

## J. Michael Locke

### Musings

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#### #164: Musing February 4, 2022

Most companies need to do a better job of managing CAC / LTV, that is the cost of customer acquisition (CAC) compared to the lifetime value (LTV) created by that customer. This looks at every customer like a profit center, how much it costs to get them, and how much profit they generate, which will then cover overhead expenses. SaaS businesses do a decent job but the basic rubric applies to all businesses. Personally, I prefer using gross margin rather than revenue for the LTV. You shouldn't pay \$5,000 to attract a customer who will spend \$6,000 with 50% gross margin. That business will never make money. Time also needs to be considered. By definition, LTV happens over time so you could lose money on that customer for a while since the CAC happens first. I believe the breakeven point should be a year or less but it depends on renewal rates/recurring purchases and access to capital fund CAC early.

With the arrival of high inflation, many companies will raise prices to offset increases in their cost structure. Another option is to change your bundling. According to the WSJ, one fast food restaurant is changing the number of chicken nuggets in its' offering from 10 to 8. Pretty clever. Would you have even noticed? Look for other reductions in food volumes or unbundling like hotels no longer defaulting to daily housekeeping.

It is best to match the dynamics of your revenue line to the dynamics of your cost structure. WeWork totally violated this principle as it signed fixed commitment expensive long-term leases (its' cost) and then sought to sell "fractional" shares month to month (its' revenue). Spotify is an interesting model. It gets \$15-\$20 per month flat fee but then pays out royalties based on usage. It makes decisions harder – does it matter if Neil Young comes off the list of artists available? I bet they have some really good analytics to "infer" the value of a given artist to the bundle based on how often they are listened to. My guess is Joe Rogan listening minutes beat Neil Young and Joni Mitchell by 100,000 to 1. Compliments to Neil Young on standing behind his principles as he will lose 60% of his streaming income by coming off Spotify.

Earnings season showing a divergence amongst tech companies. Good results for Amazon, Google, Apple and Snap. Bad results for Facebook, Spotify and PayPal. Not sure of the pattern. Clearly, the iOS privacy change on cross-app tracking hurt Facebook to the benefit of Google.

Lots of Washington conversation about forgiving student debt. College students can borrow cheaply from the federal government to attend school (Stafford loans). There is no underwriting --- so credit worthiness does not matter --- if you are a student at an accredited school you can borrow the money. Unfortunately, many of these borrowers are not paying back their debt. Payments have been "on hold" due to Covid but even before that as many as 50% of borrowers were not making any principal payments. In a case of Washington "gimmickry," the government keeps the loans on the balance sheet at full value assuming it will get paid back (student debt does not get wiped out in

bankruptcy). Since the government can borrow money so cheaply, under its' accounting, it is making tons of money on student loans and it is a "pay for" in Washington speak. Unfortunately, that is all hocus pocus. The loans are not getting repaid and now the political momentum is to forgive them. This isn't great for the taxpayers who have put up the money which is being lent out. It also sets terrible precedent on "not paying your debts" for our young people IMO. Student debt is a problem that has broader ramifications like delaying household formation but let us focus on modifications rather than just straight forgiveness.

Nomenclature example: heard someone change the nomenclature from "non-profit" and "for-profit" to "tax exempt" and "investor owned."

Good opinion piece in WSJ: [end-covid-panic-now](#). *"The seemingly unto-eternity extension of the Covid crisis is now doing more nonmedical damage to the country than the virus itself. Masking and testing have turned life into a Rubik's Cube of detail and wheel-spinning decisions. Isolation has become its own pandemic. Untended friendships have eroded."*

Some interesting commentary on return to office from Joe Brady: *"The world is no longer binary (home/work; work/home). The tectonic shift caused by Covid-19 changed "Work" from a noun to a verb. From a place we went, to a thing we do, irrespective of place. Workers are now consumers. They will act with agency, autonomy and optionality. They will choose to earn their money the same way they spend it. Retail (spending money) moved from centralized to decentralized (think rise of Amazon). Omni-channel retail became do or die. Shop morphed from a place we went, to a thing we do...Hybrid working is the equivalent of multi-channel retail. We, as consumers, like having choice and optionality. Now with this tectonic shift, we can earn out money the same way we spend it. So... saying "return to the office" is tone-deaf to the real and complex wants and desires of the professional working population. No one knows what the next normal will bring. But, if we remain curious, empathetic and apply an anthropological examination regarding the change in human behavior, we will better understand how to make the built environment (i.e. \$4T office asset class) more agile to run at the speed of business. The future will be more quantum (existing in multiple states / places in the same day) than digital (home/work, work/home)."*

Demographic tailwinds and more flexible work-from-home arrangements are supporting housing demand. The large millennial cohort is starting to buy homes at a rapid rate. Homeownership could become more attractive with a shift to more work-from-home arrangements. Technology like ride-sharing and food delivery apps could make living in the suburbs more convenient. Housing demand could exceed supply for years as the pace of new construction has recovered slowly since the housing crisis, resulting in a shortage of homes. Some millennials are "flipping the script" by buying vacation home first and still renting primary residence. [vacation-house-starter-home-trend](#). In a sign of the robust market, according to Redfin, almost two-thirds of home buyers made an offer without seeing a house in person in 2020. Cash offers are way up (although that is a misnomer because all offers are cash. The question is the source of cash and whether they are all equity offers vs depending on mortgages).

Beware of the new IRS rule which just went into effect. They are making Venmo and PayPal report commercial transactions over \$600 annually so they can issue a 1099 to the recipient. Washington could come after your babysitter. <https://www.nbcnews.com/news/amp/rcna11260>.

Count me out on hiring in NYC. Under a new local regulation, companies must include salaries in job

opening advertisements. The policy argument is that “transparency” will reduce the reported discrepancies in pay based on gender and race. I view salaries as a private matter and an employee doesn’t need to know what all other employees are making. If someone feels discrimination is occurring, sue the company and get the data and make the case. In the meantime, I encourage employers just to put in their remote work advertisements that residents of New York City are not eligible.

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