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Interest rates on wheels

It's an ill wind that blows no one any good, and the gale of radical monetary policy has showered its blessings alike on Silicon Valley and the Valley of the Venture Capitalists, wherever the latter may be. Enterprising people forever strive to produce a better mousetrap. Different these past 10 years or so is that the gizmo didn't have to make a profit. Free capital has the patience of a saint.

But maybe that's changing, to judge by the mounting travails of SoftBank Group Corp. (for a preview, see "Epitome of the cycle" in the issue dated Dec. 15, 2017). The mantra of the Japanese unicorn collector long had been growth first, profits later, if ever. "Ever," is a word we use advisedly, recalling Maximilian Tayenthal, co-founder of a German fintech company called N26, speaking in July to the *Financial Times*. Said he: "In all honesty, profitability is not one of our core metrics."

True-blue, market-determined interest rates focus the minds of the financiers of loss-making businesses on the cost of the red ink they buy. Arbitrarily low interest rates postpone the inevitable facing of that hard fact. But though interest rates cling to ground level, Mr. Market has had an epiphany. Bloomberg News last week couched the revelation thus: "In WeWork's Wake, Stock Investors Demand Profits Over Growth."

Investors may demand till they're blue in the face, but can bubble-era business models deliver? Uber can't and won't, Hubert Horan, noted aviation and rail consultant turned ride-share authority, told the *Grant's* audience at the Plaza last week.

Our speaker said he set about studying Uber because "its business model depended on everything we've learned about transportation economics being totally wrong." Whereas every big transportation company insists on the central control of labor and capital and on mobilizing sophisticated planning systems—the volatility of competition and demand requires nothing less—Uber is exactly the opposite. "They have no control of capital or labor," Horan said. "They have no data on the total market. They have primitive pricing tools compared to what the airlines had 30 years ago." He titled his remarks, "Uber's disruptive war on economic welfare."

Somehow, Horan proceeded, Uber came to decide that taxis, "the most fragmented transportation industry, magically became a winner-take-all industry. Demand peaks and back hauls are the biggest problem in every transport mode. Nothing in the Uber model addresses them at all. Variable pricing is valuable, but only, as you see with airlines, in that it increases both asset and revenue productivity. Uber pricing does neither and actually reduces total demand."

What is the value of a business that never pays a dividend? Horan steered clear of that speculative question, but his listeners could draw their own conclusions. The bottom line of his analysis, Horan went on, is that "Uber has no hope of sustainable profits in competitive markets. A company with $20 billion in losses in years six through ten is not rapidly growing into profitability like Facebook or Amazon. Uber's economics are totally uncompetitive. They are actually a higher-cost, less efficient producer than your traditional yellow-cab company.

"All of Uber's popularity and growth has been the result of massive, predatory subsidies that were used to drive out the more efficient operators," Horan contended. "The market shows no willingness to pay the true cost of Uber's services. Reversing these losses would be one of the biggest turnarounds in corporate history, and Uber doesn't have a profitable core to restructure around."

Horan called Uber a "totally unprecedented" corporate phenomenon, certainly no ordinary bubble creature. Skipping the standard entrepreneurial preliminaries of creating a legitimate product, the promoters raised $10 billion "pretty much out of the gate." Our speaker concluded his indictment with the charge that "Uber has been conducting a war on markets."

Hearing him, we thought of another kind of institution that's been warring on markets, specifically on price discovery. Central banks are these aggressors, and they created the speculative and interest-rate environment in which such shooting stars as Uber could flourish for a time. Maybe that time is ending.

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