thoughts

FROM HANSON+DOREMUS **MARCH 2023**

HANSON+DOREMUS
INVESTMENTS AND PLANNING

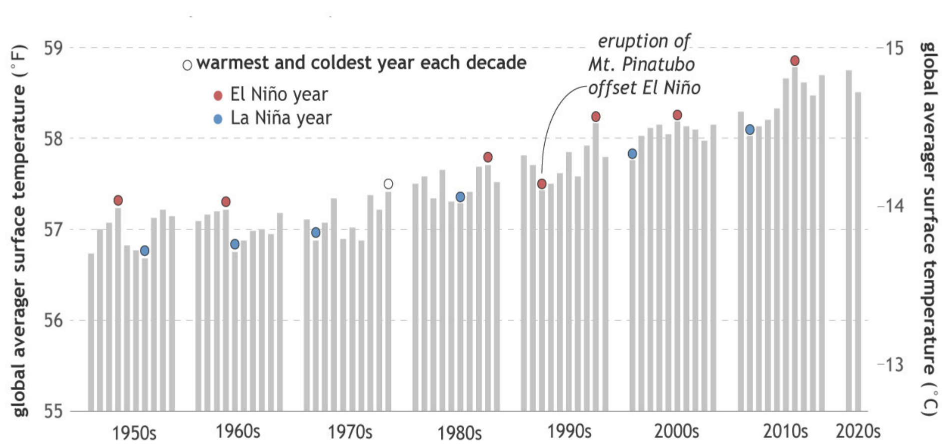
Snippets of news worthy of mention...

Word of the year in 2022. *The Economist* recently reviewed candidates for 2022's word of the year. The Ukraine war introduced us to newfangled terms like "MANPADS," "HIMARS," and "Loitering Munitions." In grocery stores we have to deal with "Shrinkflation" (the same price but a shrunk product--think candy bars). Facebook (sorry, forgot the new name is Meta) activated the "Metaverse," but nobody, including Meta employees, seems to know what it is or how to use it. The Oxford Dictionary awarded word of the year to "Goblin Mode" (huh?). Apparently, this is where consumers, exhausted by Covid, indulge their most selfish habits. *The Economist* choice for word of the year is "Hybrid Work." I like this; my choice too.

The traffice jam of the future - space.

Here in the northeast corner of Vermont the internet is slow. Fiber to the home is always "three to five years" away. We rolled the dice and opted for Elon Musk's newfangled satellite service, Starlink. It arrives with no lengthy instruction manual, just an app that helps you find the best signal on your property. Then plug it in and voila, fast internet. Since 2019 Starlink has put up 3,500 mini satellites, or about half of all active satellites in the sky today. And it is planning on eventually having 40,000 aloft. Other companies are working on their own systems. As a non-tech person my dumb question is, I like the product, but can the sky really handle all these satellites? Might we end up with satellites crashing into satellites, a giant space version of bumper cars?

GLOBAL SURFACE TEMPERATURE EACH YEAR SINCE THE 1950S



Source: *Adirondack*, Spring 2023; NOAA Climate.gov; Data: NCEI, CPC

The death of cash?

The Wall Street Journal recently reported that cash and checks now total only 14% of total payments in the economy versus 42% in 2010. Covid jumpstarted a surge in online shopping, and banks are starting to remove many ATMs due to crime. Cash is not going to go away. It is still the method of choice for purchases of $25 or less, but it is not hard to imagine many merchants wishing they could just ditch the hassle of the cash drawer entirely.

And finally - climate change.

The chart here is a good visual of the warming planet. Some of us enjoy the winter months (well, maybe not mud season) and the activities the cold brings -- downhill and cross country skiing, snow shoeing, ice fishing, etc. But winters here in the north are not what they used to be. A lot more thawing now and a lot less snow. It's sad.

- Eric Hanson

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WORKERS

By Julie Won

Will we ever have enough again?...

Worker shortages are a problem. Everywhere. You know it if you've been looking to hire – or trying to see a doctor, renovate a kitchen, or pick up your burger and fries. Everything is harder and takes longer when the help is not there. Whether it's railroad workers or accountants, there just are not enough of them.

January data from the Bureau of Labor Statistics (BLS) showed over 11 million job openings but only 5.7 million unemployed -- and the shortages are widespread. We know there aren't enough nurses, teachers, retail workers, or childcare providers. But what about plumbers? The National Association of Home Builders says we need 55% more. And doctors? The Association of American Medical Colleges sees a deficit of anywhere between 37,000 and 124,000 U.S. doctors in the next decade, a looming public health crisis.

The early pandemic narrative was that workers were quitting in droves because they were burnt out, fed up, and flush with savings. But Covid is receding now, and there seems to be something deeper and longer-lasting at work. Last January, IBM CEO Arvind Krishna said, ". . . I don't believe that the skill shortage is because of Covid. I do believe Covid may have exacerbated or created a pull-in of those demographics, but those, I think, are going to last us for a decade." And he may be right. Certainly, demographics are working against us. And certainly, we have some long-run skills deficits that Covid highlighted or accelerated through economic dislocation.

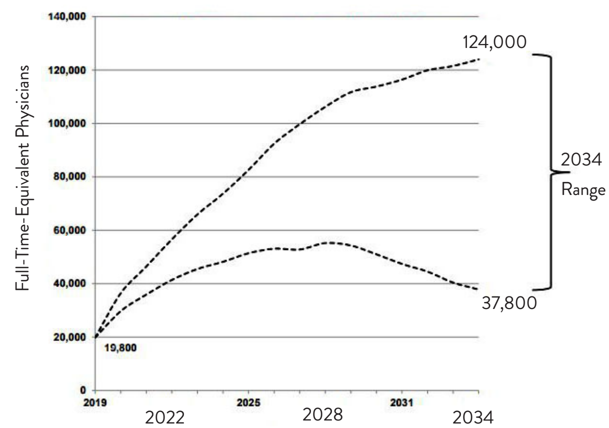
Burnout, demographics, and skills deficits sometimes combine in spectacular ways. Going back to doctors, the Association of American Medical Colleges says almost 30,000 new doctors completed their education and entered the workforce the last year, but 117,000 doctors retired – and some below traditional retirement age were exhausted from the pandemic. About 45% of U.S. doctors are over the age of 55, making for poor demographics. And becoming a doctor takes a long time and is hard, which has many asking if it is too hard and too discouraging.

Those also are questions for the field of accounting and auditing, which isn't everyone's cup of tea, but as Adrian Wooldridge of Bloomberg wrote, "Capitalism can't function without a healthy system of accounting." The number of accountants and auditors fell by 17% between 2019 and 2021, and half the people who take the CPA test each year fail. Plus, with more regulation and things to account for, the job is only getting harder.

We shouldn't lose hope about working our way out of this, but even optimists must speculate that solving labor issues will take a long time. In the shorter term, weak economic conditions could force more people back into the work force, including early retirees. But demographic challenges and skills deficits are long-term issues. All professions are going to have to compete harder for a dwindling pool of people. At the same time, as automation and AI pick up more of the slack, as they surely will, skills requirements will change even more dynamically.

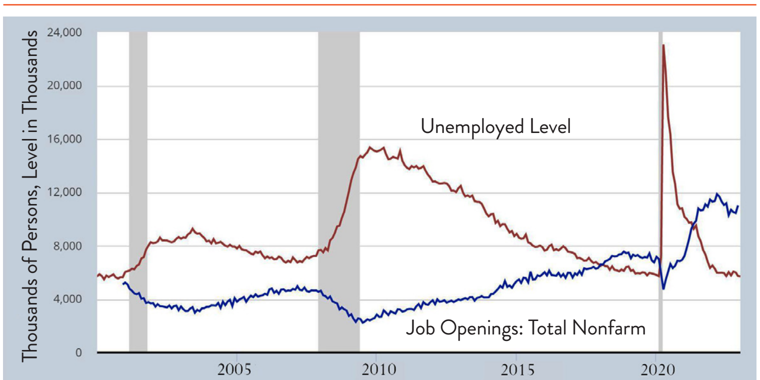
The January BLS data revealed that the two occupational categories with the lowest unemployment rates (at a slim 1.5%) were health practitioners and "computer and mathematical occupations." Yes, despite all those layoffs, techies still are needed. When Peter Coy of *The New York Times* looked into the tech skills most in demand, he read that the number one was MapReduce, "which," he wrote, "I admit I had never heard of." Then he wryly added, "A good way to make yourself feel clueless is to read all the other must-have skills that, unless you're in tech, you probably know nothing about. Here are Nos. 2 through 12: Go/Golang, Elasticsearch, Chef, Apache Kafka, service-oriented architecture, Teradata, Redis, PAAS, Kubernetes, Containers and Amazon Route 53."

TOTAL PROJECTED PHYSICIAN SHORTAGE RANGE, 2019-2034



Source: Association of American Medical Colleges

THERE ARE MORE JOB OPENINGS THAN UNEMPLOYED



Source: *Federal Reserve Bank of St. Louis and U.S. Bureau of Labor Statistics*

THE FEDERAL RESERVE

By Mark Andrews

What's up with the Fed and inflation?

The Federal Reserve is in the news a lot. With inflation running hot, everyone is trying to figure out how high the Fed will raise interest rates. At Hanson + Doremus, we are not trying to guess where rates end up, but we do think it is important to understand the Fed and its thinking around inflation.

The Fed's goals are maximum employment and stable prices, the latter defined as two percent inflation. The Fed's main tool to achieve these objectives is the control of short-term interest rates, especially the "federal funds" rate at which financial institutions borrow from one another. By raising interest rates, the Fed makes borrowing more expensive. The thinking goes that this results in fewer projects and slower hiring, reducing wage growth and the demand for goods and services, and thereby reducing the rate of inflation.

The Fed has now raised interest rates from zero to 4.5 percent with further increases expected (Figure 1). That is well into the territory they believe is restrictive for economic activity and where they expect some impact on inflation. And yet, the latest inflation reading was 5.4 percent, well above the Fed's two percent target. So how does the Fed figure out how deep into restrictive territory to go and how long to stay there? That depends on the impact the Fed thinks it is having on inflation, and therein lies the problem—it's a little like feeling your way in the dark.

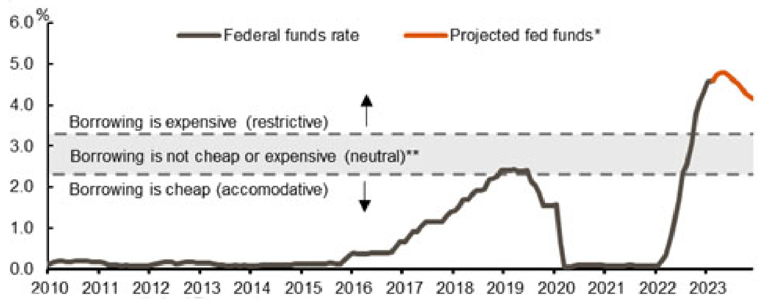
First, the Fed recognizes "long and variable" lags between changes in interest rates and their impact, so the Fed does not get feedback until some unknown future date. Second, the feedback itself is not clear. Inflation data are noisy, and the Fed is currently relying on less than half the prices in the economy, so-called "core non-housing services," for signs of the impact of rate hikes. Finally, the Fed believes psychology plays a role, and psychology can be fickle. The risk is that if people come to expect higher inflation in the future, they will buy more today, pushing prices up even faster. To prevent expectations from taking off, the Fed is inclined to talk and act aggressively.

Looking at Figure 2, it is hard to know yet whether the Fed is succeeding in reducing inflation. Since they began hiking rates last spring, big picture inflation (dark grey) has come down, but their watchpoint inflation number (orange) remains elevated. Longer run inflation expectations (light grey), however, are still around the Fed's two percent goal.

Another dilemma is that by trying to push down inflation, the Fed might cause a recession. The labor market and economy have thus far proven resilient to higher rates, but the Fed needs them to slow down because their strength contributes to inflation. However, continuing to raise rates to get back to two percent inflation could involve slowing growth to the point of recession, or exposing business practices born of the low-rate environment that suffer with higher rates. Right now, presented with the risks of runaway inflation versus slower growth, the Fed has indicated it will side with more rate increases to tamp down price increases. This does not paint an encouraging picture for the chances of a "soft landing."

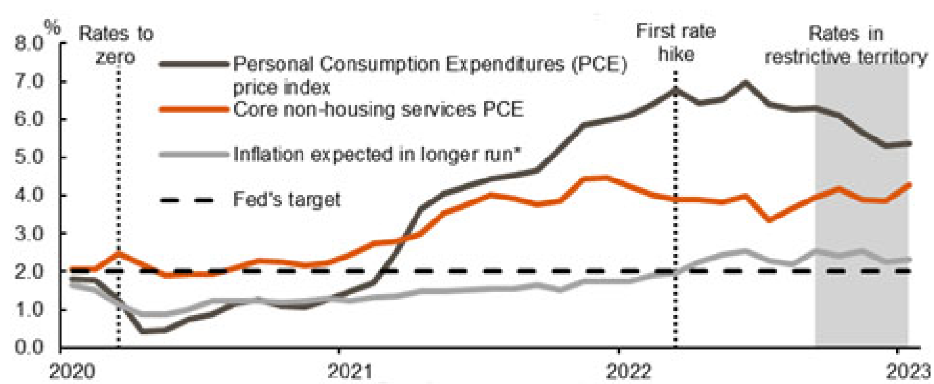
The Fed meets next week and will update their projections for the federal funds rate and inflation over the next several years. What actually ends up happening probably won't follow that script, but these estimates will shed some light on the impact the Fed thinks it is having on inflation and how long they expect to keep rates in restrictive territory.

FIG. 1 THE FEDERAL FUNDS RATE



Source: Bloomberg; Federal Reserve Board *Fed Funds Futures as of 3/13, **Fed estimate of longer run fed funds

FIG. 2 INFLATION AND INFLATION EXPECTATIONS



Source: BEA, FRED; staff calculations; data through Jan. 2023; * Cleveland Fed 5-year expected inflation

THE AMERICAN MOOD TODAY

By Eric Hanson

The state of our (un)happiness...

As if rising inflation, a falling stock market, and the possibility of a recession were not enough, now we are here to talk to you about unhappiness. (Spoiler alert, there is hope and a positive spin at the end).

But first the unhappy part. The Gallup organization has been asking people in many countries over many years how their lives are going. *The chart at the bottom* is from Gallup CEO Jon Clifton's new book, *Blind Spot*. People are getting more unhappy. Some of the most recent increase is due to Covid anxiety, but worldwide unhappiness has been steadily increasing. We don't know exactly why this is but contributing factors include unfulfilling jobs, insufficient finances, unsafe communities, poor health, and the lack of a strong network of family and friends.

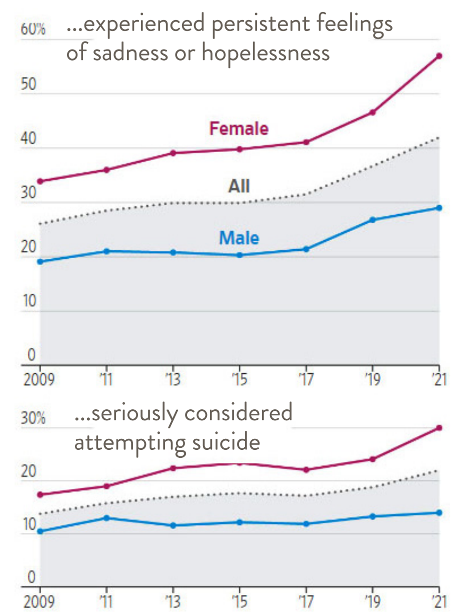
Here in the U.S., one particular group suffering unusual stress is Gen Z, young people born between 1997 and 2012. They are showing an alarming increase in loneliness and sadness. There are many reasons for this but in an interview in *The Wall Street Journal*, Jonathan Haidt of the Stern School of Business at NYU points to one outsize factor: social media. In 2012 Facebook bought Instagram and the "selfie era" took off. Young people, especially girls, post pictures online of their perfect lives only to find even more perfect lives posted by others. It becomes "compare and despair."

The average American according to the WSJ spends 11 hours a day on media, from TV to videos to smartphones. And young people probably spend more than 11 hours a day. We are social creatures, and this time alone breeds loneliness, timidity, and in the case of Gen Z, lifelong negative consequences according to Haidt. This generation will be more fragile, less effective, and less impactful than previous ones. This is a pretty extreme indictment, and it may be that the current state of unhappiness among the young is a passing thing. Boomers survived the drugs and politics of the 60s and 70s, and this generation may also survive their current problems.

Now for the good news. The Harvard Adult Development Study has been tracking for over 85 years the physical and mental changes in a group of 724 Harvard undergraduates and their 1300 male and female descendants. They also added a group of 456 young boys from troubled families in Boston to balance what might be perceived as an Ivy League bias.

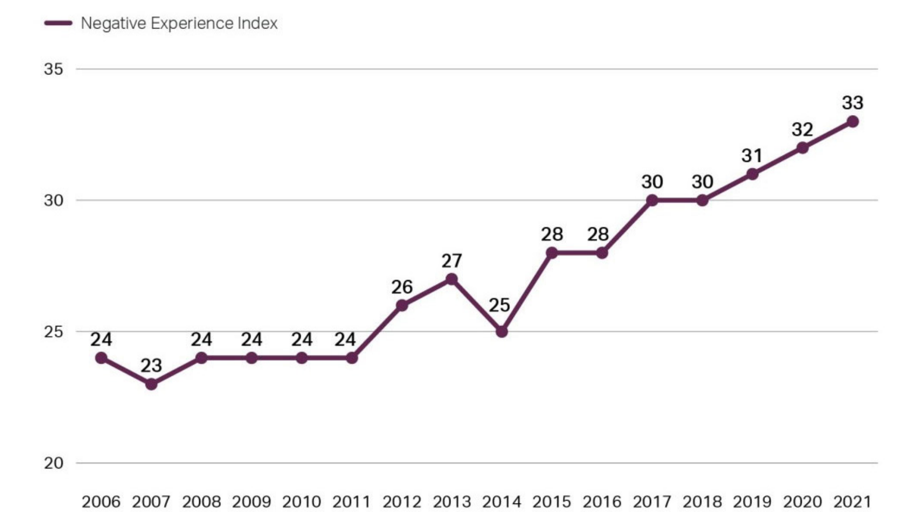
They found that there is one factor that has contributed the most to a longer, healthier life and reduction in loneliness. According to George Vaillant, the head of the Harvard study from 1972-2004, "When the study began, nobody cared about empathy or attachment. But the key to healthy aging is relationships, relationships, relationships." Fame and fortune are certainly nice but the secret to life according to Harvard's nearly century long study is to ditch all the background noise (i.e. your smartphone) and focus on family and friends. It will pay dividends.

PERCENTAGE OF HIGH-SCHOOL STUDENTS IN THE PAST YEAR WHO...



Source: *The Wall Street Journal; Centers for Disease Control and Prevention Youth Risk Behavior Survey*

THE GLOBAL RISE OF UNHAPPINESS



The Negative Experience Index is a composite measure of the five negative experiences (anger, stress, sadness, physical pain, and worry). Index scores range from zero to 100.

Source: *Galllup*