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# Something to Think About

OAKWORTH CAPITAL BANK

COMMON CENTS

Over the holidays, I watched the Will Ferrell movie "Elf" on two occasions. Although I don't normally like that sort of silly/slapstick humor, there is enough of a story there to make it work. All told, I suppose I have seen the stupid thing a couple dozen times.

One scene that always cracks me up occurs the morning after Buddy the Elf has stayed up all night decorating the toy department in anticipation of Santa's visit to the store. It is truly a wonderland. The department manager storms up to Buddy and the Jovie character and says:

> "Hey, guys. Have you seen the place? Mm-hmm. It's pretty good. It's a little too good. Corporate must have sent in a professional. I don't know why some body's gunning' for my job, but, look, let's remain team, okay? 'Cause if I go, we all go. If you get wind of anything, Call me on my radio, Channel 3. Code word is "Santa's got a brand new bag, okay?"

Where could I possibly be going with this?

Well, this morning, the Bureau of Labor Statistics (BLS) released the Employment Situation report for December 2015, and it was pretty good. It was a little too good. The BLS must have sent in a professional to cook up the data. It took me quite a while to find anything really negative about the release, but I finally did. I was inclined to do so, and wasn't going to stop trying until I found something, anything.

What I found was a lot of jobs in a lower paying industries, and I won't bore you with the breakdown. According to table B-3 in the report, average hourly earnings fell by a penny, and average weekly earnings slumped 35¢. While that isn't necessarily worrisome in and of itself, and one month doesn't a trend make, the 2.2% year over year change in weekly earnings probably isn't enough to propel a consumer driven economy into the stratosphere.

Admittedly, it is much better than a sharp stick in the eye, and better than the official rate of inflation. This means the US consumer's purchasing power actually increased in 2015, thanks largely to a severe slump in energy prices. However, it likely isn't enough to get GDP growth to 3% or more without an improvement in the trade deficit and/or an increase in government purchases. Given the strength of the US dollar relative to other major trading currencies and the persistent Federal budget deficit, neither seems highly likely in 2016.

As a result, nothing has really changed, other than perhaps a Federal Reserve official or two might have a bruise on their back from patting it so hard. To that end, and unfortunately, these types of reports give the Federal Reserve the ammunition it needs to raise rates, but don't really suggest an economy in dire need of a tight monetary policy. It is almost like when the mayor and entire city council, of any city, show up at the ribbon cutting of a burger joint situated next to a shuttered factory and then have the temerity to bloviate about economic development.

Perhaps that is the reason why the markets haven't been able to hold onto this morning's early gains, as I type. While the report was good, it was perhaps a little too good, leaving the door open for the Fed to tighten in the face of global uncertainty, I hate that word, and what proves to be

***Inside this issue:***



**Innumerable confusions and a feeling of despair invariably emerge in periods of great technological and cultural transition.**

**Marshall McLuhan**

## Something to Think About Cont.

more of the same for the US economy. In that regard, I suppose you could say the report wasn't really all that good after all.

Further, I am inclined to believe the monthly jobs numbers are currently masking a longer-term problem for unskilled and semi-skilled labor in the United States. Looking into the proverbial crystal ball makes me uneasy for these types of workers. Recent advancements in technology seem to be increasing efficiencies at a far greater pace than creating the need for additional capacity. This will lead to what human resource departments and consultants call redundancies. Everyone else calls them job cuts, at worst, or attrition in the probable case.

Take the ride sharing service Uber as an example. Part time folks looking to make a buck or two drive paying customers around, and Uber generates a form 1099 for their troubles. At first blush, the kneejerk reaction might be: so what? Outside of some major population centers, cab companies aren't really major employers, are they? Well, certainly not in Birmingham, which is why our core city's reticence to allow Uber into the area was so confusing. However, the tentacles are much longer than that.

What does Uber mean for rental car companies and corporate fleets? It isn't just taxi drivers which will feel the pinch from Uber, no. Car manufacturers eventually will as well, let alone all those mechanics which work on rental and corporate cars. Perhaps that is part of the reason why GM said this in its December 2015 sales release:

- During December...deliveries to rental customers declined 14 percent, or 3,300 units, per plan.
- In 2015...rental deliveries were down 11 percent, or nearly 50,000 units, per plan.
- GM expects another significant reduction in rental deliveries during 2016.

Perhaps as a result, 'fleet' sales a percent of total sales fell 2% for GM in 2015 to 22%, and were only 16.7% during December. Trust me, as Uber, and other rideshare services , catch on with consumers, these numbers will continue to fall. Oh, they might not fall through the floor, but they will be enough, at some point, for US auto manufacturers to start really lobbying in Congress.

Then there is the persnickety problem at Disney. While most people might think of Mickey Mouse and theme parks when they think of Disney, the company made more money from its cable networks than it did its 'parks & resorts' segment in 2015. That is a lot of revenue, but there are problems...namely American viewing habits.

Younger people don't watch TV the same way older people do. Nope, it isn't even close. They find content through Netflix and other sources through their devices and smart TVs, greatly reducing the need for a cable contract. All they need is internet access and an app. Trust me, Netflix costs less than cable does, and has no shortage of stuff to watch. So, why pay up with a cable contract to watch, say, Modern Family when it originally appears when you can catch it later using something else? Basically, millennials don't see the need to pay umpteen dollars for hundreds of channels of nothing to watch, when they can pay a fraction and watch exactly what it is they want to see.

For all the talk about millennials being lazy and the like, they are really onto to something here. You can call it what you will, but I call it being a smart consumer.

## Disclosure

## *Something to Think About Cont.*

Of course, we all know about internet shopping, and many of us have heard about Macy's plans to shutter 36 stores and eliminate roughly 4,500 positions in response to slumping sales. To that end, the department store giant saw same store sales fall 4.7% during the important holiday shopping season, this as analysts estimate total retail sales were up close to 7.9%.

However, before anyone thinks traditional retail is completely dead, consider this article from a "retail industry expert," a Barbara Farfan:

> "Looking at the photo gallery of all the Macy's stores closing in 2016 reveals an obvious theme that likely influenced the decision to close these particular 36 retail locations. These Macy's locations that are going out of business for good in 2016 are old.
>
> There is no implication that age and longevity are detrimental to physical retail stores in general.
>
> Legacy is an appealing quality to certain segments of the department store consuming population. But these particular Macy's stores that are closing in the Spring of 2016 look old and tired and in great need of a brick-and-mortar facelift.
>
> From the outside they represent a Macy's of the past, which again is not necessarily completely negative.
>
> **But it's pretty obvious that the 36 Macy's stores that are closing in 20 states don't really have the magnetic aesthetic that can continue to draw new generations of Macy's shoppers through the front doors in the future**. These closing Macy's stores bear little brand resemblance to any of the Macy's flagship stores, or the bright, shiny new Macy's stores opening in 2016.
>
> No doubt the need for renovation investments in these Macy's physical retail locations influenced the decision to permanently close them. **And these days there's not such a worry about eliminating access to Macy's merchandise when the only Macy's store in town goes out of business**."

When you boil everything down, you can come to the following conclusion: changing American behavior due to technological efficiencies is shifting consumption patterns away from the traditional middleman distribution network model to more direction transactions and actual content providers. Those middlemen which succeed will be those who provide some measure of "value add" to the purchasing experience, be it access to unique products and services or lower prices due to economies of scale.

This means there will be enormous amounts of redundancy, particularly in slower growth markets with outdated facilities. When it comes time to upgrade or reinvest in a community, many businesses will opt to shut down and funnel those customers to the company's website or a unit in a more densely populated area. While the most obvious example of this is retail, it spreads across numerous economic sectors. Banks are another great example. Shoot, drive through a sleepy Southern town of 5-10,000 souls, and you can tell the transition is already taking place. It will just start moving upstream.

Now, as for Disney...the company didn't take an ownership stake in Hulu, the streaming media online company, for grins. Neither did NBC or Fox. The end aim for the company, or at least the technology behind it, is to be able to provide content directly to the consumer. As bandwidth increases and cable contracts expire, the major content providers will increasingly shift distribution to their own apps/websites, etc. So, instead of paying the cable company, say, $100 for access to umpteen channels, the consumer will be able to pay Disney, let's say, $20/month for all Disney generated content: ABC (and all the affiliates), History Channel (and all the offshoots), A+E (again, and all the associated channels), Disney channels (of course), formerly direct to DVD Disney movies, and, most importantly ESPN (and its myriad of companies/channels/networks).

But do the numbers work? Well, consider ESPN currently has something like 92 million subscribers, and Disney made $16.6 billion in its cable network division in fiscal year 2015. So, 20 * 12 * 92,000,000 = $22.1 billion. Oh yeah, don't forget the advertising. Within 5 years, this will be the way it is. Major content providers will have their own distribu-

# *Something to Think About Cont.*

tion system, and enterprising companies will bundle smaller ones into theirs. Look for the Big 4 networks to start buying local affiliates and arm twisting the FCC in order to broadcast all of its programming over the air.

I could go on and on, but I will spare you. Suffice to say, even after the whopper of a recession we had, the US economy still has a lot of redundancy in it. The problem is it is still more expensive to write down the excess capacity than it is to keep it limping along. As those properties and outlets age out, look for companies to close them. Laughingly, by the time my grandchildren are my age, it will probably be pretty hard to find a non-descript office building or retail outlet built in the 1970s and/or 1980s in the United States. They will be empty if you do, and the new facilities will be bright, gleaming, and attractive to a new breed of consumer who is more comfortable shopping or banking, etc., from their living room.

All of this is alternatively scary and exhilarating. It is the latter due to the fact the array of apps, shows, and other content available will be nothing short of awesome. My goodness, it is exciting to think about. Conversely, not everyone is bright enough to develop apps, shows, and other content, and the need for a middleman will be greatly diminished thanks to technological efficiencies, as I hope I have established.

You know, maybe this is further along than anyone has thought. Maybe that is the reason why the US economy created 36.9K jobs in restaurants & bars in December 2015. Maybe it is why it created another 59.3K in 'administrative & waste services.' Perhaps it examples the 15.1K in couriers & messengers (which is a seasonally adjusted number). Could be this economic transition helped create another 13.2K positions in 'social assistance.' Hmm.

If so, perhaps it helps explain why department stores employed about 33K fewer people this past December compared to the previous one; commercial banks had about 16K fewer on staff, and 'rental & leasing services' have seen their payrolls decline around 1% over the last 12 months.

In the end, this morning's payroll report was pretty good. It was a little too good, because it masks what is a painful economic transition for a huge chunk of our workforce.