer is a deal worth adding, or if you should shop elsewhere.

**Extended Warranty Administrators:** While auto and PC manufacturers have the top spots, insurance companies and third party administrators grab the bulk of the pie.

**Flat Rate Extended Warranties:** For shoppers, the choice at the cash register is to say yes or no. The competition is between administrators vying for exclusive contracts with the retailers. But now there's a new choice, for consumers to go home and buy their extended warranties over the Internet.

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