

It's All About Employment July 2010

It takes a job to earn a salary. It takes a salary to pay a mortgage. Seems quite simple. If you look at our current economy from this perspective it is easier to understand why we have a mortgage and a housing problem, which is why we have/had a banking problem, and why we are rapidly adding to our government debt. It is safe to say we would have fewer problems if we had ample jobs because then we would have ample salaries that could pay off our ample debt.

Unemployment today seems stuck around 10%. Add in under employment and we are close to 20%. So about one out of five workers is either making zero or less than they were not long ago. Expect if you asked your neighbors...and everyone in California...the great majority would suggest they are also making less than in 2007. It seems today that pretty much everyone save a few hedge fund managers is making less than they were a couple years ago.

To someone in debt earning less can be almost as challenging as being unemployed. You have less money to pay off that debt, or increase consumption, which is now growing nationally around 1%. Imagine consumption growth without a trillion dollar "stimulus".

To make matters worse we seem to be in the early stages of employment losses in one of our most stable "industries"...government. Teachers are getting laid off in states drowning in fiscal red ink. Municipal construction projects have been put on hold. Government pension and health care benefits are starting to be cut. The austerity in government trend has just begun. Now even the 40-hour a week government employee has a job at risk or is about to earn less money and/or receive less in benefits.

What's going on here? Why can't we seem to grow employment? How can it be that only three to four years ago U.S. unemployment was about 5%, what economists then liked to refer to as "full employment"? How could we have fallen off the cliff so fast and so far? And why can't we seem to climb our way out of this employment ditch?

Early readers may remember the very first official Armchair musing. That is when the light bulb went off which inspired the Armchair. Our problem...the reason we can't seem to grow employment is because we are experiencing a **Technology Hangover**.

Technology is destroying jobs faster than our natural economy can replace them.

We all know today's technology story. It seems to have started with the fax machine followed by the Personal Computer followed by the cell phone followed by the Internet followed by the search engine. Those were some glorious days from around 1980 to about 2000. Gadgets kept showing up we absolutely couldn't live without and they kept getting better and better, cheaper and cheaper.

For the first ten or more years we were spending around \$2,500 to get the latest and greatest Personal Computer. Now you can get the latest PC for about \$500. PC's were initially assembled in the U.S.,

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some right up the freeway at Compaq Computer in Houston. That changed. You can thank Dell and the Internet. Dell led the wave of supply chain innovation. The Internet inspired it to happen.

Dell was born out of the new technology. Their initial business model shunned traditional retail. Technology allowed them to skirt that distribution channel. Then Dell used technology to increase their supply chain productivity. Benefiting from instantaneous communication around the world...thank you Internet...Dell began outsourcing its manufacturing.

In short order, because their costs were lower, Dell became the 800-pound gorilla in the PC market. To stay competitive HP and IBM scrambled to replicate Dell's model. Compaq disintegrated into HP and Lenovo, a Chinese company, now owns IBM's PC business.

Manufacturing around the world followed Dell's lead. The "Platform Company" revolution exploded. Thank you GaveKal (www.gavekal.com) for understanding and describing this change. Platform companies are design studios and marketing departments. Production is moved to cheaper markets. We all know where those cheaper production markets are, the part of the world that is growing, not stagnating or contracting.

Technology today has inspired a feverish search for the cheapest most reliable source of design, production and distribution in everything around us. We are on this perpetual hamster wheel of forced productivity growth. If we don't make our operations more productive today and every day, those competitors who do are going to eat our lunch. And increasing productivity means...obtaining the same or greater output for less man-hour input...read...fewer jobs.

Just look at one massive job destroying technology...the Amazon Kindle. Look at the jobs that can be (are being?) destroyed by the electronic book.

It starts with forestry management, then there are the lumberman, then truck drivers from the forest to the lumber mill, then lumber mill workers, then more truck drivers from the lumber mill to the pulp and paper plant, then pulp and paper plant jobs, then more truck drivers from the pulp and paper plant to the printing and binding plant, then printing and binding jobs, then more truck drivers from printing and binding to the warehouse, then warehouse jobs, then more truck drivers from the warehouse to the retail store, then retail store jobs.

Look at all those jobs the Kindle can destroy! And guess what? It can destroy even more jobs. Now we need fewer chainsaws, fewer paper mill machines, fewer paper mill buildings, fewer trucks, fewer truck parts, less fuel, less retail space, fewer retail development and construction companies, fewer property managers, plumbers and electricians to maintain the vacant mall, the vacant paper mill, the vacant printing and binding facility and the vacant warehouse.

Well-schooled economists should at this moment be calling me on the carpet. "Doug. You are totally wrong!!!! Every period in history has proven that innovation inspires more not fewer jobs!"

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They are right. Millions of jobs are being created...in the Emerging Markets. That is where the Kindle is manufactured, as well as the iPhone and just about every appliance, toy, clothing, sporting good, electronic gadget...okay...just about everything you find in a store save some food. The Mature Markets can't compete in the production of many products. Our costs are much higher for labor, social safety net, environment, government and debt service. We might never have seen the Kindle or the iPhone if they had to be made in America. They would probably each cost about \$2,500, not the \$200 provided by technology and cheaper labor markets.

Don't get me wrong. I love the new technology. I love innovation. Innovation is what inspires the world to be a more prosperous, more exciting, more engaging, more fulfilling and even a more peaceful place. But...**innovation today is changing the nature of industry in Mature Markets faster than we can invent enough new industry jobs to replace the ones being destroyed.**

With each company and soon each government forced to improve their productivity, we are likely facing high unemployment and under employment for quite a long time. We may ease the pain some by allocating stimulus to increasing infrastructure productivity rather than saving Wall Street gamblers, but we are a Mature Market. Our productivity can't increase to such a degree that we steal jobs back from China. And the Apple, Google, Amazon and Facebook jobs are not going to former lumberman, auto, or home building construction workers.

So on the one hand we have a jobs – skills mismatch. We have too many production worker trained folks who don't have skills for the information worker jobs. The lifestyles and mortgages of those production workers are based on compensation they can no longer earn. But on the other hand we really don't have enough information worker jobs to go around as technology continues its relentless path to increasing productivity...getting the same or greater output for less man-hour input.

It takes a job to earn a salary. It takes a salary to pay a mortgage. The double edge sword of innovation is slicing through us. Productivity growth will keep a lid on jobs which will keep a lid on compensation which will continue to challenge debt levels, asset value levels and the social responsibilities of Mature Market government. Of course this couldn't have happened at a worse time, at the beginning of the Baby Boom retirement cycle. People need to be drawing down savings not paying down debt as they retire.

This is the unintended consequence of our current innovation period. This is economic evolution.



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