Ad-tention

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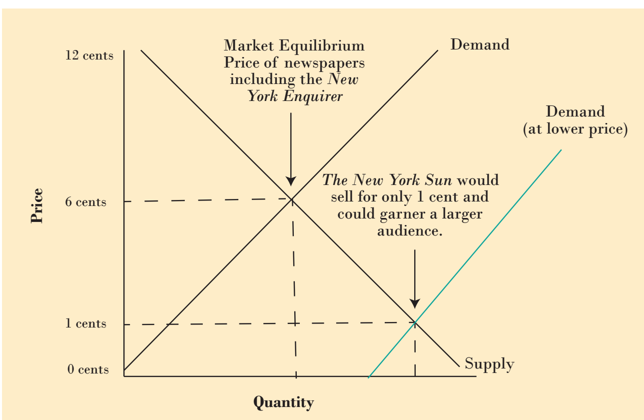
In the fall of 1833, a young man had a revolutionary idea that would change the world. His name was Benjamin Day, and he was captivated by the entrepreneurial spirit of the early Industrial Revolution. Day owned a small print shop that was struggling, so he devised a plan to keep his presses running: he would start a newspaper. Day named it *The New York Sun*, and to boost sales he sold copies for only a penny (much less than it cost to produce), while other well-established papers such as the *New York Enquirer* were selling for 6 cents. It appeared to many to be a money-losing proposition doomed to fail, but instead, it was vastly successful.

What Day achieved is illustrated in the chart below.



As the chart shows, Day was selling newspapers for 1 cent, while the market set the price at 6 cents, where supply and demand intersect. Economics teaches that the price of an item is determined where supply and demand intersect, so that a company can cover its costs. If Day sold his newspaper for only 1 cent, he could sell a lot more copies but would be losing money on each one sold. However, Day wasn't concerned about making a profit from selling the papers. Instead, he wanted to sell his readers' *attention*, and the bigger the audience, the more he could charge advertisers who were eager to pay a premium to get in front of the largest audience possible. What Day realized was that the money he lost in selling copies could easily be recouped by selling space in the paper to advertisers looking for a large audience. (This is how news corporations still operate today). The trick for Day was to

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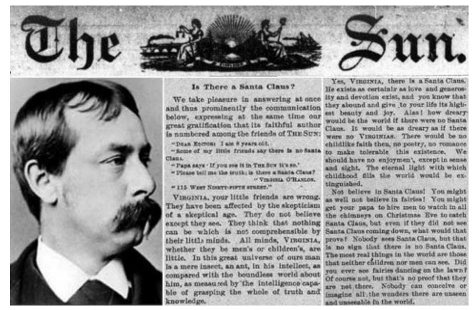

On September 21, 1897, *The New York Sun* published what was to become the most famous editorial ever written. It was a response to a letter sent by 8-year-old Virginia O'Hanlon. The 1897 editorial with the famous line "Yes, Virginia, there is a Santa Claus" was their most popular piece, and has been reprinted thousands of times throughout the years.

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find a way to grab people's attention. To do so, his newspaper would bend the limits of reputable journalism by publishing such stories as the discovery of life on the moon and accounts of lurid and comical material from New York's police court. Day is considered the pioneer of "fake news" and one of the first "attention merchants."

Day created the idea that the customer is the product. Almost 200 years later, companies like Google, Yahoo, Facebook and Twitter follow in his footsteps, making billions of dollars each year selling their customers' attention and using their personal information to aid advertisers. However, today's attention merchants are much more advanced. By utilizing various behavioral marketing tactics, these firms develop sophisticated tools to not only grow their audience, but to also alter consumer behavior. For these companies to prosper, they must expand the number of users and the amount of time each user spends using a specific application. As Day demonstrated, one can sell a newspaper for less than it costs to produce if they can also sell access to their customers. By offering their services for "free," today's social media companies can build much larger audiences, as the above chart illustrates.

Once consumers are using their service, these companies will often implement behavioral marketing strategies to alter users' behavior. The most obvious one is enticing people to spend more time using the service—social media companies have excelled at this. Not surprisingly, Americans now spend an average of 2 ½ hours per day on social media. Other schemes include targeted ads and identifying certain demographic information, along with various nefarious actions that aim to alter behavior, called "priming." According to the Nobel Prize-winning work of Daniel Kahneman and other behavioral economists, an individual's decision-making can be affected by the words and images they have seen beforehand. This is what makes the current technology such an effective tool. "Adhesiveness. That's what the technology aspires to achieve," wrote Ayad Akhtar in the December 2021 issue of *The Atlantic*. "The longer we stick around—on YouTube or Facebook, on Amazon, on the *New York Times* app—the deeper we scroll, the greater the yield of information, the more effective the influence. We are only starting to understand just how intentional all of this is," he continued. The endgame is to keep us engaged and glued, so as to alter our behavior.

As if out of a science-fiction novel, the aim of many of these apps is to alter users' decision-making while keeping them oblivious to the priming that is occurring. As the services are offered for free, the consumer feels as if there is no cost to them when in reality, the opposite is true! The billions that these companies make come from users' lost privacy, and the opportunity cost each one incurs. In 2020, the average user spent 325 hours on Facebook alone. If we wanted to place a financial value on this time, we could use a rate of $15 per hour, which would equate to $4,875 per year.

The problem for the attention merchants and the advertisers who pay them is that once people realize that their attention is being disrupted by ads, they develop very good tools for tuning them out. This is why the tactics being used have grown from subtle to outright invasive, sometimes crude, and too often appeal to our most basic instincts. In his entertaining book, *The Attention Merchants*, Tim Wu reminds readers that up until 100 years ago, advertisements were predominately encountered outside of the home. Today, the average person will see up to 10,000 advertisements per day! (If you would like a copy of the book, we would be happy to send you one).

Investors are not immune to outside influences affecting their decisions. In fact, there is a name for it: "noise." Noise is the information in the market that distorts underlying trends and contributes to the stock market's volatility. Often, a disturbing story on a "free" news service will spark investors' fears and cause a selloff, only for the story to later be refuted, which then causes a market rebound in the following days. Most recently, the stock market fell on fears of the Omicron virus in early December, only to rebound the following week.

There are several ways to measure noise in the market. We have a database that is quite complicated that enables us to do this very thing, but there are simpler models that can provide a rough estimation. Many years ago, Jack Bogle, the founder of Vanguard Investments, showed me his "simple model" for measuring noise. His model compares the current S&P 500 Index price/earnings (P/E) ratio to its historical average. (The P/E ratio indicates what one will pay for a share of stock for the annual earnings that it will produce). Mr. Bogle's model helps determine how much of the market's value is the result of earnings growth versus speculative growth, which is often the result of noise. From December 31, 1990 to June 30, 2021, the S&P 500 had an average P/E ratio of 25.0. On June 30, 2021, the P/E ratio of the index was 27.1, slightly higher than its historical average, indicating that the market was overvalued. However, earnings are expected to grow strongly in 2022. If we use earnings estimates for 2022, the P/E ratio of the S&P 500 would be 22.25, which is 11% below the historical average, providing a compelling argument that 2022 could be a good one for the market.

For investors, knowing how to recognize noise in the market is critical. The key is accepting that too often, those who report the news (whether political or financial), are actually publishing/media empires looking to build bigger audiences by grabbing our attention any way they can. This is why calculating the intrinsic value of stocks is more important than ever. Today's news is often the work of modern attention merchants who see us as the "product," but with the right tools we can learn to tune them out, regardless of how noisy they have become!