

APRIL 1998

Computers, Eyeglasses and Productivity

“Worker Productivity” is of paramount importance in today’s environment of record stock prices, low interest rates and diminished inflation. One of the many unique features to this Bull Market is the fact that inflation is low during a time when wages are rising. In previous times, tight labor markets have foreshadowed inflation and caused higher interest rates, lower stock prices and, possibly, a recession.

One reason why the markets are calm in the face of higher wages is the fact that increased productivity has largely offset higher wages. Improved productivity means computers and other management techniques are used to produce more goods per hour than ever before. When productivity increases as fast or faster than wages, it is not “inflationary” for a company to grant 10% pay increases if employees work “smarter” and generate 20% more products for the same hours worked.

In large part, we credit computerization over the last twenty years for today’s improved productivity. While computer systems have been around for a while, it seems that only recently have they genuinely benefited industry. A good example is the retail trade which “scans” customer purchases and immediately knows which goods are selling and at the same time updates inventories. While they have been scanning for sometime, only recently have the retailer’s suppliers interfaced directly to automatically replenish inventory. The computer industry calls

this revolutionary process the development of a “digital nervous system”.

The question now is “can productivity continually increase enough to offset higher wages and keep inflation at bay?” In looking for historical perspective on this question, we turned to David Landes’ recently published book entitled “*The Wealth and Poverty of Nations.*” Our reading brought us to a startling analogy from nearly seven hundred years ago when a discovery was made which allowed Europe to leapfrog the world via improved productivity. In the 1300’s skilled craftsmen past the age of 40 were often unable to see well enough to continue their trade. However, the development of eyeglasses (crude magnifying glasses initially) enabled craftsmen to double or triple the number of years they could work. To quote the book, “Europe enjoyed a monopoly of correction lenses for three to four hundred years ... in effect eyeglasses doubled the skilled craft workforce and more than doubled it if one takes into account the value of experience”. Eye-

glasses also opened up the possibility for precision instruments which could not have been developed or manufactured by the naked eye alone.

In many ways, the development of eyeglasses seven hundred years ago and today's computer software industry are similar. With essentially no cost to society, a simple invention has caused a giant leap in the productivity of the human being. Only in today's case, Bill Gates plays the part of Europe. While we don't think his dominance will last 300-400 years, we do wonder how much he would have charged in 1306 for his latest version of "Bifocals '98"!

Closer to home, we recently added a company to our Buy List that exemplifies computerized productivity enhancement. **Parametric Technology Corporation** is the leading supplier of 3D solids modeling software used for automation of the mechanical design process. Parametric's software allows a company to design new products on a computer as opposed to doing so on drafting paper. Testimonials from Parametric customers indicate that the software allows them to introduce products in far less time, with higher quality and lower cost; great selling points for Parametric's direct sales force.

The operative point here is that for many reasons, worker productivity in the world is accelerating. Coupling that fact with an abundance of basic commodities (oil, etc.) and you have the essentials for a Bull Market. We are "focused" on taking advantage of these technologies (i.e., Parametric), but also concentrate on making rational investment selections in the heat of battle. The valuations on many wonderful companies are increasingly unsuitable by any measure except supply (too little) and demand (too much).

In conclusion, we have maintained our clients' asset allocation targets by rotating out of expensive stocks which have appreciated beyond their growth prospects (we sold **McDonald's** and **AT&T**) in favor of reasonably valued equities such as **Parametric**. Our emphasis on quality at a reasonable price has allowed our clients to enjoy market returns with a reasonable level of risk, and we will likely use the next correction in stock prices as an opportunity to add new names to our Buy List.

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Hamilton Point Investment Advisors, LLC is a fee-based investment advisory firm suitable for high net worth individuals, not-for-profits, retirement plans and corporations. We welcome comments or questions and can be reached at (877) 636-3765, or e-mail us at aburns@hamilton-point.com.

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