



Basis Points – February 26, 2019

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Above the Fold

- Food conglomerate Kraft Heinz took a \$15.4 billion write-down in two of its largest and well-known brands last week, a stark warning that even the most iconic consumer brand names are vulnerable to shifts in consumer tastes. Kraft Heinz reported losses of \$12.6 billion in the fourth quarter, compared with a profit of \$8 billion a year earlier, and cut its dividend by 36%. CFO David Knopf said the company is expected to “take a step backward in 2019.” The large write-downs on the value of their Kraft and Oscar Mayer brands highlight the struggles that packaged-food companies face as they try to keep up with the changing tastes of consumers and the rise of smaller, organic and online competitors. Consumers are turning away from processed foods, even Kraft Singles, a ubiquitous staple of lunches since the 1960s. Processed cheese sales now decline every year while natural cheese sales are growing strongly. Even McDonald’s has eliminated artificial preservatives from its own cheese to show consumers it’s prioritizing clean ingredients. Chains like Panera Bread and Cracker Barrel have cut classic grilled cheeses from their menus in favor of sandwiches with artisan cheeses like cheddar and Gouda.
- Warren Buffett released his annual letter to shareholders on Saturday. The 88-year-old Chairman of Berkshire Hathaway noted that profit figures for the company would be much more volatile going forward, as new accounting rules require the firm to count unrealized gains and losses in its stock holdings on its income statement. Previously, a company was only required to account for gains and losses after stock was sold. This new rule caused a fourth quarter 2018 loss for BRK on stock holdings of \$22.7 billion after the stock market corrected sharply in December. Buffett is not a fan of the new rules, as he sees them as not reflective of the true ongoing finances of his company. Berkshire is also sitting on a huge cash pile of more than \$100 billion, and Buffett would love to spend it on an “elephant”-sized acquisition, but he is just not seeing opportunities to deploy the cash in this market.

Three Things

- Warren Buffett spoke with CNBC on Monday morning and noted a trend in consumer tastes and purchasing patterns that is negatively affecting the business of Kraft Heinz. Buffett noted that Costco’s Kirkland private label has grown strongly over the past few years, and now accounts for one-third of all Costco sales. Buffett said the packaged-food icons in Kraft Heinz’s portfolio are struggling to compete with private-label brands at retailers such as Walmart and Costco. These private-label brands have been winning over customers with lower prices as the stigma surrounding generic brands has declined in recent years. Kraft Heinz sales totaled \$26.3 billion in 2018, while Kirkland brand sales grew to \$39 billion.

- Why do zebras have stripes? That question has puzzled scientists and zoologists for centuries. But the New York Times reports that we may finally have an answer. Scientists have concluded that black and white stripes create an optical illusion in the eyes of flies which keeps them from landing on zebras, saving them from disease and annoyance. Flies do locate zebras and attempt to land, but once they get close, the zebra stripes seem to dazzle the flies so much that they cannot manage a controlled landing. Flies zoom in too fast or veer off just in time, or simply bump into the zebra and bounce off. The high contrast between black and white most likely tricks the fly's low-resolution vision, which relies on sensing movement. How the stripes evolved on zebras is anyone's guess. Mother nature is a mad scientist.
- The WSJ reports that the current job market is so tight that even the FBI is having trouble filling positions. Few law enforcement jobs are more coveted than the FBI's special agent positions, but the extremely low unemployment rate is forcing the bureau to do something it has rarely had to do: aggressively recruit candidates. A slump in the number of special agent applicants — from a peak of 68,500 in 2009 to 11,500 in the year that ended in September — has forced the nation's top law enforcement agency to overhaul its recruitment, increase its outreach, target women and minorities and relax some eligibility requirements. FBI officials say that it takes about 16,000 applicants to get a healthy pool of candidates for the 900 special agent positions that open each year. The bureau has fallen short of that number for the past several years, as in the current job market qualified applicants have many other financially lucrative options. The applicant pool has been declining for years and is not the direct result of the current state of D.C. politics.

Did You Know

What was the worst year in history to be alive? The world may seem tumultuous these days with terrorist bombings, mass shootings, increasing economic inequality and a divisive political climate. Our world today is a far more hospitable place than in the past. If we think back through history to try to identify the worst year to be alive, we may consider that it would be 1943, as World War II engulfed the world and the Holocaust ravaged the Jewish population. Or we may conclude that it is 1918, as the Spanish Flu infected 500 million people worldwide, leading to between 50 and 100 million deaths. Or we could say that a very bad year was 1349, as the Black Plague savagely killed 50 million people in Europe, or 60% of the continent's population.

These are all valid guesses, but Science Magazine has reviewed the last few millennia and concluded that 536 was the worst year in history to be alive. Little was known about this period until recently, although people called it the Dark Ages, and it turns out for good reason.

A strange fog plunged Europe, the Middle East and parts of Asia into darkness, both day and night, for 18 months. People at the time had a very limited understanding of science and weather, and had no communication, so citizens could only guess as to why the sun was no longer shining. Many concluded that an angered god was punishing humans for their wickedness. Temperatures in the summer of 536 dropped 2 degrees, which brought on the coldest decade in 2,300 years. Crops failed due to the cold that year, global food supplies plunged and people around the world starved. Many people were only put out of their misery in 541, when bubonic plague struck many populous cities around the globe.

Although historians were aware that the middle of the sixth century was a dark time for both the planet and its citizens, the reasons for the darkness were not clear until recently. An ultraprecise analysis of ice from a Swiss glacier performed by a team led by Michael McCormick and glaciologist Paul Mayewski at the Climate Change Institute of The University of Maine has discovered the source of the global catastrophe.

This team of scientists analyzed an ice core from a Swiss glacier that revealed the dark secrets of the past. Digging down into the ice, inch by inch, reveals as much data about climate conditions in the past as cutting down a large tree and inspecting its rings. The scientists can analyze each slice of the glacier, ascertain its year and take chemical samples of the ice to note the compounds present in each slice. The team concluded that a cataclysmic volcanic eruption in Iceland spewed ash across the Northern Hemisphere in 536. Two other large explosions followed the first in 540 and 547. The massive, global climate changing events plunged the planet into economic stagnation that was not relieved until 640. Scientists also discovered that nearly every unusually cold summer over the past 2,500 years was preceded by a large volcanic explosion incident.

The ice sample from 640 showed a high level of lead ore in its chemical makeup. This was good news, as silver is smelted from lead ore, which indicated that European economies had rebounded from the long dark period, and economic activity had rebounded with the wide demand for silver for both industrial production and use as silver coins in a thriving economy. Lead also was missing from the ice samples from 1349-1353, as the Black Plague ravaged the population.

While we may feel like we are living in a very complicated world filled with disease, terror and war, just be glad you were not alive in 536.

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