



BlackBerry Ltd. Is Finally Giving Up

Description

For years the future of **BlackBerry Ltd.** ([TSX:BB](#))(NASDAQ:BBRY) has depended not on its well-known phone-manufacturing business, but on its fledgling software segment. Even BlackBerry's CEO knows software will undoubtedly be the future: "I personally do not believe devices are going to be the future of any company," he reportedly said.

This month the company finally admitted defeat, revealing that it will discontinue production of its Classic cellphone model. Other outlets also reported that BlackBerry has told major U.S. carriers like **Verizon Communications Inc.** and **AT&T Inc.** that all devices running BlackBerry 10 will be discontinued. According to *The Globe and Mail*, BlackBerry is finally starting to "shift its focus further away from its money-losing handset business and toward its software."

By giving up on handset hardware, will BlackBerry finally deliver long-term value to shareholders?

Ditching hardware is a major step

After peaking at 20% in 2009, BlackBerry's smartphone market share has fallen to just 1%. Failing products resulted in crumbling financials. Since 2011 revenues are down 70% with profits swinging to a loss.

While hardware is in the DNA of BlackBerry, it looks like it's time to admit defeat. The company's latest smartphones have continually been disappointments and are expensive to continue developing. Over 65% of BlackBerry's research and development expenses are related to hardware. By ditching a money-losing business that is a significant drag on cash flows, BlackBerry could stage a turnaround in a matter of months, not years.

Can software fill the gap?

On June 23, BlackBerry released its quarterly earnings report, and for the first time ever, it generated more revenue from software than from its handset division. Sales for its software and services unit grew to US\$166 million in the first quarter, besting declining hardware revenues of just US\$152 million.

The handset division sold 500,000 phones during the quarter, nearly 100,000 fewer than the quarter before. In the mid-2000s, the company was selling millions of phones every quarter.

The transition towards software should come with a few major advantages. First, these sales come with higher profit margins, a fairly easy task considering the handset business has been generating losses for years. Second, 70% of software sales are recurring, meaning BlackBerry can count on these sales for many quarters to come. "If it is successful, the sustainability of profitability is very high," BlackBerry's CEO has said.

A sale could speed up the process

For nearly five years, BlackBerry stock has been stuck at about \$10 a share. Moving towards software is clearly the best long-term option for returning to profitability. That process, which may take years, could be shortened considerably with a sale of the company, a proposition that was made all but impossible under the former Canadian administration.

"We are under a different administration now," BlackBerry's CEO said. "I don't want to get into politics, but a statement was made under the prior regime. I think the whole Canadian-champion concept ... I don't believe the same standard applies nowadays."

Finally, BlackBerry appears to be on the verge of generating long-term value, all while maintaining the option for a quicker profit in the form of a buyout.

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