3 Investing Lessons From BlackBerry

Description

BlackBerry (TSX:BB, NASDAQ:BBRY) has just released its much anticipated earnings report. And judging from the market's reaction, investors are impressed with John Chen's vision for the company.

But the damage has already been done. Maybe the troubled handset maker will be able to engineer some kind of a turnaround, but it's unlikely the company can recover the billions of dollars in shareholder capital that has been lost.

And given the stock's mass appeal, no doubt thousands of regular investors took a painful licking on this one. Unfortunately, losses are just the tuition we all have to pay to Mr. Market on our investment journey.

But rather than just giving up, it's a good practice to reflect on past mistake to avoid repeating them in the future. Here're three lessons investors should take from BlackBerry.

1) Be skeptical of 'cheap'
Since 2011, BlackBerry shares have always looked deliciously 'cheap'. When the stock was trading below 10 times earnings, many investors didn't look past the price tag.

Afterall, how much more could the stock go down?

They forgot the E in P/E can disappear quickly.

Then in the past year or two other investors noticed the stock trading below its book value. In theory, the stock could fall any further because you could just liquidate the business and ensure a guaranteed profit.

But the stock traded at such a steep discount for a reason. The company was burning through cash. The inventory on the books was grossly overvalued. And if management doesn't want to sell the business, it doesn't matter how big the discount to book value is.

Usually in investing, you get what you pay for. Like buying a $20 pair of shoes at **Wal-Mart** versus

$200 for a pair at **The Bay**, there *is* a difference in quality. Don't be afraid to pay up for best of breed.

When something's too good to be true, it probably is. The next time you spot an amazing deal, ask what might the market might be pricing in. While Mr. Market certainly makes mistake from time to time, he usually get it right.

2) Know your moat
The decline of BlackBerry illustrates just how fragile competitive advantages are in the technology industry.

What was BlackBerry's competitive advantage? They were the first to put email on a mobile phone. It was a spectacularly successful idea.

Then **Apple** copied it…and **Google**…and **Nokia**…and **Microsoft** and so on. Other technological innovations also wore away at BlackBerry's profits.

Any business that earns excess returns is going to be under attack in the marketplace. That why a *sustainable* competitive advantage is so important.

When evaluating an investment, you have to ask yourself if this company's moat can hold up over the next 10, 20, 50 years.

It's hard for me to imagine a major new competitor emerging for say **Royal Bank**. But reinventing a consumer gadget isn't actually that hard. It happens every few years.

If a technology company isn't constantly innovating, it will be left by the wayside. That's an awfully challenging business and one I'd rather avoid as an investor.

3) Don't bet on the underdog
I love underdog stories. Is there anything better than watching a challenger rise to the top in the face of overwhelming odds?

But investing is not about stories. In business raw size beats tenacity every time.

When BlackBerry released the Z10 it was going up against Apple and Google, two of the largest technology companies on Earth. More importantly iOS and Android boasted well established product ecosystems. A hurdle that would be pretty difficult to overcome.

Sure in the technology space, small companies occasionally disrupt the industry. But the next big thing is just as likely to come out of some guy's garage than BlackBerry's R&D department.

In the meantime I would much rather own the biggest, baddest names out there.

Foolish bottom line
So what's in store for BlackBerry? I have no idea.

There may be considerable value to unlock from inside the business and CEO John Chen may just have the plan to turn the company around.

But regardless of what the future might hold, the stock should serve as a useful lesson for investors.

CATEGORY

1. Investing

TICKERS GLOBAL

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