J. Michael Locke
Musings

#120: Musing
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One breakdown in our public equity markets is the poor oversight/governance provided by institutional money managers. U.S. corporate law puts the ultimate power in the hands of the "owners"-- the shareholders. However, with the rise of mutual funds, the "owners" with their money at risk now go through a middleman. Too many mutual fund managers ignore their oversight responsibility. Wall Street contributes to this failure by looking through "one-time charges." Case in point: last month, ATT announced a deal to spin-off DirectTV which it bought in 2015. ATT paid $48.5bn. The spinoff valued DirecTV at $16.25bn. They lost $32bn on the acquisition! Mispriced it by over 60%. Where is the accountability? It will be written off as a one-time reduction in goodwill.

On the opposite end of the spectrum are good activist investors like ValueAct capital started by Jeff Ubben. In 2013, ValueAct bought roughly 1% of Microsoft for $2bn and pushed for a change of CEO and strategy. They got underperforming CEO Steve Ballmer out and helped push the hiring of one of the most underappreciated CEOs today (Satya Nadella). Microsoft stock has gone from $35 to $232 since ValueAct came in. We need more stock held by activist investors with their own money on the line and less held by mutual fund managers just collecting fees based on AUM (assets under management) regardless of performance. A good investment strategy might be just to follow firms like ValueAct who buy public equities and must disclose their position. BTW – one of the takeaways from the Archegos debacle is how Bill Hwang's firm was able to take huge "economic" positions in companies without actually owning the stock via "Total Return Swaps" so he didn't have to disclose his positions to the public. Regulations need to change to capture that.

The financial markets are currently being driven by inflationary expectations. The fed has openly and passionately emphasized the full employment pillar of its "dual mandate" (the other being controlling inflation) and the government is currently undertaking massive deficit spending. Good article in the Economist (thanks Bob Thompson) on how consumer inflationary expectations determine the strength of the anchor (Economist article here just-how-anchored-are-americas-inflation-expectations). The disruption in the supply chain due to the Suez canal situation is not going to help as consumers already are seeing rising gas prices and six month waits for a couch. Add in the rapidly expanding vaccination numbers and I think there is going to be a blow-out in consumer demand.

The labor market is starting to reflect this building economic momentum. A surprisingly high number of jobs were created and unemployment went down according to the monthly jobs report released yesterday. I wish we could move the focus away from unemployment rate and towards the labor participation rate or the employment-population ratio. These latter two measures show that only 55-60% of our population is working. Long term it is hard to grow an economy when 1 out of 2 people are not working. I also think work has broader positive social effects like greater cohesion and added meaning to life. *For the macroeconomic wonks in the readership, the actual BLS (Bureau of Labor Statistics) press release is printed at the bottom of this musing after my initials.*

Modern management theory has moved from a "command and control" military style to one of "empowerment," especially of millennial employees. I worry it is going too far and we are now "enabling" employees (and many children) in a way that hurts their development and ultimately their capabilities. We need to stop "snowplowing" and using purple pens (yes, some teachers have moved away from red when grading because it is "too harsh"). Development comes from having to work hard on something and figure things out. Employees need to struggle to grow. Great article from a couple years ago on the "Tyranny of Convenience" which describes how technology is making things too easy. tyranny-convenience In contrast, go rewatch the 2004 movie "Miracle" about the 1980 Olympic hockey team. We need more Herb Brooks' leadership where individuals are challenged to perform to their peak potential not coddled. (Fun fact: Mike Eruzione still gets $25,000 to give a speech. Or you can get go cheap and get a customized video message from Dennis Rodman on Cameo for $750.)

Kudos to new Citibank CEO Jane Fraser who has called for "Zoom Free Fridays" to combat Zoom fatigue. She also announced that when folks return to the office, most will do three days in the office and two at home. The "norm" for returning to the office post-pandemic seems to be settling in around a hybrid work model with some days in the office and some days from home. While some companies have announced moving to a fully remote model (ex. Salesforce), I think it is hard to build company culture in a fully remote model. Managers need to be working extra hard to connect with employees working from home doing things like building in non "productive" time. Good article about Microsoft addressing this challenge. microsoft-message-to-managers-after-decline-in-team-connections . I also think employees will be more interested in working from the office than some people think. Working from home can be lonely. Good article: zoom-remote-work-loneliness-happiness. So I think the art form is to provide the employee with some control – flexibility at their discretion -- so they aren't required to come in 5 days a week but many will.

One beneficiary of a move to blended work model is WeWork. After the debacle of the attempted IPO and the transparency our securities laws provided on the shortcomings of former CEO Adam Neumann (I have been told "Billion Dollar Loser" is a good read) and the poor corporate governance, WeWork has actually been fixing its problems and recently announced a deal to go public via a SPAC. Still losing money but in a much better place and projected to make money next year. In a hybrid model, companies may ditch the long term fixed office lease and what more flexible arrangements like that provided by WeWork.

A Covid innovation is the arrival of "virtual brands" where existing operators in the restaurant space have created brands and products only offered online via food delivery. Example is Applebee's which created "Cosmic Wings" to offer Cheeto-covered chicken wings (applebees-launches-cheetos-inspired-virtual-wings-brand). This move allows product extensions without brand confusion. It is also often using "demand side product development" where you use search results/website behavior to figure out what customers want. The food delivery operators share what consumers are looking for and the restaurants can then respond (or they can just create a whole new delivery-only restaurant with a ghost kitchen.) This dynamic is happening in other spaces like children's books. Digital book company Epic has used website tracking to launch big hits. Per WSJ: *"Epic's team knows that children prefer owls to chickens and chickens to hedgehogs. Kids hunt for unicorns almost twice as often as they look for mermaids. Volcanoes are more popular than tsunamis, which are more popular than earthquakes. The Titanic is bigger than cowboys, pizza is bigger than cake, science is bigger than art and "poop" is bigger than all of them."*

RIP Libor. Stands for the London Interbank Offering Rate. A survey is done on what rate banks in London are charging each other to borrow money. Most commercial loans are priced at Libor + "x" bps. With bps being basis points (one bps is .01%). The x is the increased rate necessary to compensate for risk so this spread over Libor goes up the riskier the credit. There was a scandal roughly a decade ago where folks were manipulating the survey to control Libor leading to its demise. Unclear what the alternative will be but the Fed is demanding banks stop doing loans in Libor by year end.

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From the Dept. of Labor for the economic geeks:

THE EMPLOYMENT SITUATION -- MARCH 2021

Total nonfarm payroll employment rose by 916,000 in March, and the unemployment rate edged down to 6.0 percent, the U.S. Bureau of Labor Statistics reported today. These improvements in the labor market reflect the continued resumption of economic activity that had been curtailed due to the coronavirus (COVID-19) pandemic. Job growth was widespread in March, led by gains in leisure and hospitality, public and private education, and construction.

This news release presents statistics from two monthly surveys. The household survey measures labor force status, including unemployment, by demographic characteristics. The establishment survey measures nonfarm employment, hours, and earnings by industry.

Household Survey Data

The unemployment rate edged down to 6.0 percent in March. The rate is down considerably from its recent high in April 2020 but is 2.5 percentage points higher than its pre-pandemic level in February 2020. The number of unemployed persons, at 9.7 million, continued to trend down in March but is 4.0 million higher than in February 2020.

Among the major worker groups, the unemployment rate for Asians rose to 6.0 percent in March, following a decline in the previous month. The jobless rate for Hispanics edged down to 7.9 percent over the month, while the rates for adult men (5.8 percent), adult women (5.7 percent), teenagers (13.0 percent), Whites (5.4 percent), and Blacks (9.6 percent) changed little.

Among the unemployed, the number of persons on temporary layoff declined by 203,000 in March to 2.0 million. This measure is down considerably from the recent high of 18.0 million in April 2020 but is 1.3 million higher than in February 2020. The number of permanent job losers, at 3.4 million, was little changed in March but is 2.1 million higher than February 2020.

The number of long-term unemployed (those jobless for 27 weeks or more), at 4.2 million, changed little over the month but is up by 3.1 million since February 2020. In March, these long-term unemployed accounted for 43.4 percent of the total unemployed. The number of persons jobless 5 to 14 weeks declined by 313,000 to 1.9 million. The number of persons jobless less than 5 weeks, at 2.2 million, was essentially unchanged over the month.

The labor force participation rate changed little at 61.5 percent in March. This measure is 1.8 percentage points lower than in February 2020. The employment-population ratio, at 57.8 percent, was up by 0.2 percentage point over the month but is 3.3 percentage points lower than in February 2020.

The number of persons employed part time for economic reasons, at 5.8 million, changed little in March but is 1.4 million higher than in February 2020. These individuals, who would have preferred full-time employment, were working part time because their hours had been reduced or they were unable to find full-time jobs.

The number of persons not in the labor force who currently want a job was about unchanged at 6.9 million in March but is up by 1.8 million since February 2020. These individuals were not counted as unemployed because they were not actively looking for work during the last 4 weeks or were unavailable to take a job.

Among those not in the labor force who currently want a job, the number of persons marginally attached to the labor force, at 1.9 million, was essentially unchanged in March but is up by 416,000 since February 2020. These individuals wanted and were available for work and had looked for a job sometime in the prior 12 months but had not looked for work in the 4 weeks preceding the survey. The number of discouraged workers, a subset of the marginally attached who believed that no jobs were available for them, was 523,000 in March, essentially unchanged from the previous month.

Household Survey Supplemental Data

In March, 21.0 percent of employed persons teleworked because of the coronavirus pandemic,

down from 22.7 percent in the prior month. These data refer to employed persons who teleworked or worked at home for pay at some point in the last 4 weeks specifically because of the pandemic.

In March, 11.4 million persons reported that they had been unable to work because their employer closed or lost business due to the pandemic--that is, they did not work at all or worked fewer hours at some point in the last 4 weeks due to the pandemic. This measure is down from 13.3 million in the previous month. Among those who reported in March that they were unable to work because of pandemic-related closures or lost business, 10.2 percent received at least some pay from their employer for the hours not worked, little changed from the previous month.

Among those not in the labor force in March, 3.7 million persons were prevented from looking for work due to the pandemic. This measure is down from 4.2 million the month before. (To be counted as unemployed, by definition, individuals must be either actively looking for work or on temporary layoff.)

These supplemental data come from questions added to the household survey beginning in May

2020 to help gauge the effects of the pandemic on the labor market. The data are not seasonally adjusted. Tables with estimates from the supplemental questions for all months are available online at www.bls.gov/cps/effects-of-the-coronavirus-covid-19-pandemic.htm.

Establishment Survey Data

Total nonfarm payroll employment increased by 916,000 in March but is down by 8.4 million, or 5.5 percent, from its pre-pandemic peak in February 2020. Job growth in March was widespread, with the largest gains occurring in leisure and hospitality, public and private education, and construction.

In March, employment in leisure and hospitality increased by 280,000, as pandemic-related restrictions eased in many parts of the country. Nearly two-thirds of the increase was in food services and drinking places (+176,000). Job gains also occurred in arts, entertainment, and recreation (+64,000) and in accommodation (+40,000). Employment in leisure and hospitality is down by 3.1 million, or 18.5 percent, since February 2020.

In March, employment increased in both public and private education, reflecting the continued resumption of in-person learning and other school-related activities in many parts of the country. Employment rose by 76,000 in local government education, by 50,000 in state government education, and by 64,000 in private education. Employment is down from February 2020 in local government education (-594,000), state government education (-270,000), and private education (-310,000).

Construction added 110,000 jobs in March, following job losses in the previous month (-56,000) that were likely weather-related. Employment growth in the industry was widespread in March, with gains of 65,000 in specialty trade contractors, 27,000 in heavy and civil engineering construction, and 18,000 in construction of buildings. Employment in construction is 182,000 below its February 2020 level.

Employment in professional and business services rose by 66,000 over the month but is down by 685,000 since February 2020. In March, employment in administrative and support services continued to trend up (+37,000), although employment in its temporary help services component was essentially unchanged. Employment also continued on an upward trend in management and technical consulting services (+8,000) and in computer systems design and related services (+6,000).

Manufacturing employment rose by 53,000 in March, with job gains occurring in both durable goods (+30,000) and nondurable goods (+23,000). Employment in manufacturing is down by 515,000 since February 2020.

Transportation and warehousing added 48,000 jobs in March. Employment increased in couriers and messengers (+17,000), transit and ground passenger transportation (+13,000), support activities for transportation (+6,000), and air transportation (+6,000). Since February 2020, employment in couriers and messengers is up by 206,000 (or 23.3 percent),while employment is down by 112,000 (or 22.8 percent) in transit and ground passenger transportation and by 104,000 (or 20.1 percent) in air transportation.

Employment in the other services industry increased by 42,000 over the month, reflecting job gains in personal and laundry services (+19,000) and in repair and maintenance (+18,000). Employment in other services is down by 396,000 since February 2020.

Social assistance added 25,000 jobs in March, mostly in individual and family services (+20,000). Employment in social assistance is 306,000 lower than in February 2020.

Employment in wholesale trade increased by 24,000 in March, with job gains in both durable goods (+14,000) and nondurable goods (+10,000). Employment in wholesale trade is 234,000 lower than in February 2020.

Retail trade added 23,000 jobs in March. Job growth in clothing and clothing accessories stores (+16,000), motor vehicle and parts dealers (+13,000), and furniture and home furnishing stores (+6,000) was partially offset by losses in building material and garden supply stores (-9,000) and general merchandise stores (-7,000). Employment in retail trade is 381,000 below its February 2020 level.

Employment in mining rose by 21,000 in March, largely in support activities for mining (+19,000). Mining employment is down by 130,000 since a peak in January 2019.

Financial activities added 16,000 jobs in March. Job gains in insurance carriers and related activities (+11,000) and real estate (+10,000) more than offset losses in credit intermediation and related activities (-7,000). Financial activities has 87,000 fewer jobs than in February 2020.

Employment in health care and information changed little in March.

In March, average hourly earnings for all employees on private nonfarm payrolls fell by 4 cents to $29.96. Average hourly earnings for private-sector production and nonsupervisory employees, at $25.21, changed little (+2 cents). The large employment fluctuations over the past year--especially in industries with lower-paid workers--complicate the analysis of recent trends in average hourly earnings.

The average workweek for all employees on private nonfarm payrolls increased by 0.3 hour to 34.9 hours in March, following a decline of 0.4 hour in the prior month. In manufacturing, the workweek increased by 0.2 hour to 40.5 hours over the month, and overtime increased by 0.1 hour to 3.3 hours. The average workweek for production and nonsupervisory employees on private nonfarm payrolls rose by 0.3 hour to 34.3 hours.

The change in total nonfarm payroll employment for January was revised up by 67,000, from +166,000 to +233,000, and the change for February was revised up by 89,000, from +379,000 to +468,000. With these revisions, employment in January and February combined was 156,000 higher than previously reported. (Monthly revisions result from additional reports received from businesses and government agencies since the last published estimates and from the recalculation of seasonal factors.)