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SA INC

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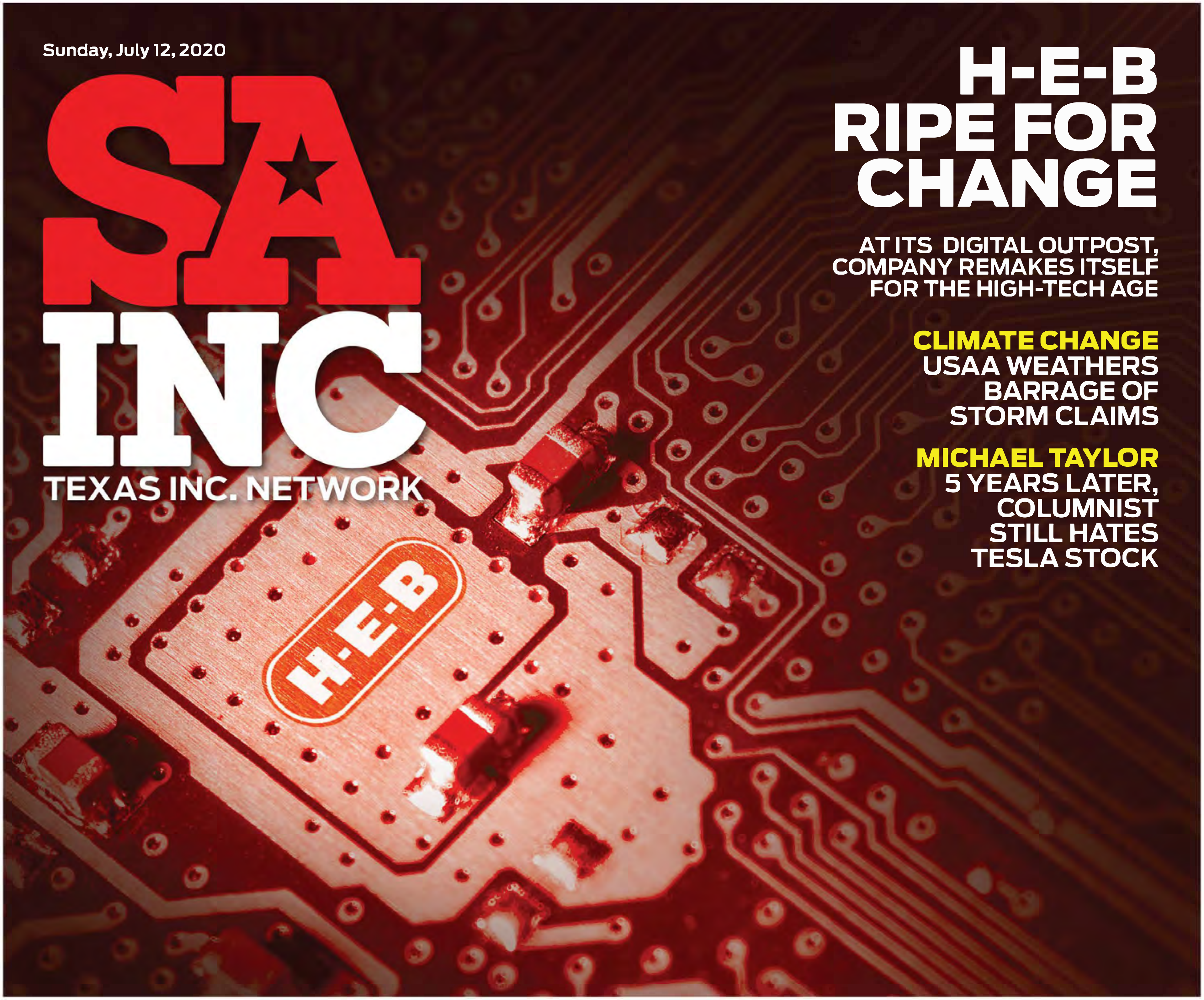

H-E-B RIPE FOR CHANGE

AT ITS DIGITAL OUTPOST, COMPANY REMAKES ITSELF FOR THE HIGH-TECH AGE

CLIMATE CHANGE
USAA WEATHERS BARRAGE OF STORM CLAIMS

MICHAEL TAYLOR
5 YEARS LATER, COLUMNIST STILL HATES TESLA STOCK

EDITOR'S LETTER

I'm pleased to introduce our newest weekly product focused on San Antonio's rapidly growing business community.

We'll publish SA Inc. every Sunday – a standalone section that'll highlight the news and data, trends, executives, entrepreneurs and companies that make our city a great place to do business.

SA Inc. features will include:

- Profiles of business leaders
- Investment advice
- Coverage of real estate deals and trends
- "Movers and Shakers," focusing in on company promotions and appointments
- News about the military's influence on our businesses and economy
- Business travel tips and reviews
- Property transactions
- Information on lawsuits and other legal actions

SA Inc. will be available in print and online. Our newsweekly will appeal to the C-Suite, business owners and managers, entrepreneurs, investors – and everybody else who wants to know the latest on business in San Antonio.

I look forward to hearing your feedback on our new journey.

GREG JEFFERSON
BUSINESS EDITOR

RESTLESS CITY

Presented by: **Your Company Here**

USAA is feeling the heat from climate change

GREG JEFFERSON
Commentary

Associated Press file photo

Wildfires are among the natural disasters increasingly gnawing at USAA's bottom line.

Last March, one of USAA's social media producers posted this blurb on Twitter: "During the past five years, floods have affected every single state – even those considered low-risk."

The tweet invited readers to use a tool on the San Antonio insurer's website to gauge their flood risk.

You've probably already guessed how it played out. A couple of the more predictable responses: "No climate change though!" and "Funny so much cold and snow in a warming climate."

Climate change deniers are going to deny, and some of those who accept that global warming is real are going to be zealots – and will come off just as cartoonishly as their foils.

Whatever.

What's key is that storms, flooding and wildfires have been getting worse, and USAA, which employs 19,000 people at its North Side headquarters-fortress and other local offices, has been trying for years now to adjust to the new reality. Just like every other major insurer.

Of the 10 costliest wildfires in U.S. history, as measured by insured losses, the top five broke out in 2017 and 2018, according to the Insurance Information Institute. The worst was the deadly Camp Fire in Northern California in November 2018.

Natural catastrophes bruised USAA's results in 2018. Profits slipped from $2.4 billion the year before, even as revenue hit a record $34.2 billion. The company will release its 2019 numbers in the spring.

The 2018 results, however, aren't a clear window into how climate change is affecting USAA's property and casualty business. Those figures include the performance of the company's investment management arm and its federal savings bank, as well as its life insurance line.

And there's this: USAA isn't a publicly traded company – it's a member-owned mutual insurer – so a detailed financial picture is hard to come by.

But we know the insurer paid more than $2 billion in claims in 2018 for the Camp Fire and other wildfires, two hurricanes and other catastrophes. As Express-News Staff Writer Patrick Danner reported, it was third straight year for USAA in which claims stemming from natural disasters surpassed $2 billion.

When USAA employees learned a year ago that their bonuses would drop to 14.8 percent of annual pay from 16.2 percent the year before, their bosses cited disaster claims as one reason.

The latest bonus, announced in January, slipped again, to 14.5 percent, the lowest since 2008.

"Overall performance, to include but not limited to financial, is part of the consideration by the board" in determining the size of the annual bonus, USAA spokesman Matt Hartwig said.

Clearly, no one is weeping over USAA employees' slightly diminished bonuses. That's because, unlike many other San Antonio-area workers, *they're getting bonuses*.

The annual payout, in addition to the $2.4 billion that USAA returned to policyholders last year in rebates and dividends, is a sign of the company's financial strength. So is its net worth of $35.5 billion.

And no one's weeping for the property and casualty insurance industry as a whole. Insurers made combined profits of $48.1 billion in the first nine months of 2018, their second-biggest haul since 2008.

But just as the fact that it's still snowy in some places doesn't mean global warming is a hoax, the insurers' net income doesn't mean that storms and wildfires aren't becoming more perilous. The effects of climate change are gnawing at their core business.

Insurance companies have responded by hiring more climate experts, changing their catastrophe models and pushing up premiums in higher-risk communities. USAA probably has, too, but Hartwig declined to discuss specifics, saying, "We view our efforts as competitively sensitive."

Moody's Investors Service, for one, still likes USAA. In a May 8 report, the bond-rating agency gave the company's insurance business a rating of Aaa, or exceptional. It cited USAA's "efficient operations and its strong balance sheet," as well as its "market leadership" in serving active-duty and retired military personnel and their families.

But Moody's analysts included this caveat: "Tempering these strengths are USAA's volatile (property and casualty) results in recent years, reflecting industry-wide catastrophe losses and fluctuating personal auto loss cost trends."

The fallout from global warming is obviously a greater threat to humans than to corporations. But San Antonio's second-largest employer – a big part of whose business is tied to the weather – is feeling the heat.

greg.jefferson@express-news.net

THE SMART MONEY S.A.

Presented by: **Your Company Here**

5 years later, Tesla still not a good stock to own

MICHAEL TAYLOR
Commentary

Ringo H.W. Chiu / Associated Press

Tesla CEO Elon Musk's company has never turned an annual profit in nearly 10 years.

The most important rule for writing a business column – at least my most inviolate rule – is to never, ever forecast or make "market calls" on individual stocks.

I have broken this rule only once in my 5½ years. It's time to break my rule again. On the same stock.

Some background: I last tucked my first-and-only individual-stock forecast into a column in March 2015.

The point of that 2015 column was to highlight the unpleasant fact that "sin-investing," especially in a nasty tobacco company such as Altria (formerly known as Philip Morris, ticker symbol MO) has been extraordinarily profitable over the past 40 years.

But that wasn't my stock forecast. Instead, I contrasted MO with green-tech market darling Tesla (ticker symbol TSLA), the sexy electric-car company that combines virtue-signaling for reducing your carbon footprint with 0-to-60 acceleration in 1.9 seconds.

I wrote the following about Tesla in March 2015: "Tesla Motors, to name one public company that I'm reasonably certain will be dead in five years, despite its $25 billion market cap, is an innovative company. But that doesn't make it a good stock to own."

Then, to further metaphorically point to the bleacher seats while stepping into the batter's box for my inevitable home run, I wrote, "Would a few people mark their calendars for five years on Tesla and let me know how I did with my call? Because I AM SO RIGHT."

Anyway, time flies. It's five years later.

I'll save you the hassle and let you know that Tesla stock increased 170 percent since then, from $200 per share at the time of my home-run call to $569.56 per share at Wednesday's close. The market cap has expanded from $25 billion to $97 billion. It's up 30 percent just this year. Tesla will announce fourth-quarter 2109 results on Wednesday.

Having broken my inviolate rule five years ago, it is only right and just that I have both my hypocrisy and terrible market call publicly mocked.

But that's not the main lesson you should take away from this shameful episode. The main lesson is that you, too, should never forecast individual stocks.

You will be emotionally invested in a way that hurts your chances of building wealth. You will buy, or sell, that stock too frequently. You will let fear and then greed cloud your judgment.

You will look up that stock price exactly at the moment when you should be enjoying your daughter's ballet recital. (How many times do I have to tell you to put your phone down?) You will read headlines that confirm your preconceived biases, and you will discount headlines that contradict them.

You can guess how I know all these things about you.

Beyond the emotional reasons, you should avoid forecasting because you will also be wrong. You will even be wrong for all the right reasons. Like me.

Tesla, by all rational analyses, has always been a stupid stock. It's been overvalued forever. But as the Wall Street phrase goes, "The market can remain irrational longer than you can remain solvent."

I was correct about Tesla then, and I'm still even more correct! I will now double down on all of my errors.

Unlike, say, software technology companies that enjoy infinite scalability, building an auto manufacturer is highly expensive to scale. It takes cash. Tesla has burned billions in cash to build plants in Nevada and Shanghai. The competition from other auto companies is intense and global. Regulation is massive. Innovation, for which Tesla is known, is expensive to implement. The company has nearly run out of money more than once in the past five years, even by the admission of its CEO/evangelist Elon Musk.

And then there's Musk himself. Ugh. As clearly brilliant and visionary as he is, he can't stop himself from tweeting nonsense, earning rebukes and a $40 million fine from the Securities and Exchange Commission, and lawsuits from fights he picks unnecessarily. He also employs his knack for distracting the media to change the subject whenever they attempt to ask about Tesla's lack of profit.

Oh, yeah, and about that profit. Tesla has never turned an annual profit in nearly 10 years as a public company.

Tesla's market cap at $98 billion is larger than Ford and General Motors combined.

Let's compare those companies to Tesla. Ford sold 5.9 million vehicles in 2018 for a profit of $3.8 billion. General Motors sold 8.4 million vehicles in 2018, earning a profit of $1.9 billion. Tesla, which has never turned an annual profit, sold 367,500 cars in 2019.

Tesla has sold 891,000 vehicles since it began manufacturing. Total. In other words, Ford and General Motors sell more cars in any given month than Tesla has ever sold. I could go on, but you get the idea. Tesla is a stock that mostly exists in our collective imaginations.

It turns out that Wall Street pros mostly agree with me about Tesla. It is the most "shorted" large stock on the U.S. stock market, meaning sophisticated investors have bet against the share price, finding it as absurd as I do.

Shorting means hedge funds have sold shares at current prices in anticipation of buying back shares when they drop in the future. Shorting Tesla has been, as you can imagine, one of the most spectacularly unprofitable trades of the past few months.

Some people never learn. Like me and you, the pros also shouldn't be forecasting individual stocks.

THE SKYLINE

Presented by: **Your Company Here**

Austin developer moves into Pearl area

By Madison Iszler
STAFF WRITER

Courtesy of the Historic and Design Review Commission

Sabot Development has proposed constructing a 10-story mixed-use development with 325 units near the Pearl.

An Austin firm wants to build a 10-story mixed-use development with 325 units across the San Antonio River from the Pearl.

Sabot Development is proposing putting the project on about 1.5 acres bounded by East Euclid, East Myrtle, East Elmira and East Locust streets. It would include 14,000 square feet of retail and about 400 parking spaces.

The development, expected to cost upward of $100 million, is the firm's first in San Antonio.

Jim Young, a San Antonio native and president of Sabot, said he visited the Pearl complex several years ago and has been eyeing the area around it.

"We see multifamily as a future for a lot of people," he said. "A lot of baby boomers and millennials alike, they want to enjoy the camaraderie of living with a diverse set of neighbors … and they seek to live in apartments because of the high level of experiences they get with their neighbors."

The firm's plans involve demolishing several buildings on the site, which currently is home to coworking business Cubes at the Quonset, a storage facility, a construction company, a real estate office and a food truck. The project excludes lots at East Myrtle and East Elmira.

Sabot is under contract to buy the land. The firm expects to close next year and start work in the second quarter of 2021, Young said. It currently is not seeking incentives for the project, he added.

The city's Zoning Commission OK'd a request Tuesday to rezone the property to allow for the multifamily development with retail space. Last month, the city's Historic and Design Review Commission gave its initial approval to the firm's plans.

Several neighborhood residents and property owners spoke at the Zoning Commission meeting, with some voicing their support for the project and its design and others expressing concerns about how it would fit into the area and parking.

"The rezoning is quite inconsistent with our neighborhood in height and density," said Scott O'Brien, who lives in the area and added he was worried about parking and privacy.

Richard Moore, president of the Tobin Hill Neighborhood Association, said Sabot representatives met with local residents and asked for input. The project will be "a first-class architectural development," he said.

Pipe Dream Hotel?

A New York-based company plans to open a 217-room, 25-story hotel dubbed Dream San Antonio along the River Walk.

Whether it's nothing but a pipe dream remains to be seen — the company won't reveal who's developing the project — or where.

In an announcement this week, Dream Hotel Group described the boutique hotel as "the centerpiece of a large mixed-use development that includes office space and private residences." The hotel itself is to feature a rooftop pool deck, two street-level restaurants, fitness facilities, meeting space and a bar and lounge.

The company declined to disclose an address or name the local developer handling the project. The developer still is raising funds for it and owns the land the hotel will be built on, spokeswoman Katie Fontana said.

PAID ADVERTISING

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IN SAN ANTONIO

SAN ANTONIO EXPRESS-NEWS MEDIA

Raj Ramanan

San Antonio Express-News names chief revenue officer. Ramanan, previously served as president of HYFN Local, an ad agency owned by Irving-based Nexstar Media Group, where, he said, he increased revenue by double digits, returning the company to profitability. Before that, he worked for Disney, investment bank Bear Stearns, private equity firm KKR and consulting firm McKinsey. Ramanan also founded and sold a search app startup with a friend.

ACCOUNTING

Professional

Christopher Davis

Christopher is a shareholder with Sol Schwartz & Associates, P.C. and has been with the firm since 2008. Christopher practices in various areas of public accounting including tax compliance and consulting for individual, corporate, S-Corporate and partnership taxation. Christopher is a graduate of the University of Texas at San Antonio with B.B.A. in Accounting and a Masters of Accountancy with a concentration of Taxation.

Movers and Shakers don't need to brag. Let **Texas Inc.** do it for you.

Submit your announcement today!

THE WARY TRAVELER

Planes gets cozier with more seats, tighter legroom

By Randy Diamond
STAFF WRITER

Fort Worth Star-Telegram file photo

Dallas-based American Airlines is trimming the legroom in coach to 30 inches.

If your knees hit the seat in front of you on your next American Airlines flight, rest assured – you're not growing. Passengers' legroom is shrinking.

American Airlines, the world's largest carrier and the second largest at San Antonio International, is in the midst of a multiyear overhaul of its entire fleet. That includes increasing the number of seats on each plane, with the obvious result: less space for passengers.

The Dallas-based airline is trimming legroom in coach to 30 inches, which is the amount of space you have before your knees bump into the seat in front of you.

Airlines have been cutting legroom for years, and cramped conditions have become the norm. Legroom of 31 to 32 inches is standard on major carriers. While 30 inches isn't unheard of, no airline has revealed plans as ambitious as American's to go below 31 inches on domestic routes.

American's legroom does have an exception: flights between New York and Los Angeles and San Francisco.

You won't be able to pay your way out of the situation, at least not entirely.

American's Main Cabin Extra seats, which travelers can purchase for an extra fee or frequent fliers receive for free, still will be available – but their legroom is shrinking, too. Previously, these seats had 6 inches of extra legroom; on some planes, that's being cut to 33 total inches, the airline says.

Even first-class space is being reduced, a reduction to 37 inches from 40 inches on some American aircraft.

"If you are going to fly American in upcoming months, expect to be cozy with your neighbors," said Brian Sumers, senior aviation business editor at travel industry website Skift.

At San Antonio International, American mainly flies two plane models – the Boeing 737 and the Airbus 321. The program to increase the number of seats on the Boeing 737 from 160 to 172 began several years ago. The retrofits were suspended over the summer because America needed all its planes to make up for the grounded Boeing 737 Max jets.

American spokeswoman Andrea Koos said the retrofits on the Airbus 321 began recently – only one plane has been refurbished. The Airbus overhaul will add up to nine seats, for a total of 190 seats.

American has nearly 1,000 planes in its fleet, and airline officials have not said how long it will take to complete the renovations.

The carrier also is squeezing restroom space. American's new configuration reduces the restroom size in coach to 24 inches, taking away 7 inches, to help accommodate the additional seats.

"You really have to practice yoga or gymnastics to squeeze in," said Scott Mayerowitz, executive editorial director of the travel website Points Guy.

Less legroom and tighter restrooms aren't the only, or even most pressing, concerns for passengers on American in recent months.

A labor dispute between the airline and its mechanics union led to an unofficial work slowdown this summer as mechanics refused to certify that planes were in working order, leading to hundreds of cancellations.

June was an especially bad month at San Antonio International for American, with 5.31 percent of its flights canceled, or 39 of 735, the Federal Bureau of Transportation Statistics reports.

In comparison, Delta Air Lines and United Airlines each canceled two flights that month.

The number of American cancellations in August dropped after a federal judge ordered an injunction against the mechanics. The carrier still canceled 15 flights, or more than 2 percent of its flights that month, at San Antonio International.

Throughout its entire system, American canceled 2.9 percent of its flights in August, the worst of any airline besides Spirit Airlines, which had a 3 percent cancellation rate.

"Unfortunately, during the summer there was an illegal work action ... and it slowed down our airline," Derek Kerr, American's chief financial officer, said at a Skift travel conference last month.

According to data provider Flightaware, American flight cancellations at San Antonio International in September declined to 3.

Koos said in a statement, "(We) have worked to improve our operation" and that on-time arrivals have been increasing.

American has been near the bottom of airlines in terms of on-time performance in the latest data from the Bureau of Transportation Statistics. More than 14 percent of its flights departing out of San Antonio International were late by more than 15 minutes in August. However, Flightaware data show American's late flights had declined to 10.7 percent in September.

Another problem area for American over the past year has been damaged and lost checked baggage. The company scored badly compared to other airlines between January and August, federal statistics show. Of the 17 carriers tracked by federal officials, American consistently placed in the bottom three in the eight-month period. It was last among major airlines.

In June, more than 1 percent of checked baggage was reported delayed, lost, stolen or broken into.

Asked about American's quality of service, Koos noted the retirement of Kerry Philipovitch, senior vice president of customer experience, and the appointment of new officials to oversee operations and network strategy.

Joe Brancatelli, who runs the business travel website Joe Sent Me blames American's problems on top executives like Kerr and his boss, chairman and CEO Doug Parker, both of whom were the top executives at US Airways before it merged with American in 2013.

"We all know how they ran US Airways – it was a terrible airline," Brancatelli said, adding that US Airways was known for poor customer service and uncomfortable planes.

While passengers are losing legroom, the renovated planes also include larger luggage bins and a power outlet at every seat. Brancatelli said the larger bins speed up boarding and end fights over limited luggage space. And if American speeds the boarding process, it might be able to add an extra flight to an aircraft's schedule, increasing profits.

"Its all part of an effort to maximum revenue, " said Brancatelli. "Its great for American Airlines but not as good for the customer."

COVER STORY

Wth digital outpost, H-E-B embraces shifts in shopping

By Dwight Silverman
STAFF WRITER

AUSTIN — When you walk into the building at 2416 E. Sixth St. on this city's trendy East Side, it's immediately clear that it's a tech workplace. Visually, it's almost a cliche.

Scores of young women and men are glued to computers — many with two or three monitors — in sprawling, open-concept office areas. Coffee and snack bars with free food and drink abound. There's a rock-climbing wall in the gym and wall-mounted bicycle racks. Conference rooms have red or green lights to signal if they are occupied or available.

Creature comforts are everywhere. Carts in unisex restrooms are loaded with mouthwash, bobby pins, hair ties, moisturizer, even individually wrapped toothbrushes in multiple colors.

Oh, and don't forget the beer. Look to the right once you've cleared security and there's a bar sprouting multiple taps in front of a neon sign that reads "Beer Friday." It's lit up at 4:30 p.m. on the last day of the workweek, when the 400-plus coders, developers and marketers in the building are more than ready to refresh and relax. (There's a kombucha keg for teetotalers.)

That all this is found in an Austin technology hub is not surprising. What may come as a shock is that the company that leased this 81,000-square-foot former recycling center is H-E-B, Texas' biggest regional grocer. Here — on a street where its neighbors are software development firms, graphic design houses and trendy restaurants frequented by digital-native millennials — the supermarket chain has drawn a tech line in the sand.

"It's a no-brainer to set up a presence here," said Jag Bath, H-E-B's chief digital officer, pointing out that Austin, a major outpost for Google, Facebook, Apple and others, has a critical mass of technology talent.

"When you have conversations about tech, it's all about the talent," he said. In other words, to compete for that talent with the tech giants that lumber around Austin, you need a workplace as cool as theirs.

To be clear, only half of the building is occupied by H-E-B. The rest of its real estate belongs to Favor, an on-demand delivery startup that H-E-B bought in early 2018. Bath was its president and CEO, a title he retains. At the time, it was H-E-B's first-ever acquisition, and it was a bet that combining a pure technology company with a venerable grocery retailer would jump-start the latter's efforts to survive and thrive as its business undergoes digital disruption.

"You can learn a lot from a pure-play technology startup and apply that to the core business," Bath said. "That's exactly what we have done."

Embracing change

The grocery business has long had a reputation of being resistant to change, but that may not be deserved. The industry has adopted technologies that made sense as they came along — think self-checkout kiosks or the computer-managed inventory control pioneered by Walmart. In Europe and Japan, online shopping and on-demand delivery have been popular for a decade, even though startups offering it fizzled in the U.S. in the dot-com bust of the early 2000s.

But nothing sounded a digital

H-E-B continues on J14

NC.

Young men and women work seem glued to their computers in the sprawling, open-concept office areas at H-E-B Eastside Tech Hub in trendy East Austin.

Godofredo A. Vásquez / Staff photographer

H-E-B from page J12

clarion call like the $13.4 billion acquisition of Austin-based Whole Foods by online retail goliath Amazon in mid-2017.

"Amazon buying Whole Foods woke a lot of people up," said Katherine Black, a principle analyst for consumer and retail strategy at KPMG. "Amazon was a big catalyst in the marketplace."

With its expertise in online shopping, its emphasis on rock-bottom pricing and its ability to leverage its Prime membership program, Amazon instantly became a force to be reckoned with. While grocery companies had already been dabbling in online initiatives, the acquisition of Whole Foods by the company upending retail created a new sense of urgency.

It was against this landscape that H-E-B bought Favor Delivery in February 2018 for an undisclosed amount. At the time, Favor claimed it was the first on-demand delivery service to become profitable. Founded in 2013 in Austin, it has 80,000 contract "runners" who bring food from restaurants and goods from retail stores to homes in 130 cities across Texas.

Favor continues to operate as an independent entity, but it's also how H-E-B handles deliveries to customers who order online.

And if you want to see just how Favor has impacted H-E-B's approach to technology, you need only download the grocer's updated smartphone app released in December. "My H-E-B," available for both iOS and Android smartphones, is a sleeker, more capable app than the one it replaced.

Before, if you wanted to order groceries to be delivered via the previous version of the app, you were kicked out to H-E-B's website to complete the process.

Annie Mulligan / Contributor

Employees use an program to fulfill curbside orders. For custotmers, H-E-B also is testing an app allowing cashierless checkouts.

Now, you can order groceries and arrange delivery or a pickup with the company's Curbside service in the app itself. It also lets you manage digital coupons, compile a grocery list and more.

Bath said this is just "the first phase" of the new app and more features are coming. That might eventually include being able to check out without going through a cashier or even a self-checkout kiosk.

H-E-B has another smartphone app called H-E-B Go that's used with a handful of stores testing cashierless checkouts. Its users scan barcodes on items on shelves or from scales used to weigh produce and bulk items. They proceed to a checkout station if a purchase includes alcohol or involves coupons. Payment for the groceries is made on the phone, and the customer shows a receipt on the phone's screen as they exit the store.

Most of the H-E-B Go trials are at stores in San Antonio and Austin.

The focus of work at the Eastside Tech Hub, as the Austin center is called, is on the app and the technology behind. But it also serves as a showcase to attract talent in the hypercompetitive Austin tech job market. The building is designed not just to provide the kind of amenities tech workers have come to expect,but to also do it with a flair that's distinct to Texas and H-E-B.

For example, there are multiple food bars throughout the building, each one themed around H-E-B's four grocery brands — the core H-E-B store; Mi Tienda, which targets the Latinx market; Joe V's Smart Shop, a budget brand; and Central Market, the company's answer to the higher-end Whole Foods. While the Central Market food bar features locally roasted espresso beans, the Joe V's has jars full of M&Ms.

Even with these perks, why would a software developer want to work at H-E-B instead of, say, Google or Apple?

"This is an industry that is ripe for disruption," Bath said. "That's very appealing to someone like a software engineer who's interested in e-commerce."

Shopping ease

What happens when you order groceries through the H-E-B app or website for pickup or delivery involves both internet wizardry and old-fashioned retail logistics.

At the company's new Buffalo Heights store on Washington Avenue in Houston, online orders appear on a computer screen in an area packed with rows of tall carts. At another end of the room is a cooler with more carts inside. Managers like Shannon Canty monitor the screen. When customers place an order, they can pick a time for pickup or delivery. Canty serves as triage, assigning employees dubbed "personal shoppers" to fulfill orders.

"The busiest times are between 7:30 and 10 a.m., and 3 to 7 p.m.," Canty said. "We can process up to 60 orders at at a time."

On a cold, blustery December day, personal shopper Brenda Flores worked the produce section, putting fruits and vegetables into the compartments of a cart she pulled from the cooler. The chilled shelves of the cart — which can hold orders for a dozen customers — help keep the produce fresh.

Elsewhere in the store, other personal shoppers — wearing T-shirts that are the same blue as Favor's delivery drivers — are fulfilling other parts of customers' online orders. An order may have three or four shoppers working it, and then its items are bagged and combined for delivery or pickup.

H-E-B now has 200 stores statewide that offer Curbside, its pickup service. Customers drive into a space near the Curbside entrance and send a message via smartphone that they've arrived. One of the personal shoppers then brings the shipment to the vehicle. For delivery, the order is whisked away by a Favor runner.

Scott McClelland, H-E-B's president, previously managed the grocer's Houston region. He said the company's approach has been to use technology to provide convenience to shoppers. And customers are increasingly willing to pay the fees associated with pickup and delivery for online shopping.

"One of the things we know our customers want is for life to be simpler," McClelland said. "There are so many pressures on our time. There's a difference in the way our generations have looked at the value of time. My father would happily spend 10 minutes to drive further to save

H-E-B continues on J16

Godofredo A. Vásquez / Staff photographer

H-E-B's Eastside Tech Hub occupies half of the building. The rest belongs to Favor, an on-demand delivery startup H-E-B bought in early 2018.

from page J14

$5 on cheaper gas. Today, his kids will spend $10 to order food to be delivered rather than driving to pick it up."

Technology is also used in the store to help H-E-B understand what works to sell groceries.

McClelland said every display and every 4 feet of shelving in the stores have bar codes. Managers in charge of that department can scan the code with their smartphones and see how many items have been sold from there.

"They can see what they made on that display, and whether things are selling or are just gathering dust," he said, adding it lets the managers see what's happening without consulting a computer in a backroom.

"We want them on the floor, we don't want them stuck in the office," he said.

H-E-B, of course, is not the only grocery operation adopting technology at a rapid clip. Kroger, the biggest grocery chain in the country, made a splash in Houston last year when it kicked off a test of driverless delivery vehicles with a company called Nuro. The fleet of Toyota Priuses topped by lidar sensors have become a common site on some Houston streets.

H-E-B has its own autonomous delivery trial, though it's on a much smaller scale than Kroger's. When you talk to McClelland about autonomous delivery, he doesn't wax as enthusiastic as other grocery executives. He says the average e-commerce order is twice as big as the average in-store purchase, and that amounts to a logistical challenge.

"What happens when an autonomous delivery vehicle arrives and the customer has to walk out to it and pick up 20 bags?" he asked, adding that apartment and gated-community deliveries further complicate the scenario. "It's a much better experience if a human brings it to your door, or even better, inside your home."

H-E-B also lags behind Kroger and Amazon's Whole Foods when it comes to offering in-store digital payment systems. Whole Foods and Albertson's-owned Randalls accept phone-based payments such as Apple Pay and Google Pay.

Kroger last year launched its own phone payment system using a scannable QR code tied to a credit card in its app.

H-E-B has thus far not gone this route, even though its stores have the phone-scanning hardware to do it. McClelland said it's a privacy issue, and potentially a competitive one.

"Who is going to own the customer and the customer's

Annie Mulligan / Contributor

H-E-B personal shopper Brenda Flores gathers cold food items for a curbside order inside a Houston store. An order may have three or four shoppers working it.

data?" he asked. "Apple is not in the grocery business today, but Amazon wasn't in it a few years ago, either."

H-E-B also doesn't have a loyalty card as do many of its competitors, even though these are popular with customers. A Kroger spokesperson said 96 percent of all in-store transactions involve its loyalty card, which gives customers discounted gasoline at some of its stores, customized coupons mailed to their homes and an in-store discount on many items.

McClelland says H-E-B "feels everybody deserves to have the same low price, you shouldn't need a card to get it."

"Customers feel those are a hassle, and there's some invasion of privacy. Does Big Brother need to know everything that I buy?"

However, H-E-B can collect shopper purchase data when customers make a credit-card purchase. In the privacy policy on its website, the company says it may "supplement" personal information you supply with, among many other sources, "in-store transactions."

"While it is possible to collect data from credit card usage, a lot of our customers do not use them in our stores for purchases," said Lisa Helfman, director of H-E-B's public affairs in Houston. "Therefore we don't find data sourced through credit card usage in our stores to be very reliable."

Tech expansionBack in Austin, Bath said he hoped the experiment of putting the Favor staff in the same building with the technology employees of H-E-B would have an impact on the grocer as a whole.

"We're already starting to see it," he said. "We have many instances where people come together and share ideas."

In fact, H-E-B is planning to build a second technology hub at its existing headquarters campus in San Antonio.

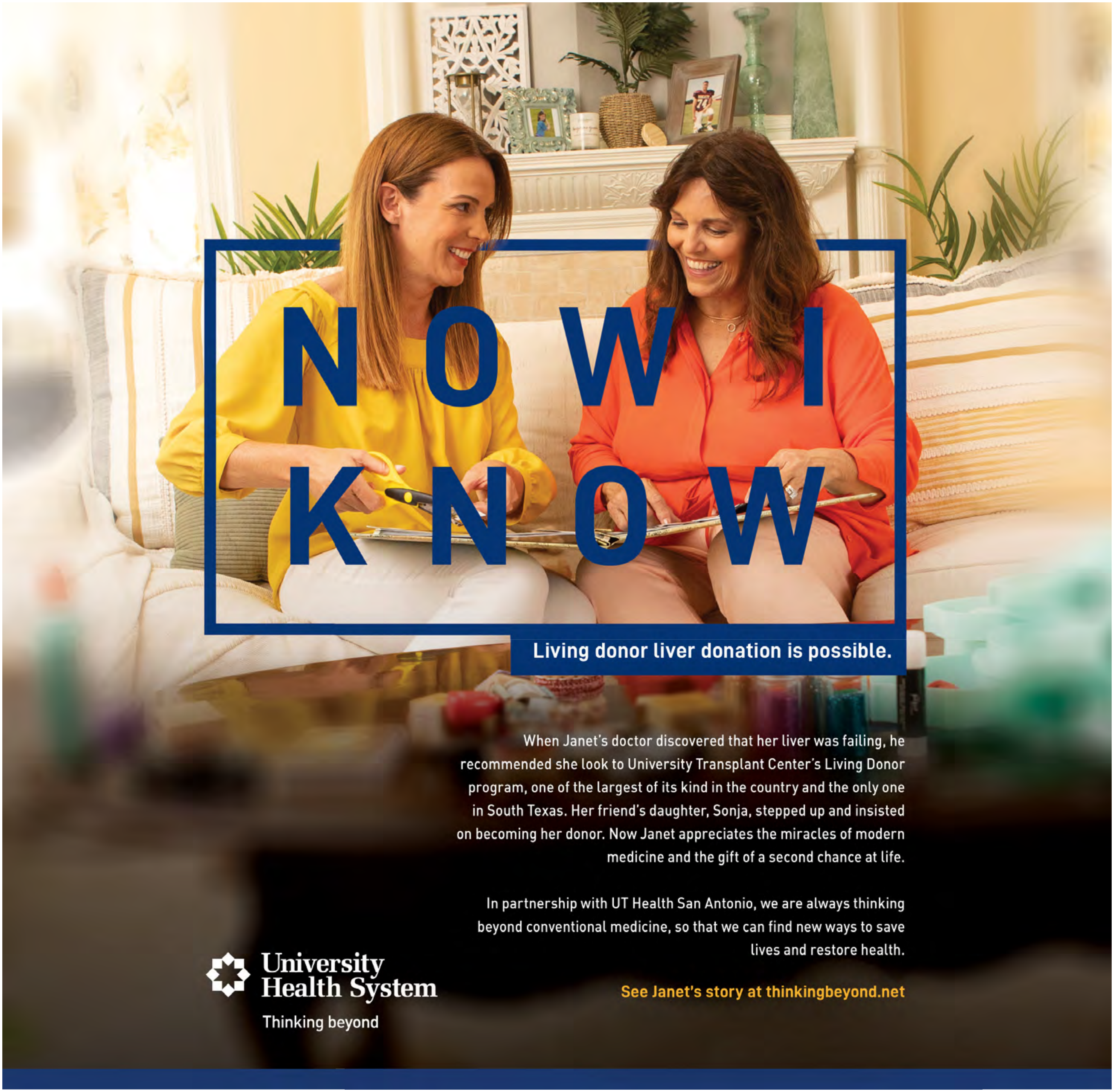
Bath said the building, which is expected to be completed in the fall of 2022, will be vertical, rather than the sprawling warehouse style found in East Austin.

H-E-B already has hundreds of tech employees who work at its headquarters, and more are being hired all the time. The new building will be 170,000 square feet and be home to 1,000 tech workers.

How technology might change H-E-B stores 10 years from now?

Bath paused.

"I don't know if any of us know the answer to that," he replied. "What you won't see is this technology replacing our people. We believe our people make a tremendous difference to the customer experience."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SPOTLIGHT

Investment czar talks Frost, Great Recession

By Greg Jefferson
STAFF WRITER

As Bill Sirakos, chief economist for Frost Bank and head of its capital markets arm retires, the Great Recession still haunts banking. Don't get Sirakos started on one of its aftereffects: the Dodd-Frank banking regulations.

Carlos Javier Sanchez / Contributor

A decade ago, in the chaos after the U.S. housing market's collapse, Bill Sirakos called U.S. Rep. Lamar Smith to plead with him to vote against a bank bailout.

Sirakos was Frost Bank's chief economist and head of its capital markets arm, but he'd contacted the San Antonio Republican's office as an agitated constituent. He passionately believed banks that had allowed greed to overwhelm their prudence should pay the price.

As he waited, Sirakos learned that Tom Frost Jr., chairman emeritus of the bank, was on the other line — asking Smith to vote *for* the bailout bill.

"I was like, 'Oops.' I'm glad he didn't know I was on that phone, too," the 67-year-old Sirakos said.

He hadn't worked much directly under Frost. The bank hired Sirakos as an asset liability manager in 1996, just a year before Frost stepped down as CEO. Frost died in August at age 90.

Yet Sirakos, who retired from Frost Bank on Friday after 23 years, talks about Tom Frost with a combination of respect, deference and enough understanding that he didn't begrudge Frost his views on the bailout.

"Mr. Frost was a very wise man," Sirakos said. "He didn't want violent shocks to the economy. Whereas I, being a little younger and more brash maybe, more libertarian — I was more willing to say, 'Well, we need the shock. Go ahead and let's have the shock.' "

Even that understates the differences between the two men. Sirakos is opinionated, blunt-spoken and honest, funny and fiery. Frost was polite, understated and courtly, with a sense of obligation to the bank's customers, employees and investors and to the community.

One thing they shared was a conservative approach to banking and investing.

Sirakos launched the capital markets division, which mostly trades stocks and bonds, in 2000, as many internet companies — better at selling Wall Street on their "story" than selling goods and services — began faltering. Sticking largely to bonds, Sirakos said, "we were profitable in our first year. It wasn't big, but it was a profit."

The Pittsburgh native, whose mother taught high school math and whose father worked at the

Federal Home Loan Bank, marveled as insanely complicated securities backed by lousy mortgages enriched investors — then nearly wiped them out in the Great Recession.

"We're like, 'Who buys this stuff? This is nuclear waste,' " Sirakos said. Frost stayed out of the toxic mix and was one of the few regional banks strong enough to turn down federal bailout funds in 2009.

As he retires — his immediate plan is to spend more time raising sheep on his 140-acre ranch in Gillespie County — the Great Recession still haunts the economy and banking. And don't get Sirakos started on one of its aftereffects: the Dodd-Frank banking regulations, intended to stop financial institutions from behaving badly.

Sirakos talked with the San Antonio Express-News recently in his office at Frost Bank headquarters. The following transcript has been edited for clarity and length.

Q: Your first job out of college was bank examiner at (the Office of the Comptroller of the Currency, a bank regulator), and you hated it. What did you hate about it?

A: I hated the traveling. We traveled all the time, and I had a girlfriend, who is now my wife of 44 years — but we'd never see each other except on weekends. And there were just a lot of things about traveling that just didn't fit me. Also, some of the people I worked with were, let's just say, less than ambitious.

I graduated in 1974, and if we could go back to the regulatory structure in 1974, it would look like the Wild West compared to where we are today. But I was just shocked at how regulated banks were. And I said, "I thought we were a free country." I was very idealistic. "We're a free country. How can you tell the banks you can't pay any more than this on deposits and that you have to do this and this?" So the more I learned about the regulatory environment, the more I came to despise it.

Q: From the OCC, you went to work at First Union Bank in Charlotte, N.C. Describe its culture.

A: Ed Crutchfield was the CEO, and he was a very dominant figure, intimidating. And so people really didn't feel free to speak their mind. But the bank was wildly successful because when interest rates started to fall in the early 1980s, Ed Crutchfield made the decision that we — we weren't even a $5 billion bank — we were gonna buy $500 million dollars worth of bonds. And we did. I bought seven-year Treasury notes at 14 percent. I bought 30-year Ginnie Maes. But as soon as we bought that stuff, the Fed started cutting interest rates. And so we bought more, and then we bought more, and then we bought more, and the book value of First Union rose because the bonds were going up in price. And we were able to buy other banks. So all of a sudden, we started growing into this huge bank. When I left First Union, they were a $37 billion bank. But people were intimidated in speaking out to a large extent because the CEO was very dominant.

When I came here (in 1996), the difference was profound. They encouraged you to speak out without consequence here. And the CFO, Phil Green, who's now CEO, I reported to him for 20 years. And I would disagree vehemently with him. We had some pretty good arguments, but I never, ever felt like he would hold that against me. I would just speak out — I was just out there with it. And it encouraged some pretty good ideas. But one thing about Phil, he was an accountant, and you had to have the facts to back yourself up. You didn't say, "Well I just feel like this would …" No, that didn't cut it. You have to say this, this, this, and this to back up your argument.

Q: Looking at the roots of the financial crisis a decade ago, First Union went on to acquire Wachovia —

A: That was after I left.

Q: — which was forced to merge with Wells Fargo because of bad mortgages. In retrospect, did First Union's culture seem to you a little loose, a little gunslinging?

A: Well, I think that what happened was they almost got to believe they couldn't do anything wrong — because they had done so many things right. I mean, we would just buy bonds and buy banks, and we were just knocking it out of the park.

And then they made a couple of mistakes. They bought this outfit called the Money Store. I think they paid a little over $1 billion for it, and they ended up just closing it because it was so bad. And they made this bad, bad mistake with this thrift in California that they bought. That's what really put them under. By that time, Ed Crutchfield had retired and Ken Thompson had taken over, and they'd issue statements saying, "Well, we've addressed all of our mortgage-backed concerns, and we should be clear going forward." And I looked at that and I thought, "I don't think so." So I sold my stock.

Carlos Javier Sanchez / Contributor

Bill Sirakos, chief economist for Frost Bank and head of its capital markets arm is retiring after 23 years with the company.

"Being a little younger and more brash maybe, more libertarian — I was more willing to say, 'Well, we need the shock. Go ahead and let's have the shock.' "

Bill Sirakos, recalling the bank bailout of 2008


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BUILDING PERMITS

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