3 Companies Vulnerable to Disruption

Description

We've seen it happen over and over. A company churns out healthy profits year after year. Customers are loyal. Investors are happy. And then, slowly but surely, their business models start to erode. Sometimes it's a new technology, other times it's a cheaper alternative. But when companies are making so much money off of their core products, they can be very slow to adapt.

These types of situations are profiled extensively in Clayton Christensen's book *The Innovator's Dilemna*. And they can be devastating for investors.

Below are three companies that could be vulnerable to "disruption", as Mr. Christensen refers to it.

Transcontinental

In both the United States and in Canada, anything to do with paper does not get a lot of love from investors. As digital media captures more and more of our attention, these companies risk getting left behind. Many of these printing businesses talk about digital as an opportunity for growth. But the transition is rarely that lucrative – digital media has fewer barriers to entry, and as a result is far more competitive and far less profitable.

One Canadian company in this predicament is **Transcontinental Inc.** (TSX: TCL.A). Transcontinental makes most of its revenue off of products such as flyers, magazines, newspapers, and other forms of mass marketing. The company is doing its best to transition to the digital world, but in the most recent quarter revenue was down 5%. It's going to be a struggle.

Thomson Reuters

Thomson Reuters (TSX: TRI)(NYSE: TRI) makes its money off of selling information services, mainly to law firms and financial services companies. This has very attractive economics, but also faces issues.

In the legal space, the problem is that traditional law offices are facing more competition than ever from cheaper alternatives. And clients have become less willing to pay sky-high fees. This is slowly eroding the prospects for big law firms, which is Thomson's most lucrative market for its legal products.

In the financial and risk division, Thomson is facing a more competitive environment for its products. On one side, Bloomberg offers a premium product that is much more popular in the marketplace. On the other side, providers like **Factset** and Capital IQ are offering cheaper alternatives.

Thomson does have some "growth businesses", which it loves to highlight. But revenue growth for the company as a whole is practically non-existent, and Thomson is having to fight harder than ever for market share.

AlarmForce

Like Thomson Reuters, **AlarmForce** (TSX: AF) offers a subscription-based product with high customer retention rates. So what's not to like?

The problem for AlarmForce is new sources of competition, above all Smart Home Monitoring from **Rogers** (TSX: RCI.B)(NYSE: RCI). The good news is that Rogers is not undercutting AlarmForce on price; in fact if you want 2-way voice monitoring, AlarmForce is cheaper than Rogers.

But Rogers has much deeper pockets than AlarmForce, and looks determined to win in this market. Furthermore, as one of Canada's big three telecom providers, Rogers has more technological capabilities than AlarmForce, and can use those capabilities to offer more features. AlarmForce deserves credit for continuing to grow its revenue and subscriber base; those numbers were up 10% and 5% respectively in 2013. But if Rogers is determined enough to steal market share, one has to wonder how long AlarmForce can continue to grow.

Disruption stories can be very tricky for investors. Once-great companies can see their earnings decline very quickly, and stocks that appear cheap can get a lot cheaper. In these situations, it's usually a good idea to just stay away.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NASDAQ:TRI (Thomson Reuters)
2. NYSE:RCI (Rogers Communications Inc.)
3. TSX:RCI.B (Rogers Communications Inc.)
4. TSX:TCL.A (Transcontinental Inc.)
5. TSX:TRI (Thomson Reuters)

Category

1. Investing

Date
2025/07/26
Date Created
2014/05/06

Author
bensinclair