

BUSINESS INTELLIGENCE BRIEF

March 22, 2019



NATIONAL AND INTERNATIONAL NEWS AFFECTING LOCAL BUSINESS

Short Items of Interest – US Economy

- **Employment Data Remains Strong** – By almost any measure the job market has been staying strong. There was another week of reduced jobless claims and that tends to offset the fears regarding the slower than expected job growth reported last week. The job market is still better defined by the shortages that persist than by any large pool of unemployed. The fact is there are more than a million jobs available than there are people to fill them. The issues now are not rooted in a reluctance to hire but the lack of mobility for those seeking work. The biggest issue is that people are trapped in a region where jobs are scarce due to the fact they can't sell their house or they have obligations they can't leave behind. The need to take care of elderly parents is now the single most common reason given for the inability to move.
- **What Does Elite Education Really Get You?** – As the college bribery scandal continues to claim those that engaged in this widespread cheating, there is another question lurking in the background. What does that elite school really deliver? The fact of the matter is that what is learned is basically the same no matter where one goes to school – elite schools don't have different facts than non-elite schools. The presumption is that the instruction is better but research doesn't support that notion. A professor is rewarded for scholarship and publishing and teaching is secondary in most schools – especially the elite ones. The real advantage is the opportunity to rub shoulders with other members of the elite – classmates and professors. Today there is doubt over who one's classmates really are. Did they get here by their merit or did they cheat their way in?
- **Improvement in Multifactor Productivity** – This is essentially a measure of innovation as it looks at whether a company has been able to improve their productivity numbers without added technology or capital investment. This means generating gains through better use of existing technology and management techniques. The latest data shows that this measure went up by 1.0% in the last year and that is the best result seen since 2010. This has been seen as especially good news given the fact that many companies have been hiring people with little experience or formal training in hopes that they can grow into the job.

Short Items of Interest – Global Economy

- **New Zealand's Prime Minister Wins Plaudits** – In the wake of the tragedy that struck a nation with very little experience in this kind of violence, there has been praise for the reaction of Jacinda Ardern. She moved quickly to ban the assault weapons used in the attack, made every effort to reach out to the Muslim community and has worked to strip the fanatics of any notoriety. The Islamic population of the country is very small – less than 1.0% and the majority of these people hail from South Asia (India predominantly). The country is very multi-cultural with the dominant population coming from the UK or from the Pacific Islands and from the indigenous Maori.
- **Recognition of Golan Heights Claims Supported by Trump** – During the Six-Day war the Israeli military seized control of a region called the Golan Heights as it gave the Syrians a military advantage and it has been held as contested territory ever since. The Trump decision to endorse the Israel claim has angered Syria, Turkey and Russia. Not that the US loses any sleep over what these nations think but this is just another poke and provocation that will lead to escalating tension in a region that has more than enough right now.
- **Eurozone Manufacturing Down** – The latest edition of the Purchasing Managers' Index is down to new lows for the entire Eurozone – the lowest level seen in ten years. This reinforces the notion that Europe is sliding towards recession.

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Warning Shot from Services Sector

There are many factors that drive the US economy and one can make the case for a variety of sectors as the real harbinger of things to come. There are those who watch the transportation world closely as hauling freight is often referred to as the “canary in the coal mine”. Others pay attention to sectors that touch the majority of consumers such as the housing market. The Purchasing Managers’ Index and the Credit Managers’ Index are both good early warning systems. Many focus on the sectors that drive the economy and that means consumption as the US GDP is dependent on consumers for over 80% of its growth. The key to using that consumer data is understanding what the consumer buys and why. Most think in terms of buying things and indeed the US consumer does buy an awful lot of stuff. The majority of consumer purchases are services rather than actual items and the service share of the consumer’s wallet has been steadily expanding. It can be argued that service activity is the new reliable barometer of overall economic health and right now there are some signs that things are not quite right.

Analysis: The latest data from the fourth quarter shows a dramatic decline in the amount of spending on services – the worst numbers in the last five quarters. The growth was far more anemic than had been originally forecast – only 1.2%. The original estimate was for growth near 3.5% and perhaps higher. This data is likely to show up in the next revision of GDP data and it will most certainly drag the numbers down. The GDP numbers now stand at 2.6% growth but a revised look at the service sector data is likely to drag that number down to 2.0% or even lower. There have been a wide variety of new estimates coming out and many analysts are revising what they assumed would happen for the total year – even dropping overall growth below the 3.0% mark. That would be a real comedown given the momentum at the start of 2018 and would reinforce the assessment of the tax cuts. They did a good job of boosting the economy but for a very short period – acting more like a “sugar rush” than anything else. It now seems the impact had faded by the third quarter and had been utterly ineffective in the fourth quarter.

The service sector in the US is vast and complex and it is very hard to make a lot of definitive statements about what is happening from one quarter to another. Services include activity in the health care sector, retail sales, construction, financial services, food service and tourism. The list is nearly endless and these sectors very rarely operate in any kind of sync. The estimate for the latter part of last year is that some of these areas continued to do well but others fell behind. Health care was steady and even expanding – something that can be counted upon as the Boomer generation gets older and older. Financial services held steady and even expanded a little as banks and other lenders continue to shrug off the damage of a few years ago. It would appear that the areas that saw the largest declines included retail, food service, tourism, entertainment and the like. In other words, the areas where the consumer is the most active. What makes this more than a little interesting is that conditions should be favoring more consumption rather than less. The job numbers are good and there is evidence that people have more disposable income than they have had in the past. For better or worse the consumer is accessing their credit as actively as they had been a few years ago. Why are sales down then? Part of the answer is frugality and caution as there are more suggestions that people are more nervous about the future than they have been. The last few consumer confidence surveys show that people are pretty happy with the situation they are in right at the moment but they have some real trepidation about what happens by the end of this year and into next. Another issue is that inflation has been showing up in the service sector to a greater extent than in product. It has been noted that inflation has really spiked as far as entertainment and restaurant meals are concerned and as one would expect this price hike has more people electing to spend their money in some other way. One other service sector area that has seen price hikes has been education and here inflation numbers have risen by as much as 200%. The over cost of a degree from a four-year college is now between \$25,000 and \$35,000 per year. That is nearly \$1,000 more annually than it was ten years ago.

Is the Fed’s New Policy Too Risky?

There have long been some basic assumptions about the workings of the Fed. Perhaps the most paramount is the determination on the part of the central bank to “be prepared”. The Fed wants to have the ability to hike rates as fast and as dramatically as needed when they think that inflation has become a real threat and by the same token, they want to have the ability to stimulate the economy meaningfully in the event there is a recession. This generally means that the Fed keeps interest rates reasonably high – it serves to control inflation and gives the Fed the necessary ammunition should there be a downturn.

Analysis: Recent statements from the Fed suggest that they consider the current situation to be the “new normal” and that has some analysts worried. If interest rates this low are now normal how does the Fed expect to deal with emerging inflation threats? Does this mean the Fed plans to tolerate higher levels of inflation before acting? What about their ability to react to a recession? If there was one developing this year or early next what could the Fed really do? Would a small rate reduction mean anything to the business community? Would it really serve to do much stimulation?

The big tax cut of last year had a very limited impact on the course of the economy – at least in the long run. If the Fed doesn’t have much room to cut and Congress is limited in terms of cutting taxes and increasing spending, what is it that can be done to address a recession down the road.

Brexit Extension Solves Nothing at All

The EU has agreed to an extension of the Brexit talks – as if they really had any other choice. The alternative would have been a UK crashing out of the EU in complete chaos and nobody was even close to being prepared for something like that. The problem now is that neither side shows any willingness to change even the smallest previous position so very little is expected from this continued dialogue. The worst-case scenarios seem far more likely than any of the best-case solutions. The future of the May government is nearly set and that will mean her removal as Prime Minister and a subsequent battle within the Conservatives to pick a new leader. Given that those that oppose Brexit are nearly as numerous as those that support it there is absolutely no confidence the Tories will be able to pick a new leader and the UK may very well be without a government. Even if May is left in place while this battle roils, she will be the lamest of lame ducks.

Analysis: Parliament will have yet another opportunity to approve the deal that May worked out with the EU but there is absolutely no sense that her own party will support her – much less the opposition. The EU granted an extension but a very brief one and most in the UK see it for what it is – another step towards forcing the UK to comply with their terms. The expectation is that May will go down to another defeat and this time it will mark the end. She would almost certainly resign as the Tory party can't formally dump her until this coming December. Should she resign the ensuing contest to replace her will make negotiating with the EU next to impossible.

There have been many that criticize the EU for their lack of flexibility but they are operating under threats of their own. There are at least five current members of the EU that have indicated they might be better off without the EU and have contemplated their own exits. The three that are the most frustrated include Italy under its virulently anti-EU leadership (combo of the Northern League and the Five Star Movement), Greece under the leadership of Alexis Tsipras of the left-leaning Syriza party and Spain as the new government contends with the unrest in Catalan territory. The thing that seems to be keeping these states engaged with the EU is the fact that Britain's departure has been so chaotic and devastating to the British economy. If the EU takes steps to make that exit any easier it may tempt those other nations to pull out and the EU will soon cease to exist.

There are battles within battles and it seems that nobody really has the welfare of the British people in mind. The economy is collapsing towards a deep recession that will plunge millions out of work and destroy thousands of businesses. The border battle over Northern Ireland could easily reignite "the troubles" and now Scotland is pushing for independence again. Remember that both Northern Ireland and Scotland voted overwhelmingly for the UK to stay in the EU. The Tory party is in shambles and the Labor Party is not in much better shape. Britain will be years in recovering from this and so far, they haven't even been able to get started.

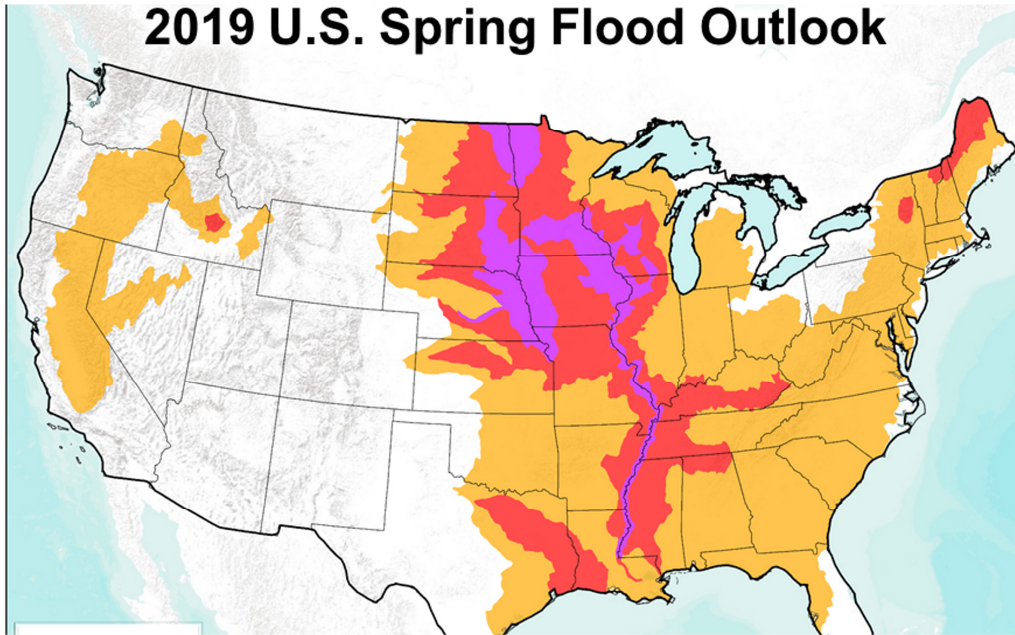
China's Farm Sector Leverage

As the trade talks between the US and China continue it has been nearly impossible to predict an outcome. Both sides are being pushed towards positions they do not really like and the leaders of both nations know that any deal will upset some element of their support base. A good percentage of the Trump base is virulently anti-China and will see any concession as a defeat. The Xi approach to growth in China lacks universal support and some within the Politburo want him to take a tougher stand.

Analysis: One of the sticking points from the start was the demand from the US that China buy more from the US and practically speaking that means more agricultural output. The Chinese have agreed to do just that but have been reluctant to commit to numbers. They are clearly seeking some leverage on other issues before diving in to buy more US food. They know full well that this spring's floods have devastated the US farmer and this will mean that China's market will be more important than ever. If the US wants China to help rescue the US farmer the Chinese are demanding something in return – probably an end to the idea of the US unilaterally imposing tariffs again if the US decides that China is violating their promises. China knows that these farmers are a big part of the Trump base and are now faced with the challenge of either supporting Trump in a hardline approach to China or protecting their livelihoods by making a deal with China that gets US exports of food back up to traditional levels. It is hard to say whether this is just a current negotiating tactic or a real impasse. Most analysts think a deal will be made as they would make most sense for both nations but that also assumes that the personalities involved see it the same way.

Have You Looked at the Black Owl Report?

It is an odd name for a publication that deals with setting strategy for the business community. The inspiration is the "Black Swan" theory that was developed by Dr. Nassim Saleb. Simply put it held that unexpected events happen all the time – the problem is that nobody knows just when that will be. A company has to have contingency plans for just about everything and they need all the intelligence capability they can get to be forewarned. The "Black Owl Report" seeks to provide that intelligence to guide business strategy. Check it out for yourself – ask for a free one-month trial by contacting Karen Sanchez at ksanchez@armadaci.com. If you like it – a subscription is \$84 a year (just \$7 a month).



By this time it has become more than obvious that this will be a very tough year for the farming sector. Things were already bad due to the issues that dominated last year (drought, low prices, foreign competition) and now those same challenges are in place but there is flooding to add to these woes. It is estimated that almost a fifth of the farmland in the middle of the country will be not be planted until mid-summer and maybe not at all. Bankruptcies in farm country were already high and will be getting higher. The trade wars are not helping either. This is not shaping up to be even an adequate year for US agriculture.

Speaking this Month

03/26/19	Austin	Bank CEO Network	Private
03/27/19	Napa	Association of Rotational Molders	Private
03/28/19	Kansas City	Nat'l Tooling and Machining Association	Public
03/29/19	Kansas City	Retired Old Men's Eating Organization	Private
04/03/19	Wichita	The Bradbury Group	Private
04/10/19	Phoenix	GAIN/PGI	Public
04/11/19	Kansas City	Landmark Bank Lunch	Public
04/17/19	Kansas City	Construction Financial Mgmt. Assoc.	Public
04/18/19	Chicago	NACM	Private
04/24/19	Kansas City	Infinitas Breakfast	Public
04/24/19	Kansas City	NACM	Private
04/25/19	Columbia	Missouri Banker's Association	Public
04/25/19	St. Louis	NACM	Private

Animal Antics

By now most loyal readers of the BIB are well aware of my attachment to the feline. With five cats there is never a dull moment and that is especially true now that one of them is a kitten. One of the conversations I can now count on when I give talks is one or two that surround the animals in other people's lives. I hear a lot from other "cat guys". We still have to somehow justify our feline buddies as we are supposed to favor dogs but I am noticing that men are a lot more cat oriented than might have been the case in the past.

One recent story features a bonded pair that had been adopted from a refuge when they were about three or four. They were deeply suspicious of their new circumstances at first and simply clung to one another and hid for weeks that stretched into months. One day as spring started to make its appearance the guy was bringing his motorcycle out and noticed that both cats found this fascinating. He sat on it and let them check it all out and then he started it – thinking they would bolt. They didn't. He rode up the driveway with the two of them in a cat carrier (which they normally hate). No protest – just wide-eyed curiosity. Fast forward a few months and he has a picture of two cats wearing little helmets and sitting in a specially fitted side car. They go everywhere with him and most days he finds them curled up in the side car – lest they miss an opportunity.

Nothing so dramatic at our household but a revelation nonetheless. My "daddy's cat" is Scoot – she has never interacted with the other cats as she is convinced she is "people" and mine alone. It has been sad that the others play with one another, sleep together and all that. Scoot was always alone...until Seamus came along. We about passed out the day we saw the two of them romping and playing. They sleep together and Scoot shares most everything with the kitten. He does things that other cats would get smacked for and he rarely even evokes a hiss. Scoot has a buddy of her own at last!

What Do We Mean by Intelligence?

The name of this publication is the Business Intelligence Brief. Why did we call it that? All three words mean something to us and inform what we do. The first is business. This is a very broad term as there are tens of thousands of different businesses and they have only a few things in common. Our intent is to provide the kind of information that helps people understand the world and helps them grow their business and make bigger contributions to the companies they work for.

That brings us to the intelligence part. We believe in providing intelligence that is actionable and timely. The aim is to be able to anticipate what is to come so that contingency plans can be developed. We are not reporters, we will rarely be involved in "breaking news". We are analysts and we strive to provide answers to the key questions of "why" and "so what".

Finally – we strive to be brief. That is far harder than one would assume. The temptation is to go on and on in detail but that is too much to digest. We simplify when we can but encourage readers that want more to reach out and ask.