



Basis Points – February 14, 2019

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Above the Fold

- The S&P 500 has now rallied 18 percent off its December lows and has risen 10 percent year-to-date. The WSJ reports that investor cash balances grew sharply during the December market downdraft. Investors sold into the correction and at exactly the wrong time, given the strong market upswing since the Christmas Eve low.
- The labor market remains extremely tight. Job openings rose 2.4 percent in December to a record 7.4 million. Private sector job openings advanced 3.0 percent to a record of 6.7 million, rising 30.4 percent over the last year. Job openings are considered a leading indicator, and this implies jobs growth in the months ahead.
- The chicken processing business in the U.S. is an oligopoly with three strong players: Tyson, Perdue and Pilgrim's Pride. There will now be a powerful new entrant, as Costco is investing \$440 million to build out a massive chicken growing and processing operation in eastern Nebraska, which will allow the warehouse retailer to control its own supply chain and continue to sell rotisserie chickens at \$4.99 each. Costco will build a huge processing plant, hatchery and feed mill, and around 100 new chicken farms in the area that will be under contract to raise the birds for Costco. Costco sells approximately 60 million rotisserie chickens each year and building a system to stock its own stores is a way for the company to better manage supply and costs in a business tightly controlled by large companies. The Nebraska operations will supply 40 percent of Costco's yearly chicken needs.

Three Things

- Amazon is a giant online retailer but has also grown its physical real estate footprint to an extraordinary scale. Amazon now owns 288 million square feet of warehouses, offices, retail stores and data centers. In 2017 alone, it added more square feet of building, 75 million, than the company owned in total in 2012 — 73 million. Amazon now has 48 times more square footage than it did in 2004. For comparison, the largest Walmart Supercenter in the world is 260,000 square feet; Amazon has added facilities equivalent to 590 of those stores just in the past three years. When your revenue increases sharply from \$136 billion in 2016 to \$233 billion in 2018, you need a lot of space to store products.
- Businessweek notes that U.S. homebuilders are not building enough homes to satisfy demand and population growth these days. While the housing bust of 2008 was caused by extreme overbuilding of homes from 2004 to 2007, the amount of housing is now lagging demand and will take a long time to catch up. The lack of affordable housing is propping up prices at levels that exclude many Americans from ownership. Aggressive homebuilders were wiped out after 2008, and the survivors are cautious about building new homes. The rate of housing starts on single-family homes remains below the level of the early 1960s, when the U.S. population was 60 percent of what it is today. Fannie Mae surveyed housing lenders recently, and only 1 percent blamed tight standards for credit for the weakness in sales. Forty-eight percent cited an “insufficient supply” of available homes.
- The average lifespan of a honey bee is 10 weeks, and their entire lives are spent collecting nectar from plants and flowers and converting their catch to honey so that future generations of bees are able to survive the winter. The average honey bee only produces one-twelfth of a teaspoon of honey over its short life and will enjoy no benefit from its work, as each bee will surely be dead by the time the honey is consumed by its offspring during the next winter. The production of each individual bee seems small and insignificant, but each bee’s contribution to the hive serves to ensure the survival of the collective in the future. The next time you feel like the work you do in your children’s life is unappreciated, consider the selfless contributions of the average honey bee.

Did You Know – The Best Thing Since...

While most inventions seem obvious to today’s consumers and feel like they have always been in use, most everyday inventions began in the mind and garage of a quirky would-be scientist and were either laughed at when rolled out to the public or were told that they would have no use in society and would not be adopted by the public. The road to everyday use is typically a long and frustrating one for the inventor, and fame and fortune only arise after a long struggle.

It was so with the invention of sliced bread. Bread has been consumed by humans for nearly 3,000 years, and in the early 20th century, Americans still ate about one-third of their daily calories in the form of bread. Any invention involving bread touched a large portion of the population. As an idea, sliced bread seems straightforward, but the invention of the machine and its adoption by the public saw great hardships, struggle and marketing hurdles before large-market success was achieved.

Born in Iowa in 1880, Otto Rohwedder moved to Chicago at age 20 and earned a degree in optometry. He later pursued a career in the jewelry business and opened three jewelry stores. With the small profit he earned from the jewelry stores, Otto tinkered with new inventions in his garage workshop at night.

At that time, all loaves of bread were served whole, as consumers thought that pre-sliced bread would quickly go stale, and it was too difficult to hand-cut bread for mass sale anyway. The only fresh bread for sale at that time was unsliced bread. But Otto heard the common complaints of many women in his town who told him that slicing bread at home was difficult, time-consuming and even dangerous, as hard bread required a very sharp knife.

Otto realized that there was a huge need in the marketplace for a mechanical bread slicer. He performed market research to prove the need for the device and to hear from women how thick the slices should be. A half inch was the near-universal answer, so Otto got to work on blueprints for his clever invention.

Otto sold his jewelry businesses in 1916 and began building the first model of his machine in an abandoned warehouse outside of town. For an entire year, he sketched hundreds of blueprints of possible bread-slicing machines and began manufacturing his first machines in 1917. But then tragedy struck. His warehouse burned down, along with all his blueprints and prototypes. Years of hard work and sacrifice were lost.

But Otto did not quit. He secured a job as a securities agent to earn money to support his family and rebuild the capital he would need to reconstruct his plant. By 1927, he had built another bread-slicing machine, which was a far better model than his original creation. The new machine not only sliced the bread, but also tightly wrapped the sliced loaves in wax paper, achieving the long-lasting freshness for the bread that everyone craved.

Otto's machine was built and ready for commercial use, but for many months there were no takers. Bakers did not believe that consumers wanted to buy sliced bread, and thought it was a fad. Bakers also thought the machine was too big and

bulky, and too expensive for small shops. Otto struggled to convince the world that his brilliant machine was needed.

Otto's only hope was his friend, Frank Bench, who owned a bakery. Otto convinced Bench to give his contraption a try, and the first sliced loaf came out of the machine in Chillicothe, Missouri, on July 7, 1928. The product was met with rave reviews from the local newspaper, who described Otto's sliced bread as "the greatest forward step in the baking industry since bread was wrapped." The expression was later changed to the now very commonly used "the greatest thing since sliced bread."

So popular was this new idea of sliced bread that in 1930 Continental Baking Company used Otto's machines to build an entire business around sliced bread, and named it Wonder Bread. By 1933, only five years after the introduction of the bread-slicing machine, nearly every baker in the country had a slicing machine installed and 80 percent of the bread in the U.S. was sold sliced.

Otto was the typical "30-year overnight success." He later sold the patent rights to his machine to an industrial machinery company and joined the company as an employee. He later retired in 1951 as vice president of sales.

Although his remarkable invention saw success very quickly, Otto's long road to that success spanned 12 lonely and frustrating years. He could have quit on his dream many times, especially after watching his hard work and dreams go up in smoke. But Otto kept his eye on the prize, and eventually changed the world and many consumers' lives with his grit and perseverance. It is not always the brightest or most lucky folks that see eventual success, but the people who do not quit in the face of adversity.

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