Fox-Smith Wealth Management Quarterly Commentary

Third Quarter - 2021

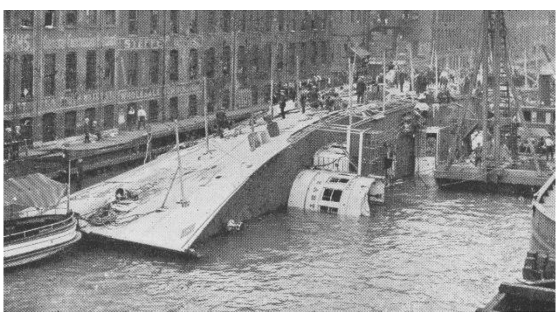
"The Law of Unintended Consequences"

Economic Outlook and Market Commentary – Gustin D. Fox-Smith, AIF®, ChFC®

It is said that "The road to Hell is paved with good intentions." This is said to remind us that even though you might achieve your goal, the process of doing so will likely generate unintended consequences which we often cannot predict. Keep in mind that it is the *Law* of unintended consequences, not a *Theory.* I believe we are seeing this effect right now as the economic recovery in the U.S. is hampered by the cobblestones of roads laid with good intentions.

History is replete with examples of times when actions were taken with the best of intentions and often with 100% support because the action made sense and was completely rational, but the actions resulted in negative and unintended consequences. When this occurs, we are told that there was no possible way to predict the unintended consequences, but I disagree. It seems in almost every case that a little extra time thinking before doing would have saved a lot of money and lives.

Take the Titanic, for example. The Titanic disaster in 1912 caused an outcry from the public for safety regulations on ships transporting passengers. One of the first regulations after the disaster, signed into law by Woodrow Wilson in March 1915, required that every ship must have enough lifeboats for 75% of the passengers on board and life jackets for all. I'm sure you can agree that no rational person would oppose this rule, it just seems like a given. However, the law of unintended consequences cannot be broken, and the consequences fell upon another ship you may never have heard of, the SS Eastland.



The Eastland was an inland steam ship that ferried passengers between Chicago and Cedar Point. On July 24, 1915, just 4 months after the lifeboat law passed, the Eastland had completed the upgrade that doubled its compliment of lifeboats and was loading passengers in the Chicago harbor. The extra weight of the lifeboats altered the ship's metacentric height and caused the Eastland to begin listing while still tied to the dock in calm water. Within minutes, the boat had "turned turtle" and rolled over on its side trapping many people inside.

Estate Planning Resource Authored by Gus Fox-Smith AVAILABLE NOW!

It is said that the only certainties in life are death and taxes and since no one gets out of here alive, why do 50% of Americans fail to plan for their mortality?

Fox-Smith Wealth Management is proud to announce the much-anticipated publication of ***"Clearing the Way Forward"***, a personal Estate Planning workbook written by our founder, Gus Fox-Smith. It is a tool that will walk you through the process of designing and documenting your own estate plan so that your wishes will be fulfilled when the time comes.

If you or someone you know is putting off doing this important work, ***"Clearing the way Forward"*** will help demystify Estate Planning and help you plan for the inevitable.

The book is now available to order from Amazon.com – Just search ***"Clearing the Way Forward",*** by Gus Fox-Smith.

Trust me, your kids will thank you.

In the end, the lifeboat law unintentionally caused the deaths of 844 people on a top-heavy boat sitting less than 20 feet from the dock. This is more than died on the Lusitania (785) or the Titanic (829), yet the story has not been remembered in the modern age mostly because there were no rich and famous passengers. That day, the ship was ferrying some of the 7,000 employees of Western Electric to their annual picnic, so the ship was full of working-class families.

During the debate over the lifeboat bill, the general manager of the Detroit & Cleveland Navigation Company had warned that some Great Lakes vessels, with their shallow drafts, "would turn 'turtle' if you attempted to navigate them with this additional weight on the upper decks." Too few legislators listened.

An example of cascading consequences comes to us from Macquarie Island, halfway between Australia and Antarctica. Discovered in 1810, the island was home to a massive population of seals. Fur seals were valued for their fur and the elephant seals and penguins on the island were valued for their blubber. This caused Australians to set up harvesting camps that nearly wiped out the entire seal and penguin population of the island within a few short decades. But this wasn't the cause of the real problem, that came from something completely unintended.

Rodents jumping from ships visiting from the mainland resulted in booming populations of rats and mice on the island. In an attempt to protect food stores from rodents, cats were introduced to the island to keep the vermin in check. The cats multiplied rapidly and did bring down the numbers of rats and mice. When seal and penguin harvesting ended about 70 years after the island's discovery, the camps were abandoned, and the island no longer had any human residents. The cats were left behind in hopes that the feline and rodent populations would balance out.

Before departing, the Australians did what the English have done for as long as they have been sailing. They left a few rabbits on the island so that any shipwrecked sailors that may come upon the island in the future would have a source of food. Rabbits are much easier to catch than rodents, so the cats multiplied exponentially with such easy prey. As the feline numbers grew, the island lost two native species of flightless birds, a parakeet and a rail, easy prey for a hungry cat. While the cats focused on eating flightless birds, the rabbits bred so fast that they nearly consumed all of the island's vegetation, leaving it barren.

By the 1970's the rabbit population was over 130,000 and they were destroying the island's ecosystem. To spur recovery of the plant life of

Financial Trivia

Last quarter's trivia question was: "What is the oldest company in the Standard & Poor's 500?"
Answer: Lorillard

Lorillard was founded in 1760 in New York City, though now headquartered in Greensboro, North Carolina. Lorillard was the third largest cigarette maker in the U.S. with annual sales of $6 billion until they were taken over by another tobacco company, Reynolds American. The company started trading in 1899. If an investor purchased shares in Lorillard on January 11, 1964, when the Surgeon General of the United States, Luther L. Terry, warned that cigarette smoking was linked to cancer, an investor would have lost 5% the day of the announcement. But if they held on to the stock until it was taken over by Reynolds, they would have increased their investment by more than 100 times!!

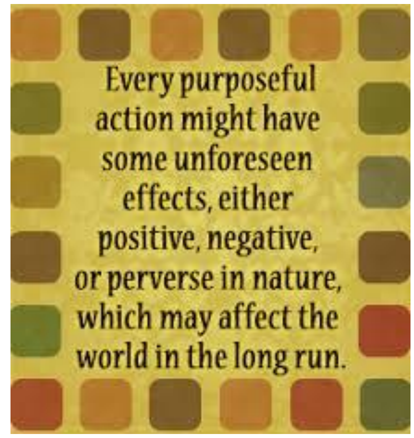
We did not receive any correct answers last quarter. Better luck this quarter!

This quarter's question:

When Windows 1.0 was first launched in 1986, the cost of the software was $100. If you bought $100 of Microsoft stock instead of Windows on the release date, what would your investment be worth today?

E-mail your answers to Erin at erin@fswealth.biz and we will award a prize to the first correct answer *(Be honest, no "googling" it!)*

the island, the disease myxomatosis was introduced to the rabbit population and their numbers dropped to less than 20,000 in just 10 years, allowing the island's vegetation to recover rapidly.



However, with fewer rabbits around, the massive population of cats turned to other wildlife for food, especially burrowing birds. In 1985, the fear of extinction of some of the species caused conservationists to approve shooting the cats, the last of which was killed in the year 2000.

To their horror, the rabbits overcame myxomatosis and in just 6 short years their numbers again threatened vegetation. It was so bad this time that rabbits were blamed for a landslide in 2006 that wiped out most of an important colony of penguins being used to bring back their numbers on the island.

This story is not yet over. The Tasmanian Parks and Wildlife Service plans to take a scorched earth approach and wipe out all of the 130,000 rabbits, 36,000 rats, and 103,000 mice that currently live on the island to avoid further meltdown of the ecosystem. But this type of move has never been attempted on such a large island and I expect that it will have its own unintended consequences. 200 years of problems that were successfully solved by rational actions that then caused unintended consequences and more problems to be solved.

I bring these two stories up because I wanted other examples of the law of unintended consequences, but also because I find them fascinating and wanted to share them. Thank you for allowing my detour away from the point of my commentary. My point, again, is that we are being negatively affected by unintended consequences of rational actions taken for good reasons.

On a local level, national corporations and companies that have remote employees working online across the US have all but ceased any hiring withing the state of Colorado and this includes some companies that are based within our state.

Seeking to combat gender-based pay gaps, a noble goal I think we can agree upon, Colorado recently passed the Equal Pay for Equal Work Act and it took effect January 1, 2021. One of the provisions of the law requires employers hiring in Colorado to publish the salary or range of salaries for the position in the job ad. The rational goal here is that current employees of the company will be able to see what is being offered to applicants for a job they may already have and may be being paid less for, which allows for factual negotiation of compensation. It also ensures that, regardless of the identity of the job applicant, the compensation has already been set.

All of this is understandable and should help to lessen any pay gaps that may exist over time. But what I want to highlight here is the unintended outcome of this law, which is less jobs for Coloradoans. Ads like these have been appearing on job sites since the law's enactment:

> *"This is a remote job except that it is not eligible to be performed in Colorado,"*
> *- A listing for an account manager position with short-term vacation rental giant Airbnb says.*

> *"We are seeking applicants from the Boston area and from any state except Colorado,"*
> *- Reads another recent job listing, this one from Denver-based tech education and shared office space provider Galvanize.*

Claims by the bill's sponsors that companies are skirting this requirement by avoiding hiring in our state because they want to "avoid pay transparency" or that they just "want to continue to underpay women." are simply political posturing. What is really at work here is the result of interstate commerce and the law of unintended consequences. They don't realize that our economies are not reliant on Colorado only.

As we all are aware, the cost of living varies greatly depending on where you live and compensation for the same job will vary along with the cost of living where the job is being offered. It has always been this way and it is completely rational. Just looking at rent vs. average income by state shows this variance clearly. The mean rent in California, the highest in the US, is $2,518 per month and the average wage across all occupations is $65,740. Utah, ranked roughly in the middle of the states has a mean rent cost of $1,526 and an average wage of $51,430. At the low end, Mississippi has the lowest rent cost of $1,055 and an average wage of $41,600. For comparison, Colorado ranks as the 36th highest cost of living with a mean rent of $1,927 and a mean wage of $60,840.

If you own an online travel company that employs a remote workforce across the US and want to ensure you are paying each of your people a living wage, the information I just quoted is vital to the survival of your business. If I am hiring someone who lives in California, I am going to have to pay them more than the national average if I want them to be able to live on their salary and thus stay with the company long-term. So, let's assume I pay them $70,000 per year, roughly 7% above the state average.

Then I am talking with a candidate in Mississippi who will be doing the same job. For them to have the exact same lifestyle in Mississippi would require me to pay the same 7% above the state average which would mean I should pay them $44,800 per year. This saves me over $25,000 per year and the employees will have the same lifestyle due to cost-of-living variances. If I am forced to advertise the job at $70,000 per year, I will have to pay everyone that wage regardless of their state of residence and then I will create another inequality, unequal lifestyle for equal work. The person in Mississippi would be making 60% more than the state average wage and would have the ability to afford a much more lavish lifestyle than the employee in California. Is this not inequality as well?

Then the bigger issue is an employer's existing workforce. Assume I am making these hires and that I always pay the state's average wage. But this time I already have 200 remote employees and most of them live in Utah. To hire in Colorado, I will have to post the $60,840 wage. As soon as my 200 Utah employees see the pay rate that I am required to post in my ad if I want to hire Coloradoans, they will be demanding the same and I will be forced to pay it. If they each make the Utah average $51,430 and I am forced to increase everyone to match the high Colorado wage it costs me $9,410 per employee per year (plus employment taxes,

Service Opportunities with Fox-Smith Wealth Management

Over the years, we have tried to keep track of our client's interests and tailor client events around those interests. (Of course, events have been on pause during Covid.)

One interest we have not asked clients about, that you may share with some of our employees, is volunteerism. If you would like to be notified when we hear of local Volunteer opportunities, such as preparing a meal at a homeless shelter or kids' home, just let us know!

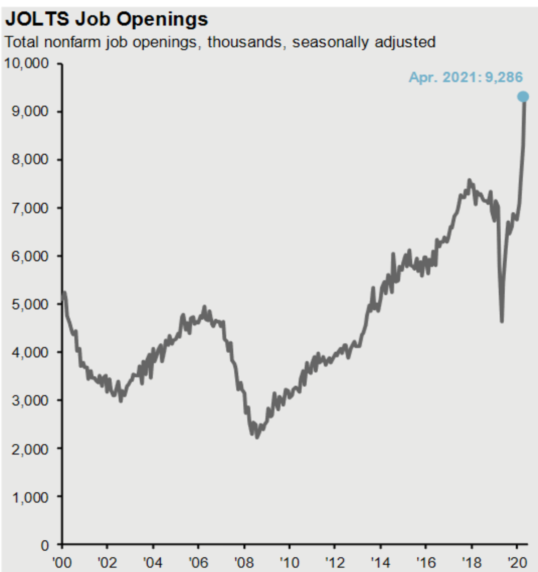
We will send out an email when volunteers are needed, you do not need to reply to us and there is never any obligation or commitment to act on any of the notifications. We will simply send information about what is needed and how to sign up. If you are available and interested, sign up and serve. It is likely that one, or more of us, will see you there! This will not be frequent, or overwhelming, just a call to action if more helping hands are necessary to provide needed services. If, at any time, you ever wish to be removed from the email list, just let us know!

To add your email to the list, please email Dahna Clarke at Dahna@fswealth.biz

Happy Volunteering!

but that is another article). That means to match my workforce with my ad would cost me $1,882,000!! Nearly $2 million just for the "privilege" of hiring within Colorado! There are 49 other states, so the smartest business decision is to avoid Colorado completely. Not because I am a sexist pig, but because it is the only choice that makes financial sense.

So, on a local level, job creation is being hampered by an unintended consequence of a well-intentioned law. On the National level our growth is being much more severely disrupted by another unintended consequence. When the Covid pandemic first caused governments to begin mandating lockdowns and closures of certain businesses, President Trump extended unemployment benefits so they would be able to be collected for as long as a full year. This is a common move by Washington when economic downturns are severe. Left alone this would not cause a problem, but Trump added the Federal Pandemic Unemployment Compensation (FPUC) program to the extended benefits. FPUC provided for an increased unemployment payment of $300 per week on top of other benefits. With the economy at a standstill and so many unable to work, the FPUC was supported by nearly all US citizens for good reason.



Source: JP Morgan Guide to the Markets

What President trump and now President Biden did not expect was that the FPUC would actually reward people for not working. Once you add $300 per week to the unemployment payment, the total income you are paid exceeds the starting wage in about 70% of companies. Thus, trying to help people who are struggling has resulted in the unintended consequence of our current labor shortage. How much more growth would we have today if every business could hire the employees they desperately need. Job vacancies are at record highs right now because people are simply acting in their own best interests, which they should be expected to do. If going back to work meant a 20% pay cut and you would see your family less, what choice would you make?

The labor shortage is so stark that it is hampering economic growth as companies compete with welfare and unemployment benefits for employees. Wages are climbing as a result as companies are desperate to hire but rising wages cannot cover the whole gap alone. The artificially inflated benefit payments need to stop before this unintended consequence will abate. Luckily, the FPUC is slated to end on September 6th, unless they extend it again like they did earlier this year.

One more unintended consequence will be felt this quarter and it is nearly impossible to predict just how big the impact may be. Since the start of the Covid lockdowns, the federal government has placed a moratorium on evictions of renters from rental housing. The moratorium has been extended several times, but the last extension is set to expire on July 31st.

The moratorium makes logical sense. If people are out of work for no fault of their own and you are trying to contain a virus, it is wise to prohibit evictions to keep people in their homes where they are not spreading illness. It is hard to argue with this logic, especially when their inability to pay rent is caused by government mandated actions. However, the unintended consequence of this policy will be seen very soon as we may see 16 months of evictions processed in a single month, a record number for sure, which will certainly make for negative news headlines.

Those who cannot pay rent will be expected to begin paying and they will need to catch up on their missed rent payments. Looking at rental statistics, even during strong economic times, makes the problem with this very clear. Any experienced property manager will tell you that once a tenant owes a month or more of rent, the tenant, no matter how well-meaning, won't be able to make up the unpaid balance as they often live paycheck to paycheck. The shortage is never repaid, and the tenant eventually moves out, leaving the debt behind to start fresh under a new lease elsewhere.

So, there are millions of people who are going to see their benefit payments drop by $1200 per month within 30 days of their landlord's bill coming due after so long. The number of evictions could be devastating but remains to be seen. On the bright side, due to unintended consequences, there are plenty of available jobs if the renters affected by this want to go back to work.

Get To Know Your Fox-Smith Wealth Management Team

In order for you to better know your team that are here to serve you at Fox-Smith Wealth Management, we will highlight one of our team members each quarter. This quarter we are featuring the person who makes sure everything is running smooth and the reason we all are able to accomplish anything in our day…the scaffolding of all of Fox-Smith Wealth Management:

Meredith Locke

Director of Operations

Meredith was born in Manhattan, Kansas, but she was not to stay there long; she has lived in 6 houses in 18 years, including Arizona and Illinois. Her father was a nuclear power plant inspector and keeping him from becoming too close with any one power plant was a good thing for all involved, except for Meredith, who got very use to moving. As a child, she loved crafting hobbies but was very much a tomboy. High school fed her love of theater as an avid member of the Tech Crew backstage or as a flute player.

Following her parents' dream to always live in Colorado, Meredith and her family moved to Colorado, where Meredith attended and graduated with a degree in Wildlife Biology from CSU in Fort Collins. Although her love of animals has never waned, it did re-direct toward being a stay-at-home Mom of two wonderful children. Although Meredith does say that her degree gave her the scientific attention to detail that makes her the perfection - expert that keeps our office in check to this day.

When not maintaining order and sanity at our office, Meredith can be found maintaining order and sanity with her Girl Scout Troop that she has led since her daughter was in 1st grade. So now all of you have an inside source for the much-coveted Thin Mints come next Spring! Meredith also loves to spend time outdoors, doing martial arts or just being with her family. She is an expert at switching gears from raising her teenage children to looking after he elder parents, all under the same multi-generational roof! Meredith's life motto is: Remember that we work so that we can live – we do not live only to perform work!

Fox-Smith Wealth Management became an even better place in 2016 when Meredith joined our team. She was originally hired to fill a part-time position while her children were at school, but it wasn't long before we begged her to take a full time role because of her incredible skills, remarkable attention to detail and amazingly kind personality!