



# Incumbent Firms Change Course to Counter Tech Disruption

Disney, Walmart, and GM are undergoing notable strategic shifts.

October 2019

## KEY INSIGHTS

- Disruption is increasingly a harsh reality for many once-dominant incumbent, or legacy, companies, but these days some of these firms are fighting back.
- Varied efforts to counter disruption abound, with incumbents developing their own capabilities, acquiring or partnering with innovators, or some combination of these.
- Some of the strategic shifts are just defensive—aimed at stemming losses—and the outcomes are mostly yet to be determined.

Disruption is increasingly a harsh reality for many once-dominant incumbent, or legacy, companies. Netflix and other streaming content services have upended cable TV. Amazon and other online vendors have challenged brick-and-mortar retailers. Tesla has pushed automakers to innovate with its electric vehicles and the promise of self-driving ones.

But these days, “some of the legacy companies have recognized how this is playing out and are fighting back aggressively,” says Rob Sharps, T. Rowe Price head of investments.

Varied efforts to counter disruption abound across a wide range of endeavors. For example, Marriott has launched an Airbnb-type property rental service called Homes & Villas. And Prudential is buying online life insurance startup Assurance IQ.

“Incumbents are going about this in many ways: by developing their own capabilities, acquiring or partnering with

innovators, or some combination,” says Jason Nogueira, manager of the Global Consumer Strategy. “Some are just trying to stem losses to upstarts. A lot of the outcomes are yet to be determined.”

That said, here are three examples of areas in which disruption has taken place—each with an example of a particular incumbent firm that has shifted its strategy to fight back. (The examples were chosen to illustrate T. Rowe Price investment managers’ thinking about industry and corporate trends.)

## 1. Disney Breaks With the “Linear Television Ecosystem”

Traditional cable and broadcast TV are dying—and, along with it, the business models of Disney and other incumbent creators of movies and television shows.

TV viewing is down with all age groups, except those age 65 years and older; it’s fallen more than 60% for viewers ages 12 to 24 since 2010, according to



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# 150 million

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Nielsen ratings. As ratings fall, so does ad revenue. And cord cutting means the cable subscriber fees paid to content creators are shrinking.

Disney—and other content creators like Warner Brothers, CBS, and Viacom—traditionally sold their products to such distributors as Comcast or Dish in what’s termed the “linear television ecosystem.” This provided content companies with great leverage, according to Paul Greene, Communications & Technology Strategy manager, as content creators didn’t have to build relations with individual consumers and could stuff some channels with syndicated reruns.

But then came Netflix, offering high-quality content globally, with no ads, on demand, and at an affordable price—demonstrating that “TV’s future is direct to consumer,” Mr. Greene says. With currently about 150 million global subscribers, he says, Netflix can invest huge sums in creating content—it came out with more than 50 new shows in August 2019 alone.

To counter, Disney has taken the radical step of pulling back its content from distributors and launching an online, direct-to-consumer service, Disney+. It also will offer a separate bundle that includes Disney’s majority-owned Hulu and a spinoff of its ESPN subsidiary, ESPN+.

From now on, Star Wars, Marvel, Pixar, and other Disney movie franchises—which collectively accounted for about half of this summer’s U.S. box-office receipts—will go to theaters first and then right to Disney+, skipping premium cable channels and DVD sales, Mr. Greene says.

“By offering a limited number of blockbuster movies every year, Disney+ will be more event-driven and likely function well alongside the ongoing vast selection offered by Netflix,” he says.

Disney of course is not alone. Many other content creators are taking similar steps, Mr. Greene says, but few—save perhaps Amazon—have the brand and

resources to compete with Netflix for general entertainment.

“It’s hard to find legacy media companies that are going to be successful at this,” he says. “This is a great narrative right now, but let’s check back in five years.”

## 2. Walmart Makes Gains With “Click and Collect”

Every day brings new evidence of the “retail apocalypse,” the devastation of brick-and-mortar stores wrought by Amazon’s rocketing growth. But long-dominant Walmart, itself once a disrupter, is fighting back by rapidly developing its online channels.

Walmart’s transition began with the purchase of Jet, an online retailer, and Flipkart, an Indian online vendor—plus heavy investments in its digital capabilities. “In the beginning, the market didn’t give Walmart the benefit of the doubt,” Mr. Nogueira says. “But now it’s demonstrated that it can win, at least in certain segments, such as groceries.”

For now, the key to Walmart’s grocery gains has been no-cost “click and collect.” Customers order groceries online and pick them up at a designated time, with the orders brought to their cars—somewhat like a drive-through lane at a fast-food outlet. Recently, it launched an unlimited grocery home delivery service for USD 98 a year.

Ultimately, Mr. Nogueira says, “click and collect” is a hybrid solution. The endgame, he says, will be free home delivery of groceries within hours of ordering. “The question is who will get there first,” he says.

In this, Walmart faces many competitors, not least Amazon; Target; Costco; and Kroger, the nation’s largest supermarket chain, now partnering with British logistics firm Ocado, to master delivery.

“Hiring someone to go around a Walmart and pick up grocery items is not cost-effective in the long run versus having dedicated, fully automated warehouses to fill orders,” Mr. Nogueira says.

“GM has decided that, in the next 10 to 15 years, it’s all about electric vehicles.

— Joel Grant  
*Investment Analyst, Industrials and Business Services Sector*

### 3. General Motors’s EV Future Is Now

In the future, cars will be electric-powered, self-driving, and perhaps available on demand rather than individually owned. But no one knows when that future will arrive. Tesla is hurtling forward and pushing General Motors (GM), more than 110 years old, to undergo a historic transition faster than once anticipated.

GM has announced that over the next few years it will introduce about 20 new electric vehicles (EVs). “GM has decided that, in the next 10 to 15 years, it’s all about electric vehicles,” says Joel Grant, a T. Rowe Price auto analyst.

After more than a century of gas-powered engines, this profound change means all car components—save for the chassis and interior—are changing too, Mr. Grant says. GM and other original equipment manufacturers (OEMs) “are rethinking cars from the ground up,” he says.

While GM’s pickup and SUV franchises remain strong, Mr. Grant says, “it essentially decided EVs are going to be cheaper, better cars, and GM must

embrace this and be really good at it. This is risky because no company is making money on EVs, and most consumers are unwilling to pay the EVs’ premium. But that premium is expected to fall rapidly with greater production scale—to where the costs are relatively the same as combustion vehicles.”

Beyond EVs, GM also has jumped into developing self-driving cars by buying a startup, now called GM Cruise LLC, as a separate entity to attract talent and outside capital. In the meantime, GM separately has come out with new technology on certain Cadillacs, called “Super Cruise,” which GM says is “the first true hands-free driving assistance feature” for certain types of highways, but which Mr. Grant says is like Tesla’s autopilot feature.

As with Disney and Walmart, GM is not alone in responding to disruption. Volkswagen and Daimler similarly are embracing EVs, for example. “There’s still skepticism about EVs’ profitability,” Mr. Grant says. “So the question over the next couple years is how much profits from trucks and SUVs can sustain manufacturers transitioning to EVs.”

### WHAT WE’RE WATCHING NEXT

Among the key questions facing incumbent firms shifting their strategies in the face of disruption from technological innovators is how much their losses in these transitions may total before potential gains from their new business models kick in. For example, Walmart is going to have to invest more to compete with Amazon and others to widely offer low- or no-cost, same-day delivery of groceries. Similarly, Disney is likely to endure headwinds from forgone licensing revenue as it pulls its content away from legacy distribution channels. And GM likely will have to rely on pickups and SUV sales to see it through its historic shift to EVs. For GM and other automakers, notes Auto Analyst Joel Grant, beyond that is the ultimate question of how quickly a high level of semi-autonomous technology “can make it into our cars—making them safer and cheaper to insure and allowing us more productivity in cars. This will be a game changer.”

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