

## Summer 2022

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The direness of the current US shortage begs the question: what did we do before baby formula?

Of course, many mothers breastfed. They also died at childbirth, at a much higher rate than now, or couldn't produce enough supply, or had to work to make ends meet. Some babies were unable to latch, and some were adopted.

So, what was the solution at a time when safe, nutritious formula didn't exist? Well, some babies were nursed by other mothers, friends or relatives, in their communities. The rich could retain a wet nurse, either a servant or a slave.

The riskiest alternative was bottle-feeding or spoon-feeding babies homemade concoctions, usually including animal milk and grains, among other things. In the days before refrigeration, antibiotics, and a host of vaccines, it's not hard to see the dangers.

It wasn't until 1846 that Justus von Liebig, a German chemist, created the first commercial formula, which appeared on US shelves in 1869. The products popularity drew competition from Nestle's Milk, among several others. Over time, nutrition scientists worked to create formulas more closely matching human milk, and companies like Mead Johnson joined the fray. The problem was, these products rarely met babies nutritional needs.

"Before the advent of modern formula (in the 1950s), a lot of babies died of illness or starvation because they couldn't breastfeed and alternative foods were not safe or adequate," said infant-feed historian Carla Cevasco.

The current US shortage has had parents scouring the internet (often paying exorbitant prices), driving hundreds of miles to search stores, and contacting regional milk banks. (Where, by the way, many donors have become heroes. Judy Cheung, a first-time mother, for example, has already donated well over 2,000 ounces to the New York Milk bank, according to *The New York Times*.) Most people have come to understand what Cevasco wrote in *Time*, "Modern Infant formula is a lifesaving marvel, not a luxury."

How did a country like the US get to the point where such a critical commodity—one that our babies rely on for health—became so scarce? The answer is far more complicated than whatever political talking points you're hearing.

The problem began with the start of the pandemic, when parents began to hoard formula in order to prepare for the worst. (Remember the toilet paper spree?) Once parents had stockpiles, and calmed, demand ebbed, and manufacturers began producing less product.

When pandemic concerns and rules eased, manufacturers began ramping back up. In January, as you've likely heard, an Abbott-owned formula plant shut down due to bacterial contamination. What exacerbated this is the company accounts for 43% of formula sales in the US. It's not a monopoly, but the industry could be considered an oligopoly. Four companies—Abbott, Mead Johnson Nutrition, Nestle USA, and Perrigo—make up 90% of the market share. To make matters worse, Abbott, according

to *Politico*, is the sole contractor of formula in 49 states for WIC, the federal program many low-income families rely on, through vouchers, to get formula.

In May, when President Biden launched the awkwardly phrased “Operation Fly Formula,” projected to import, via commercial aircraft, the equivalent of 17 million 8-ounce bottles by the end of June. Prior to that, however, little of the product had been imported. First, FDA guidelines are strict, more so than nearly all foreign food safety agencies. Trade agreements, such as USMCA (the revised NAFTA), high tariffs (14.9% to 17.5% on most favored nation’s imported formula and 25.1% on the rest), and the aforementioned WIC further discourage foreign manufactures from entering the US market.

Under the best of economic climates, Abbott’s shutdown would have been a big problem. The supply chain issues made it a full-blow crisis, adding to the other well-known pandemic related shortages—vehicles, farming chemicals, and tampons, to name just a few.

Pointing out pandemic-related economic issues has become a bit like listening to Lynyrd Skynyrd’s “Free Bird.” Just when you think there’s no more, another guitar riff begins.

Here’s a couple more: the labor shortage and rising inflation. We’ve discussed both in recent *folios*, but it’s worth updating the latter, which has relegated stories like the formula crisis to the back pages. (Not surprisingly, given the price of gas, a commodity with far greater demand.)

In the spring, we explained the causes—those supply chain issues, too much money and not enough goods and services, the war in Ukraine—and some of the things being done to combat it. Since then, as expected, the Federal Reserve and Bank of Canada embarked on interest-rate increases (0.75% in the US and 0.50% in Canada) and quantitative tightening. This brings the base rates to 1.75% and 1.5%, respectively.

These hikes have far-reaching implications in each country. Mortgage rates are now around 6%, from 2.75% at the beginning of the year. This has publications like *Fortune* declaring the pandemic housing boom over. At the same time, the bond market and equity markets have had sharp sell-offs.

Is a recession in the cards? As the pandemic and war in Ukraine have shown, anything is possible. But current signs are not indicating a recession. (It’s important to note that GDP growth is not the only measure of a recession – the signs include employment, consumption, and industrial production to name a few.) Inflation should peak soon, though likely taking the rest of the year and some of next to get back to the target rate of around 2%. The increase in the supply of workers is easing wage growth (the yearly average hourly earnings fell to a still inflationary 5.2%, from 5.5%). In July, the Fed may decide to only raise the key interest rate by a half percentage point, rather than the tentatively planned three quarters point hike, a move the stock market would welcome. COVID hospitalizations remain low. Restaurant visits, among other entertainment, continue to settle around pre-pandemic levels.

There’s a lot of opportunity out there. Government bonds, after years of paltry yields, are now paying 3%. Corporate and high-yield bonds are paying even more. Equities have slashed their stock prices 10-20% since the beginning of the year.

We understand why the good news flies under the radar—it doesn't make filling your tank less painful, or make baby formula readily available. Things aren't perfect. But they don't need to be for markets to start recognizing future potential. They just have to stop getting worse. And there's plenty of indications that's happening.