

StraightTalk

PROVIDED BY STRAIGHTLINE FINANCIAL OF RAYMOND JAMES

VOLUME 4 AUGUST 2020



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The Butterfly Effect

As we have discussed in recent months, none of us could have predicted back in the mid-1990s that air travel would involve arriving to the airport an hour early in order to wait in line with our shoes and belts off to pass through security screening. And yet, in a post 9/11 world, that is not only accepted, but is also an expected routine that has become a permanent behavioral change. Almost a half a century ago, a branch of mathematics called chaos theory coined a term for a small event to potentially have a very large impact on the future; it was called the butterfly effect. Admittedly, the terrorist attack of 9/11, and the tragic loss of over 3,000 lives was not a small event, but it did occur almost 20 years ago, and has affected air travel for roughly 17 billion passengers ever since.

The butterfly effect is most often visualized in weather terms – wherein a butterfly flaps its wings in Tokyo, Japan, which creates a small breeze that grows into a weather pattern that creates a tornado, say, in Topeka, Kansas. Without knowing the scientific truth behind that weather example, it is still interesting to consider the idea of a butterfly effect...and ask, *what will the lasting changes be from the pandemic of 2020, years into the future?*

A glaringly obvious possibility for any of us who spent three straight months at home would be the rise of e-commerce, and the decline of the retail shopping experience. This trend is not new, having been called “clicks vs. bricks” for several years now, and was well underway before the year of the virus. As I wrote in the December newsletter of last year, 2019 saw records in virtually every online shopping category, including over \$4 billion in sales on Thanksgiving Day alone. And “Black Friday” has given way to “Cyber Monday” as the peak shopping day during the holiday season.

According to a ProShares research report, the other side of that trend was that “in 2019, which was a good year for the economy, over 9,300 brick and

mortar retail stores closed their doors – a 59% increase from 2018.” The report also concludes that in 2020 this trend is widely expected to accelerate, with predictions of over 15,000 stores permanently closing. I would point out that it is somewhat more difficult to buy some things online, like furniture and vehicles, which may remain an in-person shopping experience. However, it is becoming ever easier to buy many others online, such as groceries, medicine, clothing, and tech gadgets. *Will the switch to online shopping rather than in-store shopping be a permanent behavioral choice after the pandemic? If so, will those bricks and mortar retailers that wish to survive need to offer a “shopping experience” in order to do so?*

Having recently set our oldest daughter up in her post college apartment in historic Charleston, I have learned that one of the things that is fairly easy to buy online is a bicycle. The research outfit, NPD Group, reports that “personal bike sales in the U.S. nearly doubled in March 2020, compared to the previous year, up from \$350 million to over \$650 million.” Apparently, one thing you can do during a virus lockdown is ride your bike, for exercise or for enjoyment!

But, it is not only bike sales – Bloomberg reports that bike-sharing systems around the world are showing sharp increases in users. In New York City, ride share volumes are up 67%, Beijing reported a 150% increase in bike-share use in May, and London expects a 10-fold increase in cycling over the next few years. As a result of increases in sales and bike-share use, many cities took advantage of the reduced traffic during the lockdown to alter their city streets. Over 100 cities around the world have plans to either add dedicated bike lanes, or designated streets for pedestrian and bike use only, or both. Milan, London, Paris, New York, Philadelphia, Los Angeles, Seattle – all are creating bike and pedestrian routes in their cities as an alternative to public transit.

Will commuting by bicycle become a mainstream method of transportation in cities all over the country?

Perhaps part of the switch to bicycles for transportation is a sudden health craze, but more likely it is simply to avoid the close quarters of many public transportation options. Regarding that trend, a recent Bloomberg article states “the threat to public transit may be a lasting one, with the U.S. transit industry facing an estimated loss of almost \$50 billion in 2020. Driving is rebounding all over the world, and it could eventually return stronger than ever, depending on how long commuters remain wary of public transit.” In the article, June data from several large cities in China illustrates an 18% increase in morning rush hour traffic over the volumes from June of 2019. *Will this mean an increase in new and used car sales in the coming years? And, will this trend accelerate the move to electric vehicles?*

Speaking of which, according to Forbes, the demand for electric vehicles (and the batteries that power them) has led to a significant increase in demand for base metals like nickel, aluminum, and copper. The research from Forbes estimates demand for nickel and aluminum in 2030 will be 10 to 15 times greater than today. And a recent World Bank report looking out to 2050 predicts a possible 500% increase from producers of minerals like cobalt, lithium, and graphite, just to keep up with the growing demand for electric vehicles.

Assuming mining and production of those materials allows the electric vehicle trend to continue, the next question is – if we all start driving electric cars, which themselves emit no fossil fuels, won't the world be a cleaner place? The answer is.....maybe. A 2019 Digital Trends article, titled “*Is your EV actually powered by coal?*” digs into this issue. If everyone begins plugging in and charging their cars instead of gassing them up, where will that additional electricity come from? In the U.S. – the answer to that question depends on where you live. In West Virginia, 96% of all electricity comes from coal plants, and 12 other states get at least half of their electricity by burning coal. In 19 different states, including Virginia, natural gas is the primary source of electrical power generation, while in the Northeast and Hawaii, oil is

the predominant source of fuel for power. The U.S. still has about 60 active nuclear plants creating electric power, mainly in Illinois, the Carolinas and parts of the mid-Atlantic. The Pacific Northwest gets some portion of its power generated by Hydroelectric plants, as does the Midwest from wind power. *So, given that the United States has enough natural gas reserves to last another century, will it become the dominant method of electric power generation? Or will carbon-free methods like wind and solar energy power our national electric car fleet?*

One place you might drive your electric vehicle of the future is to a restaurant for a nice meal. Clearly, those restaurants that had outdoor dining spaces fared better in the phases of reopening across the country than those with only indoor seating. As a result, local governments in many areas are loosening the restrictions and permitting time required to create outdoor dining spaces – in some cases even on city streets or parking lots. According to a recent article in The New York Times, these outdoor spaces for impromptu seating are being called “parklets” or “streateries.” The article also points out that the dining app Open Table counted a tenfold increase in outdoor seating in spring of 2020 nationwide, compared to the spring season in the year prior. A recent survey found people favor eating outdoors over indoors by a 2-to-1 margin. *Will the preference for dining outside in fresh air be permanent after the virus is gone, or will we revert back to close quarters inside a restaurant?*

It is fascinating to spend time thinking about the preferences of a collective society, both in the immediate aftermath of this year's pandemic, and into the future once we are clear of it. Your fund managers are hard at work developing research around themes and sectors poised to thrive, and selecting companies best positioned to take advantage of these trends as they unfold. I don't know the future – but what I do know is that there will be innovators who take advantage of this moment in time, and build or grow an enterprise that will succeed from this butterfly effect. After they do, we will all wonder...*why didn't I think of that?* Fortunately, I believe that your investment managers will have done so...for all of us.

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