

NEW RISK ALERT: (MSFT)

Microsoft Warns of Potential Sales Decline Even If It's Not at Fault in Future IT Supply Chain Attacks

New language in latest 10-Q indicates Microsoft sees risk of reputational damage in new, sophisticated future cyber attacks.

Published January 26, 2021

This alert compares the language used in the company's latest filing with the period before. [Research](#) suggests changes in language, particularly in the risk factor section, is a powerful indicator of future performance. Companies that change filing language, according to research, underperform those that don't by 30-50 basis points per month for the following year.

Microsoft Sees Dual Risk as Hackers Target Weak Links in IT Supply Chain

The latest [10-Q](#) details a new language detailing what Microsoft calls a software supply chain attack. The company characterizes the threat as malicious actors accessing the information technology (IT) supply chain to introduce malware through software updates or compromised supplier accounts or hardware. Not only does Microsoft disclose it was victimized in a recent, highly publicized attack, the company also discloses how it may be victimized twice:

"We may be targets of further attacks similar to Solorigate as both a supplier and consumer of IT."

Even if Microsoft isn't directly compromised, it is exposed to the new threat via its software and data center customers. As you'd expect, Microsoft actively works to identify, notify, and offer guidance to customers whose systems have been compromised. Besides increased costs and lower operating margins, Microsoft warns of reputational risk of notifying customers who have been victimized:

*"We may not be able to detect the existence or extent of these attacks for all of our customers...If we fail to do these things well, actual or perceived security vulnerabilities in our products and services, data corruption issues, or reduced performance could harm our reputation and lead customers to **reduce or delay future purchases of products or subscriptions to services, or to use competing products or services.**"*

Subtle Hint Suggests Potential For Regulatory Creep Related to Data Privacy

The global data privacy debate has centered around the consumer. But Microsoft's latest 10-Q includes a subtle hint suggesting that any new regulation may extend beyond customers. Last quarter, the warning appeared as such:

"Data protection authorities may assert that our collection, use, and management of customer data is inconsistent with their laws and regulations."

The latest 10-Q tweaks the language— albeit slightly— hints at potential new regulation on data unrelated to customers and not yet on investors' radar:

*"Regulators may assert that our collection, use, and management of customer **and other data** is inconsistent with their laws and regulations."*

Though subtle, it's intentional and suggests the battle over data and how it's used includes risks not currently priced into markets. Types of data the above language may be referring to include diagnostic and service data for Windows. These data sets allow Microsoft to monitor, troubleshoot, and improve its offerings in real time. Limiting the collection and use of such data could adversely impact product quality