thoughts

FROM HANSON+DOREMUS JULY 2021

A quarter century on...any words of wisdom?

We have been writing this newsletter for 25 years now. We are not market forecasters. We don't try to tell you when to buy or when to sell. We are long-term investors, almost always fully invested. We help clients decide on an appropriate level of risk, stocks versus bonds versus cash, and then we stick with this through thick and thin. We help clients stay patient.

The purpose of the newsletter is to bring you each month interesting perspectives on the market, the economy, and the world. In over 300 issues there are some themes that keep recurring. Some have played out but some, like these three examples, have not:

An increase in inflation and interest rates is right around the corner. This has been the most common worry we have written about since 1995. But it hasn't happened (*see chart below*). Why? Maybe the reason is globalization, or the decline in unions, or the rise of online shopping. Will we see a reversal now? We don't know. Some things that are logical and seem "certain" to happen just don't, or at least take a lot longer than expected.

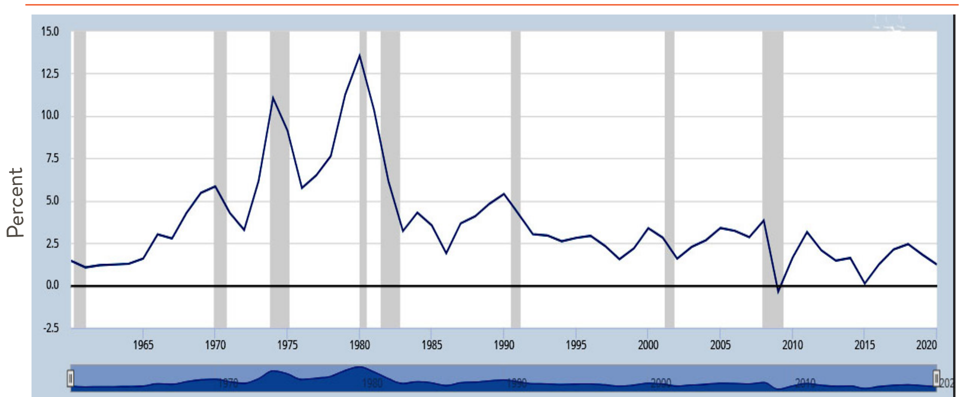
Emerging markets are the future. We thought the original BRICs (Brazil, Russia, India and China) and the fast charging countries behind them (South Africa, Turkey, Indonesia, etc.) would be the future engines of growth and that investors had better pay attention. Well again, this hasn't played out. Although many emerging economies have had fast growth and most have young populations to fuel future growth, progress has been up and down. What the market got wrong is that sustained economic development depends on effective government, and most emerging economies just don't have this.

Finally, there is China. No country has developed more rapidly the past half century than China. And no country seems to have more critics. Some argue that authoritarian regimes just can't last. Others argue that as the Chinese get wealthier, they will demand more personal freedom. Still others argue that the banking system, controlled by the State, is a house of cards loaded with bad loans. And don't get the critics started on the housing market, which they claim is massively overbuilt and the ultimate Bubble. Despite all this, growth continues.

The one constant in our newsletter the past 25 plus years is that investors are anxious and worried. They were back in 1995, they are today. But you know what? Through all the crises since 1995, the Tech Crash, the Housing Bubble, the Great Recession, etc., the total return for U.S. stocks has averaged 10.4% per year. Our advice: stay long-term and stay patient.

- Eric Hanson

INFLATION, CONSUMER PRICES FOR THE UNITED STATES



Source: fred.stlouisfed.org

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By Julie Won

Forget about success. Try "lying flat."

There's a new movement taking hold among China's 20- and 30-somethings, and it's absolutely antithetical to the way they grew up. Indoctrinated since birth to believe that hard work and intense drive were the only paths forward, they have been competing fiercely all their lives for top university spots, good jobs, and later, the best apartments and consumer trappings of success. But now, more of China's younger generations are thinking about giving up the struggle and latching on to what they call "lying flat" or *tangping*.

The term "lying flat" comes from a blog post by a 31-year-old named Luo Huazhong who decided that the stress and strife of getting ahead weren't worth it. He quit his job, went on a 1300-mile bike ride from Sichuan to Tibet, and discovered he could happily get by on odd jobs and a little bit in savings. His blog described his experiences and included photos of himself literally lying flat – and it went viral this past spring.

Lying flat is about staying unemployed or down-shifting to less stressful work. It is giving up on marriage and rejecting consumerism and social status. It also is the very opposite of the "996" trend that was the last big thing in China's work world. That was short for working intensely from 9 am to 9 pm six days a week -- and summed up the extreme work culture that pervaded many of China's most successful tech companies. "996" eventually inspired a backlash campaign called "996.ICU" – as in "intensive care unit," a reference to the medical crises that over-pressured, stressed out workers were experiencing. (Alibaba founder Jack Ma's response to the uproar was: "In this world, all of us want to be successful . . . How can you achieve the success you want if you don't put in more effort and time than others?")

Chinese state authorities have found lying flat to be alarming, subversive, and threatening. They have scrubbed Luo's blog from the internet, and state-supported media have started publishing articles on the irresponsibility of dropping out. ("The only way to ensure a happy life is if one works hard," *The Economist* recently quoted from one newspaper). The idea of getting by on meager wages, working only several months a year, and living on two modest vegetarian meals a day is not exactly the vision of economic ambition and consumerism that the Communist Party wants to instill.

A Brookings Institution article showed this picture making the rounds on China's internet. A man lying flat asks, "You want me to get up? That's not possible in this lifetime."

"The 'lying flat' movement standing in the way of China's innovation drive," by David Bandurski, July 8, 2021

But recent news articles have interviewed plenty of Chinese in their 20s and 30s who just want to take a six-month break or leave high-paying jobs for less stressful ones. A recurring theme is that even if these young workers went all out and killed themselves to get ahead, they may not get anywhere anyway. The world has changed since their parents' time when hard work really did pay off.

China is not alone either. In South Korea, the term "Hell Joseon" has been appearing since the mid-2010s. Joseon is a historical name for Korea, and the hell for young people is that no matter how hard you work, or how great your grades and resume are, you're in for a hard life of struggle no matter what. Career competition is fierce, housing costs are impossibly high, and raising children is tough. The often-heard Korean term *"sampo,"* or "three-giving-up," refers to the hopelessness of a generation that has had to give up on dating, marriage, and children. That has since been followed up with "five-giving up," which adds jobs and home ownership to the list. Then there has been seven-, nine-, and 10- giving up, all the way to *"wanpo,"* which means totally giving up.

While the U.S. doesn't have the fiercely competitive environment that East Asia does, there is a reassessment of the worth of work here too now. An unprecedented four million Americans quit their jobs in April. That may be a short-term reaction to the pandemic -- and it likely would not be possible without the government stimulus checks people have been able to save up. But there are plenty of stories of people rethinking everything and searching for more meaningful ways to work and live.

The Economist recently wrote that according to Nicholas Christakis of Yale, past pandemics have caused three big shifts: 1) a growth in state power, 2) a search for meaning, and 3) a rise in audacity. We have yet to see how the search for meaning or a willingness to roll the dice will play out in worker preferences. But so far, multiple surveys are showing that over 40% of workers are thinking about quitting soon. Business creation in the U.S. is at its highest since 2004. And it seems, far more people are talking about working to live, rather than living to work.

By Julie Won

Will there be a world without work?

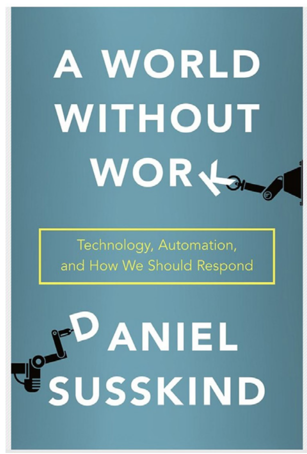
In 1930, the economist John Maynard Keynes wrote a short essay called "Economic Possibilities for our Grandchildren," where he envisioned technological advances enabling us to do all the work of agriculture, mining, and manufacturing with only a quarter of the human effort. Future generations, he said, would work only 15 hours a week. In fact, the challenge would be to share what work there was as widely as possible – or "to spread the bread thin on the butter" – because learning to live with purpose in a world without work would be hard.

Keynes' prediction has not yet come to pass, if it ever will, but the idea of machines taking over human work has long held fascination and dread. So far, technology has created more work for humans, not less -- new jobs and new opportunities, even if there were difficult dislocations for some. Still, the threat of technology robbing us of our livelihood has been with us a long time -- at least since angry weavers destroyed the newly invented flying shuttle in the 1730s and mobs attacked the first factories with the spinning jenny in the early Industrial Revolution.

The Economist did a series of articles this past spring full of optimism for the world of work, including one titled "Robots threaten jobs less than fearmongers claim." Doomsaying about machines, it said, has long been with us, but the labor apocalypse hasn't happened and probably won't. One reason is the "lump-of-labor fallacy" – the flawed idea that there is only a finite amount of work and that more automation necessarily means less work for humans. That has not been true. Instead, automation has made humans more productive by freeing them for new kinds of work.

A classic example is the bank ATM. While the number of ATMs quadrupled between the 1980s and 2010, bank tellers did not disappear. The number of tellers over that period actually rose because tellers were freed from dispensing cash and could offer face-to-face services that improved business.

Still, there is a credible case to be made for a world of much less work in the future, and it's made very well in Daniel Susskind's 2020 book *A World Without Work*. Susskind



Metropolitan Books, January 2020

fully acknowledges that technological innovation creates new, previously unimaginable jobs. What people aren't realizing, however, is that there is no reason to think humans will be better suited for these new jobs than machines. Machines are getting better and better, and we may be underestimating their capabilities.

Our traditional answer to automation has been to "upskill" – to retrain workers for higher-level work so that they can stay ahead of machines. The idea is to teach factory workers engineering skills, for example, and keep them moving up the ladder. But that's a very 20th century idea that doesn't acknowledge how good machines are getting. Being a lawyer or radiologist may be no safer than working on an assembly line.

Take the incredible progress artificial intelligence (AI) made between IBM's Deep Blue beating chess champion Garry Kasparov in 1997 and Deepmind's AlphaGo (now owned by Google) beating the world's best Go player Lee Sedol in 2016. Go is a Chinese board game that is much more complex than chess. After just three moves by each player in Go, there are 230 million times more possible moves than in chess at the same point. Deep Blue learned to play chess through brute-force processing power so it could think ahead of Kasparov. But Go is too complicated for that. To learn to win against the best humans, AlphaGo first studied 30 million moves by top human players, then kept playing against itself. In 2017, the improved "AlphaGo Zero" didn't even need to look at human play. It just learned the rules of the game, and in three days it generated enough of its own data to be able to completely destroy its predecessor AlphaGo.

Of course, we don't know what the future holds. But it seems wise to start considering AI's considerable and rising abilities to do high-level analysis, create art, and write music. Ironically, the jobs that stick in the future might be lower-paying ones that machines can do, but where human interaction still is valued – barbers, for example, or caregivers for seniors.

The implications of all this are enormous. For one thing, we will need a radical rethink of education. Really, why spend so much time teaching students to solve progressively harder math problems when they'll never beat machines? And even more radically, we will need a totally new way to distribute wealth. Up to now, work and wages have been our primary means of distributing the economic pie. That is what "making a living" has meant. But how will we do things in a world without work, or at least much less of it?

ECONOMIC TRENDS

By Anne W. Doremus

The Case for Rising Productivity in the U.S.

For most of the past 15 years, the U.S. has suffered from a productivity problem. Except for a spike after the 2009 Financial Crisis, productivity gains have been stuck at 1% per year over the past decade, or half the long-term average. Why does this matter? Economies that produce more with the same number of workers grow faster, and that faster growth supports higher wages.

Theories of the cause of this poor performance have varied. Some economists have suggested that we are simply not measuring productivity correctly. How, they claim, do you account for improvements imparted by services like Google Maps or Waze? Others suggest that we have simply become less innovative and that the advances of today (consider streaming services) compare poorly to the productivity enhancing leaps of yesterday like electricity and the internal combustion engine. Whatever the answer, the good news is that recent data shows a significant improvement in our nation's results with first quarter productivity rising at a 5.4% annual rate – a full 4.1% above year-earlier levels.

As the chart below shows, it is not unusual for economies to experience rising productivity coming out of a recession. The reason here is intuitive; early in a recovery employment gains tend to lag the actual pick-up in demand as businesses make sure the turnaround is real and hire and train new workers. That certainly appears to be the case today.

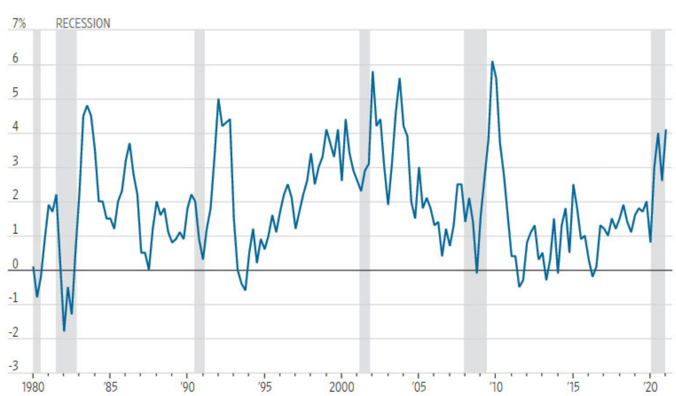
There are several reasons, however, that suggest the most recent productivity gains may be more sustained in nature. First, the pandemic forced many businesses to figure out how to produce more with fewer workers (think telehealth and electronic menus). Some of these "innovations" will fade but many will continue to spread across the economy.

Second, the unprecedented level of fiscal and monetary stimulus together with the nation's slow-growing work force could mean that businesses continue to have trouble hiring to keep up with demand. In a recent study, the Pew Research Center projected that the total growth of the labor force over the next 20 years will be lower than the total growth in any *single* decade since 1960. Many businesses, faced with a shortage of workers and related rising wages, will turn to productivity enhancing technology and process related improvements to control costs.

Finally, consider the shifting global economic landscape. For most of the past 50 years, the U.S. played a leading role in the global economy. Investments in everything from the federal highway system to technology and healthcare helped it sustain this lead. But the tremendous economic advances in countries such as China together with lagging investments here at home mean that the U.S. can no longer live off its past successes to stay on top. The current administration's effort to bolster key industries such as semiconductor manufacturing suggests a shift toward more focused industrial policies aimed at retaining our economic sovereignty. Whether this approach proves successful over time remains to be seen. In the meantime, investments into key sectors of the economy and basic R&D may well translate into productivity improvements going forward.

NONFARM BUSINESS PRODUCTIVITY

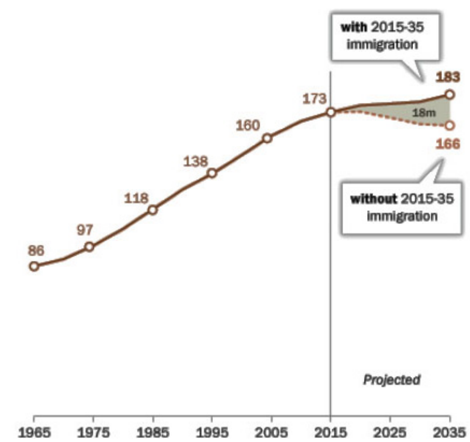
Change from quarter one year earllier:



Sources: *The Wall Street Journal*; Labor Department via St. Louis Fed

WITHOUT FUTURE IMMIGRANTS, WORKING-AGE POPULATION IN U.S. WOULD DECREASE BY 2035

Working-age population (25-64), in millions



Note: Numbers for 2015 onward are projections. Source: Pew Research Center estimates for 1965 - 2015 based on adjusted census data; Pew Research Center projections for 2015-2035.