

J. Michael Locke

Musings

#253: Musing **February 24, 2024**

Not a lot of my thinking in today's musing. More of me curating good thinking by others. Hope you enjoy.

Are higher interest rates going to change valuation metrics in the private markets? They certainly are changing managerial approaches. Historically, the public equity market focused on the bottom line earnings of a business after all expenses and trade at multiples of those earnings (PE ratios). Private markets have historically traded on EBITDA (earnings before interest, taxes, depreciation and amortization) which more closely resembled cash flow. The problem is the “I”. The dramatic rise in interest rates means lots of cash going out in payments to the lender. Management teams need to focus on bottom line cash flows inclusive of payments in interest and taxes. As folks watch their cash more closely, watch for contagion. Stretching of payables can have its own virality and economic growth may suffer. (Thoughts from Ed Lhee)

One odd dynamic in our markets is how losing money becomes an asset through the tax loss carry forward or NOL. The basic construct is losses in the past get to offset income in the future and reduce the tax liability. As such, the “future tax shield” from the losses becomes an asset. A business that has lost a bunch of money is still worth something because a profitable acquirer could take it over and get the tax savings. A related dynamics exists in the differences between marginal income tax rates and capital gains in the fixed income world right now. Rising rates have crushed bond prices and funds are sitting on lots of losses on their holdings. These losses on bonds means a lot of any price appreciation going forward will get capital gains treatment. This makes some bond funds a good investment for taxable investors as you can buy in now and benefit from these losses even though you weren’t an owner when they occurred. Thanks Jim Kelly.

Our cellular dependency was on full display Thursday morning with the big AT&T outage. I couldn’t pay my cab and struggled to get my boarding pass for security. Good reminder to have some backup plans (we actually still have a home phone).

Welcome to the new world. One CRM (customer relationship management) software provider that leverages AI uses this tagline: “secure, hallucination free, LLM agnostic, and IP liability free.”

Employee reviews are a waste in most organizations. I am a big believer in constant feedback and coaching. Don’t complain about someone behind their back unless you have directly given them the feedback. Too many people are conflict adverse and don’t provide constructive feedback and recommendations for improvement. The managers job is to grow their people and not just evaluate them.

Great piece on education institutions and how they play a role in our mental health crisis by Doug

Smith. The full piece is after my initials at end. Doug cites an Atlantic article by David Brooks with is quote I like: *"We inhabit a society in which people are no longer trained in how to treat others with kindness and consideration. In a healthy society a web of institutions – families, schools, religious groups, community organizations and workplaces – helps form people into kind and responsible citizens, the sort of people who show up for one another. We live in a society that is terrible at moral formation."*

Good stuff from Matt Sigelman at Burning Glass. His firm published a big study showing how many college grads are underemployed and the difference internships can make. From Matt *"52% of graduates land into a job that they didn't need to go to college to get, even in a red-hot job market. Worse: few who start out underemployed ever make it to jobs that require their degree, bearing a \$20,000 per year earnings gap vs. their classmates that persists throughout their careers. This underside to American higher education highlights the urgent imperative of bringing new focus to how students fare after college. It's not that college degrees aren't valuable. It's that they are valuable to too few. With 38 percent of students failing to complete their degrees within six years and then 52 percent of those who do graduate finding themselves underemployed, less than 30 percent of those who enroll in college realize the benefit they looked forward to.....Some programs of study have less than a third the risk of others. For example, 23 percent of nursing students are underemployed five years after graduation vs. 68 percent of criminal justice majors – but that still means that a quarter of students in one of the lowest risk fields fails to find college-level work. Having an internship reduces the prevalence of underemployment by almost half. Going back to school to get a graduate degree also helps considerably – but there to, it's no guarantee, with a third of non-quantitative business master's degree holders struggling with underemployment."*

Amazing stat: 17% of all public-school primary and secondary students are classified as needing special needs (WSJ).

Scott Galloway calls AI the "Corporate Ozempic." Ozempic is a GLP-1 drug which reduces your appetite just like AI can reduce your labor need. "If you want to understand how AI is reshaping business, picture it as the other massive innovation of our time: GLP-1 drugs. Both shed weight by suppressing cravings; both exacerbate existing inequities (aka the rich get richer) before generating wider prosperity; and both are having a greater impact than projected as early adopters are hesitant to admit they're using." Galloway's thesis is that AI is going to let companies operate with fewer employees and a lower cost structure. It might just enhance productivity vs replacing person. "The media portrays the impact of AI as a one-for-one proposition — Mary the copywriter losing her job to ChatGPT. But that's not how AI is trimming corporate America. Instead, it's picking off individual tasks and augmenting teams with more capabilities. Goldman Sachs estimates that AI could perform about one-fourth of the work done by humans today, but that two-thirds of jobs are exposed to some degree of AI automation. That automation is taking many different forms. UPS is using AI to determine pricing for contract proposals. Allstate's AI is developing internal training programs, doing in a day what once took three weeks.

Jobs are being lost, but augmentation will be the broader story. Rather than copywriter Mary losing her job, Mary's firm will train her on an AI tool that generates first drafts, takes approved product copy and converts it for catalog, web, and social use, and streamlines other tasks. Accordingly, Mary's manager will expect her to generate three times the copy in the same time.

Managers can take on new initiatives and domains without the headache of hiring more humans. It's growth without calories. I've founded two strategy firms (Prophet and L2) and loved everything about them, except for the clients and the employees — every additional hire creates complexity and thus

increases risk. The AI revolution will inspire a golden age of startups with lower infant mortality, as there will be fewer people (i.e., less risk) required to get to sustainability.”

Any reader of these musings knows I don’t like Donald Trump. However, the New York judgment is out of bounds IMO. The lender did not raise fraud, was fully paid and says they would do the deal again. No victim or harm to anyone yet the State says Trump must pay \$350mm and can’t operate in New York? Take your business to better states like Texas, North Carolina; Tennessee or Florida. This was political.

Jml

From Douglas A. Smith

There is a mental health crisis happening across America, and it is most pronounced and disturbing among our youth. Suicide rates, anxiety, depression, loneliness, bullying and anti-social behavior among children are at unforeseen levels. Today between 20-25% of the population will experience depression before concluding adolescence. In the last 10 years the suicide rate among ages 10-14 – let that sink in, 10-14 – has tripled, and among girls, quadrupled. (Source: Generations, Jean Twenge).

I believe our educational institutions are a key resource in addressing this crisis, but to do so will require a major change in how these institutions see their role and a change in their pedagogy.

What is Causing This Youth Mental Health Crisis?

Sure, technology, particularly cell phones, plays a role. The deterioration in youth wellbeing accelerated, suddenly and dramatically, in 2012 as cell phone ownership among kids went from a privilege, to a necessity. Technology doesn’t just do things for us, it does things to us.

But I think there is a more prolonged fundamental cause: The lack of what David Brooks calls a “web of institutions” providing a moral framework for our youth. This from his recent Atlantic Magazine article “How America Got Mean:”

“We inhabit a society in which people are no longer trained in how to treat others with kindness and consideration. In a healthy society a web of institutions – families, schools, religious groups, community organizations and workplaces – helps form people into kind and responsible citizens, the sort of people who show up for one another. We live in a society that is terrible at moral formation.”

Without this moral foundation, many of our youth live in a bewildering world, without clear expectations, guidance, without structure, without having an understanding of what it means and requires to live successfully.

The Historical Role of Educational Institutions

Until the middle of the last century, universities and public schools saw their role as enabling both academic success as well as moral and civic development. Here is how Donald Harward of Harvard University describes the very foundation of our liberal arts institutions.

“There has been, and remains, a ‘triad’ of interrelated core purposes of liberal education: the epistemic (coming to know, discovery and advancing of knowledge and understanding); eudemonic (the fuller realization of the learner, the actualizing of the person’s potential – classically, to achieve individual well-being and happiness); and the civic (the understanding that learning puts the learner in relation to what is other, to community and diversity, in the broadest sense, as well as the responsibility that comes from sustaining the community and the civic qualities that make both open inquiry and self-realization possible.”

As just one example, founded in 1831, Denison University’s mission is “to inspire and educate our students to become autonomous thinkers, discerning moral agents and active citizens of a democratic society.” Clearly Denison’s mission goes well beyond the epistemic or academic purpose.

This triad of core purposes was not confined to higher education. I have my great grandfather’s McGuffey’s Fifth Eclectic Reader, published in 1866. A quick review of it shows that most every lesson in it had some moral or civic lesson.

But starting in the middle of the 1900’s schools began abandoning their role in moral and civic development. Why? Because most all of the moral and civic education was wrapped up in religion, specifically Christian religion ... witness the McGuffey’s Reader. Given the diversity of our society and the desire to reach everyone, such abandonment is understandable, and within our public schools, essential.

Reconsidering the Role of Our Educational Institutions

But I don’t think religion has a lock on morality or on living responsibly to the common good. Religion is just one way to teach or live these virtues. We can help students develop a moral and civic framework for their lives without treading into religion. Kindness, forgiveness, gratitude, consideration for others, love ... aren’t these concepts universal and aren’t they essential to not only the success of the individual, but to the success of a society as well? These, what might be called wellbeing skills, like the skill of math or history or basketball can be taught.

And here is the really exciting part ... we are finding that when students learn and practice wellbeing skills, their ability to focus, to concentrate, to perform academically is significantly improved. It is no secret that when students are anxious, depressed, lonely, they struggle to focus on their academics. Teaching wellbeing skills and teaching numeracy and literacy are incredibly synergistic.

Positive Psychologists have been working to identify a universal code of wellbeing skills. They looked for virtues and character strengths that were respected across all cultures and across time. In 2006, under the leadership of Martin Seligman and Christopher Peterson, the Handbook of Character Strengths and Virtues was published identifying 24 character strengths, categorized within 6 virtues. The character strengths include bravery, integrity, persistence, love, kindness, citizenship, gratitude, among others.

These character strengths and virtues are playing a foundational role in the emerging field of Positive Education which seeks to combine academic skills and skills that foster wellbeing, all designed to enable students to “flourish.” Here is how Felicia Huppert, a leading positive psychologist, defines flourishing:

“Flourishing is a combination of feeling good and functioning effectively. It is synonymous with a high level of mental wellbeing and it epitomizes mental health.”

Isn't flourishing what we want for our youth ... for ourselves? Yes, to flourish we need a foundation of literacy and numeracy, but don't we also need good relationships, meaning, kindness, to care for one another, to be resilient?

Positive Education is mapping out curricula that combines academic and wellbeing skills. Some countries, particularly Australia, are well ahead of America in pursuing this. They are finding that when students experience education focused on wellbeing and academics, they outperform those who have just academic training, doing 11% better academically. Where wellbeing education has been effectively put into Australian public schools, students are 6 months ahead of others on their NETPLAN, their national testing standard.

Education should be an outgrowth of the society within which it exist. I think the dramatic challenges in student wellbeing cries out for us to reconsider the role and pedagogy of our educational institutions. I believe positive educators are showing us exactly how to do this.

I hope you found this of interest. If you have any thoughts, please share them.

Be well ... better yet flourish.