http://www.nakedcapitalism.com/2017/01/can-uber-ever-deliver-part-six-bleak-pl-performance-while-stephen-levitt-makes-indefensible-claims.html

Can Uber Ever Deliver? Part Six: Latest Data Confirms Bleak P&L Performance While Stephen Levitt Makes Indefensible Consumer Welfare Claims

Posted on January 2, 2017 by Yves Smith

Yves here. Uber's continuing losses, with no near-term prospect of reversal, seem to be denting the Silicon Valley darling's carefully cultivated image of invincibility. For instance, in Uber and Airbnb business models come under scrutiny, the Financial Times described how both companies are facing more and more effective opposition to their cavalier rule-breaking. In a Slate story, Why It's Getting Harder for Uber to Break the Law, which tellingly was reprinted by Business Insider, Henry Grabar flagged an issue that Hubert Horan has stressed in his Uber series: that Uber is not a software company, but an urban transportation company. And as the company moves more and more in the direction of owning assets, like driverless cars and autos it leases to drivers, the more it becomes subject to real word regulations.

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Latest Leaks Provide Further Confirmation of Uber's Bleak Financial Performance

Part One of Naked Capitalism's Uber series laid out all of publically reported data about Uber's Operating P&L results between 2012 and the first half of 2016. Only EBIDTAR contribution data was available for this entire time period; true GAAP profitability data was only available for the year ending September 2015 when Uber lost $2.0 billion with a profit margin of negative 143%. Through the end of 2015 Uber's EBIDTAR contribution margin was consistently a bit worse than negative 100%. While this margin improved to negative 62% in the first half of 2016, all of the improvements were explained by Uber's cuts in driver pay.

Uber EBIDTAR contribution numbers for the third quarter of 2016, leaked to the press on December 19th[1], show yet more bleak results. Third quarter EBIDTAR was worse than negative $800 million (no exact result was disclosed). Media sources said that Uber expected fourth quarter EBIDTAR contribution again to be negative $800 million. This would produce a full year 2016 EBIDTAR contribution in the range of negative $2.8-3.0 billion, meaning that true GAAP losses for the year would easily exceed $3 billion.

As with the first half 2016 data, a small improvement in the EBIDTAR contribution margin was entirely explained by further cuts in driver compensation; there was no evidence Uber had improved operational efficiency or was getting passengers to pay higher fares.

These third quarter results (and the fourth quarter projection) reaffirm the major conclusions of Part One of the Uber series – Uber's operations and growth has depended on unsustainable, multi-billion dollar investor subsidies, and in Uber's seventh year of operations there is still no evidence of the strong, steady P&L margin gains needed to show a clear path to breakeven, much less the roughly $5 billion in annual P&L improvements needed to generate meaningful investor returns.

One of the two reporters that published the leaked data (Efrati) argued that "Uber's departure from China in the middle of the quarter helped slow the growth rate of its losses" and that the losses "reflects its increased investment in areas like self-driving car technology and mapping." Neither of those claims is credible. Both impacts of the sale of Uber's shareholding in the failed Uber China venture (which include a multi-billion dollar gain from Uber's new shareholding in Didi Chuxing) and investments in speculative future ventures like driverless cars would impact cash flow and balance sheet statements, but not 2012-16 quarterly operating P&L statements, and it is not clear that the reporter understands the difference.

Stephen Levitt's Bogus Claim that Uber Creates Massive Consumer Welfare Benefits

The first four parts of Naked Capitalism's Uber series (Part One, Part Two, Part Three, Part Four) focused on the question of whether the growth and eventual industry dominance of Uber has (or could in the near future) create sustainable improvements in overall economic welfare. Neither the bleak P&L results of any other single piece of evidence is isolation could answer this question, but the range of evidence presented consistently supported the conclusion that Uber had, and would continue to reduce welfare.

Uber is a substantially less efficient producer of urban car services than the incumbents they have been driving out, so its growth reduces overall industry efficiency. All of Uber's apparent price and service advantages depend on unsustainable investor subsidies. Uber has not introduced any significant efficiency or product breakthroughs and lacks the scale economies that could quickly generate billions in P&L improvements, and all of Uber's behavior suggests it fully understands that it could not provide returns to investors without achieving exploiting significant levels of welfare reducing anti-competitive market power.

In isolation, the lower taxi fares some consumers may have received thanks to Uber's multi-billion dollar subsidies do not constitute a consumer welfare gain because those subsidies are unsustainable and are explicitly designed to drive more efficient producers out of business and create artificial market power, which would massively offset any short term welfare gains. Subsidies supporting the pursuit of industry dominance can only enhance long-term economic welfare if the dominant company can produce service at significantly lower cost/higher quality than the displaced incumbents, and if the dominant company continues to pass a significant share of those efficiency gains on to consumers. At this point there is absolutely no public evidence that Uber will ever be able to offer consumers lower prices and increased service on a sustainably profitable basis.

Stephen Levitt, a senior economics professor at the University of Chicago, and co-owner of the "Freakonomics" media venture vehemently disagrees. He co-authored an article (further publicized through his various blogs and radio programs)[2] claiming that Uber generated $6.8 billion in consumer surplus in 2015.

Given hard evidence of Uber's inferior efficiency, disastrous financial performance and aggressive pursuit of quasi-monopoly industry dominance, how could an economist find evidence that the entry of Uber into the market has not only made consumers better off versus an industry dominated by traditional operators but found consumer gains of such an enormous magnitude?

The first clue is that Levitt is an unabashed Uber supporter who admits he "loves Uber" and describes them as "a phenomenally successful company" even though they had a negative 149% operating margin during the period he studied (the first half of 2015). Levitt claims "Uber embodies what economists believe should happen with the labor market," is openly rooting for Uber "to destroy the old-school taxicab and private-car industries" and thinks the finding of the paper will be "the hammer with which I could smash all government resistance to Uber." The second clue is that the analysis was financed by Uber, and two of his co-authors are senior Uber officials. This was not the result of unbiased research by an independent academic.

The third and most important clue is that there is no data or analysis in the papers that compares how consumers fared since Uber's entry with how they fared before Uber entry (or compared consumer prices and service between markets that does and does not serve or made any other type of comparison). Nor is there any data on any of the issues discussed in the Naked Capitalism series that are critical to an understanding of whether post-Uber marketplace changes have (or could eventually) improve consumer welfare, such as evidence of major efficiency advantages or scale economies that would allow it to produce service at lower costs than existing competitors, or evidence that it could profitably offer lower prices and better service than incumbents in competitive markets.

So there is absolutely nothing in the paper that would allow anyone to conclude that consumers are better off with an Uber dominated industry than they had been with an industry dominated by the old-school taxicab and private-car industries, and there is nothing in the paper that justifies the conclusion that the headline "$6.8 million annual" number represents a consumer gain of any kind.

The $6.8 billion estimate had been derived from Uber moment-of-sale data from Uber's four largest markets during the first half of 2015 that showed when customers who wanted immediate cab service were given surged prices (which could be 10 to 500% higher than baseline fares), and whether or not service at the surged prices was accepted or refused. Levitt then estimated a continuous curve across the full range of surged price options and calculated customer price elasticity from that curve. Levitt calculated the "consumer surplus" gap between accepted prices and the higher prices they would have been willing to accept as a consumer benefit that Uber had uniquely created, and the total $6.8 billion was estimated by extrapolating the "surplus" from his half-year 4 city sample to full year 2015 traffic in all US markets.

Unfortunately estimates of the consumer surplus of Uber users in isolation does not and cannot measure incremental changes to consumer welfare across the entire market. It does not measure how consumers fared before and after Uber's entry, and only looks at an artificial subset of consumers. Consumer welfare can only improve if a marketplace change provides consumers with sustainably lower prices and/or superior service. Uber has higher average prices (21% of all trips in the study sample had surged prices, while traditional operators have no price surges), so Levitt and Uber are making the absurd claim that the company with higher average prices benefits consumers more. And the paper makes no effort to explain why its "consumer surplus" approach that apparently had never been used before in published academic economic studies would provide superior measures of changes to consumer welfare than traditional approaches.

Consumer surplus exists in every market, because even with variable pricing systems controlled by fancy software, companies like Uber offer a single price in each selling situation (Uber offers the same surged price to anyone requesting a car at a given time in a given geographic zone) and almost all of the people who purchase at that price would have also purchased at a slightly higher price. Consumer surplus would only disappear if companies read the minds of each individual consumer and then block them from accessing prices available to other, more price sensitive consumers. The fact that the Levitt/Uber consumer surplus estimate is a really big number is strictly a function of their calculation that demand is highly inelastic. Highly inelastic demand means people will often be willing to pay more than published prices (ergo much more "consumer surplus"); elastic demand means traffic falls faster when prices rise (so much less "consumer surplus" potential).

But all of the Levitt/Uber data massively overstates demand inelasticity by measuring "moment of sale" consumer decisions, instead of medium/long-term responses to price changes. The Levitt/Uber data are measuring people who are already committed to travel as soon as possible, and have started the ordering process — people who will always be highly price inelastic. But data showing many will accept a 25% price surge at that moment tells you nothing about how they would respond to longer term price changes. If all fares (peak and off-peak) went up 25% you would see a much bigger reduction in taxi usage (e.g. much higher elasticity) than the "moment-of-sale" response to a 25% surge would suggest.

The analysis is further biased because 75% of all the data reflects the behavior of people who are frequent Uber users in four of the wealthiest cities in America (NY, SF, LA, Chicago). These are the people least likely to consider alternatives when faced with surged prices, and it is highly unlikely that their willingness to pay higher prices reflects the price sensitivity of the total, nationwide market for urban car services. Large results from Levitt's methodology cannot support conclusions about changes to efficiency or welfare gains because they are primarily measuring changes in customer price elasticity. Walmart's growth was driven in large part by its efficiency/productivity advantages over traditional department stores. But if you applied Levitt's approach to Walmart it would tell you consumers were significantly harmed, because Walmart's customers are more price sensitive than typical department store customers (since Walmart's customers include many more people with lower income, the gap between prices and the demand curve would be smaller). Long-term demand of the total market is much more elastic than "moment-of-sale" demand from frequent Uber users in wealthy cities. The Levitt/Uber paper cherrypicks data from the segment of the urban car service market with the least sensitivity to price, in order to artificially generate the huge "consumer surplus" number highlighted in their conclusion.

Why Would a "Serious" Academic Produce an Indefensible Analysis Like This?

Why would a prominent economic professor from a prominent university actively publicize that his research had identified "the impact that Uber's introduction has had on consumer welfare" when there is absolutely nothing in the data or analysis that even attempts to measure consumer welfare impacts? Presumably the answer involves some combination of personal ideological affinity (his personal preference that all legal regulatory obstacles to Uber's success be smashed, along with all existing "old-school" industry participants) and financial incentives provided by Uber for attaching his name to what was largely an internal Uber study. Note that none of the reasons Levitt gives for loving Uber and rooting for its eventual industry dominance have anything to do with increased consumer welfare; Levitt participated in the study because he was hoping to find a welfare justification for his enthusiasm. Levitt's description of a company that lost $2 billion in 2015 as "a phenomenally successful company" demonstrates Levitt's willingness to ignore compelling evidence inconsistent with that enthusiasm.

Levitt would have also had reasonable grounds to assume that there was little risk that the poor quality of his work would have ever been attacked by fellow academics (many of whom undertake private consulting projects like this, where results are not subject to any type of academic peer review) or journalists (who had never examined these issues independently and in any event would be highly reluctant to openly challenge a famous academic).

Levitt took some steps to protect himself in case knowledgeable people read his paper carefully and pointed out some of the serious flaws. His radio discussion emphasized that his role on the Uber project focused on the methodological issues involved in translating raw Uber data into the demand curve and elasticity estimates.and claimed he was the first person to ever actually develop a demand curve from industry data.[3]

Levitt actually acknowledges that the analysis does not meet academic standards. Both the academic paper and the supporting Freakomics publicity acknowledge that the questions being addressed require long-term elasticity measures, and that the "moment-of-sale" elasticity measures actually used are inappropriate[4]. Including this admission in a peer-reviewed academic paper would have been tantamount to saying "stop reading here and ignore all conclusions presented because the data doesn't support them." The ethical/professional problem is that even if Levitt buried qualifying statements about the elasticity measures deep in the article text, he failed to ensure that the highlighted primary conclusions based on those elasticity measures (creation of $6.8 billion in annual consumer benefits) were qualified in any way.

Despite these questions about Levitt's intellectual integrity, it is more important to understand why Uber hired him to serve as a paid advocate, and the larger process by which Uber sought to publicize an "Uber creates billions in annual consumer benefits" meme without actually having any legitimate evidence that it did. Had this paper been produced entirely (instead of largely) by internal Uber staff, it would have been impossible to get the claims published in mainstream media outlets. By paying Levitt to put his name on the study (and publicize it through his blogs and radio programs) Uber could create the appearance that the $6.8 billion benefit claim resulted from independent analysis that met academic standards, and knew that no one in the media would scrutinize (much less challenge) work endorsed by a famous U of Chicago professor. Regardless of any nuances or qualifications buried in the paper (that no one would read) the paper created a valuable soundbite (famous U of Chicago economist says Uber creates $6.8 billion in annual consumer benefits) that Uber could circulate widely.

Uber did this by getting a series of pro-Uber columnists to publicize the highlight benefit claim through uncritical articles about the Levitt/Uber paper in a range of respected media outlets including the Wall Street Journal, Forbes, Bloomberg and the New York Times.[5] Each article falsely portrayed the $6.8 billion claim as "consumer welfare" benefits as if the paper had compared the welfare impacts of Uber versus traditional operators. Tyler Cowen, a well-known libertarian blogger (and active Uber supporter) who writes columns for Bloomberg and the New York Times, misrepresented the $6.8 billion number from the paper was the "social value" of Uber, and reflected the economic loss society would suffer "if Uber simply went away." Cowen highlighted how the finding illustrated how "consumers gain from lower prices from a new service" even though neither he or the Levitt study had any evidence that Uber passengers currently pay lower average prices, or would in the absence of massive subsidies. Cowen claimed that this evidence of huge consumer benefits justified his view that current industry competition was "a fight between progress and protection."

A Wall Street Journal columnist claimed the study proved that Uber had created net economic welfare gains because "U.S. consumers alone are reaping billions of dollars a year in benefits, far greater than the losses borne by taxi owners" even though there was nothing in the study that purported to analyze those tradeoffs. That columnist highlighted the accomplishment of estimating a "demand curve" while ignoring the caveat that the demand curve estimated was totally inappropriate for the conclusions drawn. He also insisted that Uber illustrated how "[t]he free-market system has long ensured goods providing very high consumer surplus are cheap" without explaining how a company that lost $5 billion in the last two years could serve as an exemplar of the free-market system. A Forbes columnist falsely claimed that the result showed "that Uber is indeed making us all richer." He highlighted the huge gap between price and willingness to pay, and facetiously attacked Uber for not raising prices more aggressively, but ignored the long-run versus moment-of-sale elasticity issues that the paper had pointed out. The New York Times published a nationally syndicated columnist who claimed the $6.8 billion estimate was based on demonstrated "economic theory" without bothering to explain what that theory was, or noting that Levitt's methodology had never been used in any prior academic analysis of consumer welfare impacts. He tried to argue that these benefits somehow offset the growing public evidence of huge Uber losses, and failed to disclose Levitt's "analysis" had been paid for and co-authored by Uber.

Thus the original Uber sponsored study produced a big number it could publicize ($6.8 billion in annual consumer benefits) and a famous academic name it could attach to the study to create the false impression the number resulted from rigorous, independent analysis. The secondary sources increased awareness of the headline claim, and generated new pro-Uber claims (huge social of value of Uber thanks to lower prices, victory of progress over protection, Uber making us all richer, victory for the free market) that were not based on any data or analysis.

Uber's Use of False Consumer Benefit Claims Is Not New – Consumers Did Not Benefit When Taxi Medallion Values Collapsed

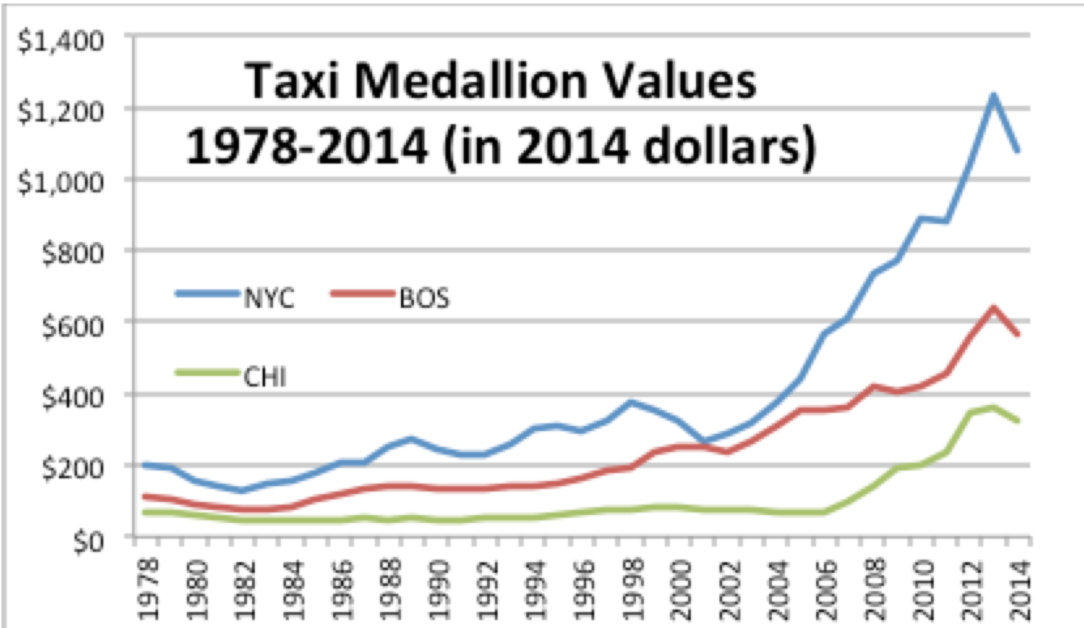
The Stephen Levitt endorsed $6.8 billion consumer benefit claim was not the first time Uber attempted to manufacture pro-consumer propaganda claims out of thin air. One of the first themes in pro-Uber propaganda is how consumers had been directly harmed by high taxi medallion values, and that by destroying that value Uber has generated huge benefits for consumers. Travis Kalanick has often claimed in 2012-13 that Uber was fighting "the taxi medallion evil empire" and in late 2016 Levitt was still claiming the only people harmed by Uber have been taxi medallion holders. To quote just one of many possible examples, an unabashedly pro-Uber article by a Washington Post writer claimed that "In exchange for all of this regulation, taxis have for decades held a government-backed monopoly. At the center of that bargain — and the debate over what form of transportation best serves the public — is the medallion…Uber counters that medallions have created a cartel that operates for its own benefit — and not in the best interests of the public."[6]

Allowing tradeable medallions is bad regulatory policy and will not be defended here, but the Uber claim that medallion trading values represents wealth extracted from consumers, and that consumers recaptured that wealth when Uber destroyed those trading values[7] is utter nonsense, and none of the many people making that claim ever provide any supporting evidence.

The Uber claims conflate two entirely separate issues – should city governments be allowed to limit the total number of taxi operating licenses issued, and should that public license to operate a car service on city streets be transformed into a tradeable private property right, as has happened with broadcast licenses, water rights, landing slots at congested airports and other private uses of limited public resources?

The first question is debatable; the historical justification for limiting market entry via license caps was that the taxi market is limited, faces a severe peaking problem and marginal peak capacity costs much more than highly-utilized average capacity. Entry limits mean all drivers get a somewhat fair share of peak and off-peak hours, and reduce the risk that higher-cost cream-skimming marginal entrants make it impossible for anyone to make any money. There is also evidence that some cities loosened or eliminated license caps without undermining industry viability, so a simple "entry limits always good/bad" conclusion probably can't be drawn.

But the tradeable medallions that are the central focus of the Uber claims only had significant value in three cities — New York, Chicago and Boston.[8] There was never any significant difference in taxi fares, service levels or driver wages between those three cities and any other large US cities, and there is absolutely no evidence of any adverse consumer impacts concurrent with the recent run-up in medallion values. Just as fluctuations in broadcast license values had no impact on advertising rates, and airline fares did not fluctuate with slot values at LaGuardia or O'Hare, medallion values did not represent wealth transferred from taxi consumers.[9]



The “medallions extract wealth from consumers” argument is based on the false claim that trading values are a direct function of the stream of future profits a medallion holder might earn. If the claim was true, one would see long-term medallion value fluctuations in line with industry profitability and supply/demand conditions, and would see major adverse consumer impacts in cities with high medallion values, compared to cities with lower values and cities that did not have medallions. In reality, these three cities established medallions in the 1930s, but values did not begin growing until the 1960s.[10]

The huge recent inflation in medallion values is totally explained by changes in speculative financial markets. When returns in most classes of low-risk investment fell in the early 2000s (and fell dramatically after 2008) investor demand for medallions soared.[11] This created massive windfall profits for people who happened to have acquired medallions in the past, but neither the initial rise nor the subsequent collapse of these values had any direct impact on consumers.

Why would Washington Post reporters falsely claim that Uber’s destruction of medallion values had created huge benefits for consumers? For the same reason that University of Chicago economics professors would falsely claim that the response of frequent Uber users to surge pricing proves that Uber has created massive consumer benefits. Both were willing participants in well-designed Uber PR propaganda programs, and were more interested in helping promulgate Uber’s desired narratives than they were in presenting analysis based on legitimate data.

In both cases Uber had developed a narrative about wonderful benefits Uber had created, featuring large dollar impacts that would get attention, and structured in ways that would ensure the business press would not seriously scrutinize the legitimacy of the claims. The false surge pricing/consumer surplus claim was protected from scrutiny by the use of a famous “brand-name” economist. The “medallion value stolen from consumers” claim handed the media an appealing narrative pitting the heroic, cutting edge innovators from Uber against a clearly defined enemy (the corrupt “taxi medallion cartel”) that provided terrible service and that no one in the press liked. Like any good propaganda campaign shifting the discussion to a simplistic good vs evil narrative meant the media did not have to investigate any of the actual competitive industry questions – did Uber actually have any powerful, efficiency enhancing innovations, could its business model actually solve any of the service problems Manhattan Yellow Cab users faced, or did it have any advantages in the 95% of taxi markets that are totally unlike Manhattan and never had tradable medallions, or could Uber actually make money in a competitive environment. Once Uber can get sympathetic columnists at other mainstream outlets to repeat the claims, they gain broader credibility and acceptance, and that fact that the original analysis was intellectually indefensible and had never been vetted by any independent experts is forgotten.

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[1] Efrati, Amir, *Uber's Loss Decelerates, Reflecting China Exit,* The Information, 19 Dec 2016; Newcomer, Eric, *Uber's Loss Exceeds $800 Million in Third Quarter on $1.7 Billion in Net Revenue*, Bloomberg, 19 Dec 2016. Efrati claimed the P&L data was driven by Uber's exit from China, but Newcomer did not.

[2] Cohen, Peter, Hahn, Robert, Hall,Jonathan, Levitt, Steven and Metcalfe,Robert *Using big data to estimate consumer surplus: The case of Uber*. National Bureau of Economic Research, 2016. Dubner, Stephen J., *Why Uber Is an Economist's Dream,* transcript of Freakonomics Radio discussion between Dubner, Steven Levitt and Jonathan Hall 7 Sep 2016 http://freakonomics.com/podcast/uber-economists-dream/

[3] This claim might come as a surprise to Sveriges Riksbank, who awarded the 2015 economics Nobel Prize to Angus Deaton for work that prominently featured demand curve estimation. Or to the thousands of industry analysts whose estimation of demand curve slopes and elasticities are critical to decisions about pricing and capacity.

[4] [What's in the paper]"..is actually not the demand curve I wanted to estimate at all. It's the only one I could estimate but not the one I really wanted. So for public policy, like in deciding how to regulate Uber, for instance, the demand curve you'd love to have is what we call a long-term demand curve."

[5] Cowen, Tyler, *Computing the Social Value of Uber. (It's High.)*, Bloomberg 8 Sep 2016.; Creighton, Adam, *Uber's Pricing Formula Has Allowed Economists to Map Out a Real Demand Curve*, The Wall Street Journal, 19 Sep 2016; Worstall, Tim, *Freakonomics' Steven Levitt On How Inefficient Uber Really Is*, Forbes, 20 Sep 2016 (the "inefficiency" was the higher prices Uber could have charged, but out of the goodness of their hearts, did not); Beales, Richard, *Uber's Value to Riders Is Clear. To Investors, It May Prove More Elusive*, The New York Times, 22 Dec 2016. Beales' piece was nationally syndicated by Reuters' "Breakingviews."

[6] Badger, Emily, *Taxi medallions have been the best investment in America for years. Now Uber may be changing that*, Washington Post Wonkblog, 27 Nov 2014.

[7] "As [Kalanick] notes, in New York there are 13,000 taxis with medallions that trade for close to $1 million, implying a very profitable cash flow from fares." Kesler, Andy, *Travis Kalanick: The Transportation Trustbuster*, Wall Street Journal, 25 Jan 2013. "Doesn't the high-value of medallions (over $1mm in some markets) implicitly prove that the market is undersupplied and that prices are above true market clearing prices?" Gurley, Bill, *How to Miss By a Mile: An Alternative Look at Uber's Potential Market Size*, Above The Crowd, 11 Jul 2014. Gurley is a major Uber investor.

[8] In New York, only street hail (Yellow) taxis have tradeable medallions; "for hire" dispatch cars and limousines do not. Miami, Philadelphia and Atlanta sanctioned medallion trading markets in the 90s but prices were always below $100,000; San Francisco reclaimed medallions as city property in 1978. Some other cities appear to turn a blind eye to small scale black market medallion trades, but true exchange markets never developed.

[9] A study of taxi regulatory practices in the U.S. commissioned by the San Francisco Mayor's Office found no relationship between license tradeability and price or service levels, but rejected any proposal to increase license tradeability unless new regulations ensured that any rents created were shared with drivers. Lam, D. Leung, K., Lyman, J. The San Francisco Taxicab Industry: An Equity Analysis. Richard & Rhoda Goldman School of Public Policy, University of California, Berkeley, (2006) 10-15.

[10] Historical medallion values compiled from multiple sources including New York Taxi and Limousine Commission data; Boston Mayor's Office of Transportation, *Boston Taxi Study*, 4 (1978); monthly reports of medallion sale prices in Chicago Dispatcher Magazine; Barlett, A. & Yilmaz, Y., *Taxicab Medallions—A Review Of Experiences In Other Cities*, prepared for the Government of the District of Columbia (2011); San Francisco Municipal Transportation Agency, *Managing Taxi Supply*, prepared by Hara Associates (Apr 2013); Badger, *supra*.

[11] Prior to 2004 medallion prices closely tracked general financial market indices such as the S&P 500. Dhar, Rohin, *The Tyranny of the Taxi Medallions*, Priceonomics, 10 Apr 2013.. The post-2004 increase was heavily influenced by the specialist financial firms that had long provided medallion-collateralized loans to cab drivers. Malik, N. *A Bet on the Rising Value of Yellow Cabs*, Barrons, Jun 2007; Mead, C., *Taxi Licenses as 'Cash Cows' Bolster Medallion Financial Shares*, Bloomberg Financial News, 16 Nov 2011.

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Can Uber Ever Deliver? Part Seven: Uber's "Narrative" and The Vox and Stratechery Critiques of Naked Capitalism's Uber Series – Defending Uber Requires Ignoring Industry Economics

Posted on January 31, 2017 by Yves Smith

Yves here. Get a cup of coffee. This post walks through some of the recent efforts to defend Uber against the evidence Hubert Horan presented in earlier posts in his series. One basic issue the loyalist fail to deal with is that the long history of transportation fleet management has shown that there is a tradeoff, in terms of capacity management (how big a fleet to have) between profitability and customer convenience (how much capacity to offer to allow customers more availability/more rapid response). Thus Uber's massive subsidies are the reason customers may find that it offers more rapid "fills" of their orders for service than traditional cabs. Remove the subsidies, as Uber eventually must, and the fact that it is inherently a high cost producer, it will offer an inferior cost/speed of response tradeoff to other providers.

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Uber's narrative for its growth and expected industry dominance is devoid of any economic evidence

Uber has managed to get its own story about its eventual dominance and its unprecedented $69 billion valuation widely accepted despite a lack of supporting evidence. Uber depicts itself as similar to a handful of other blockbuster Silicon Valley startups: an incredibly powerful business model based on cutting edge technological innovation that would work in any city in any country. Like those other well-known startups, losses will soon give way to robust profits and the enormous power of this business model will inevitably lead to global industry dominance, and could possibly even lead to Uber significantly displacing private car ownership.

Unfortunately, nothing in the Uber narrative is based on objective evidence or actual industry economics. Neither Uber nor anyone else has provided any verifiable evidence that Uber's business model can even achieve sustainable profits.   Similarly, there is no proof of massive efficiency advantages that would be necessary to achieve inevitable industry dominance in the near term or major reductions in private car ownership in the longer term.

In fact, the spectacular failure of Uber China directly refutes the claim that Uber has a clear path to global dominance. Urban car services have none of the powerful scale economies that allowed other digitally-based tech companies to rapidly "grow into profitability." No one has demonstrated that any of Uber's claimed innovations have a material impact on efficiency or profitability. Uber users may like their fares and service levels, but no one can explain where Uber will suddenly find billions in efficiencies and scale economies that would be required to make its business self-supporting.

Uber has already imposed major unilateral cuts in the driver compensation levels it used to attract the drivers it needed to support its rapid growth; no one can explain why Uber wouldn't similarly reduce passenger benefits as it approaches industry dominance. There is absolutely no evidence showing how a profitable Uber could sustainably provide cities with higher quality and lower cost transport service.

The Naked Capitalism series' finding that Uber's business model could not earn sustainable returns without exploiting anti-competitive market power was based on a wide range of evidence about the competitive economics of the urban car service industry

This series sought to establish an alternative to Uber's narrative, using economic evidence to address the question of whether Uber's growth and anticipated dominance will improve overall economic welfare. It has used traditional, well-accepted, widely used analytic techniques that a consultant or financial analyst would use to understand the market potential and/or competitive threat of a new entrant, or that an economist or an urban transport planner would use to consider whether an alternate taxi competitive/regulatory structure might improve service levels or industry efficiency.

If an Uber-dominated industry is to improve overall economic welfare, it would meet four tests

(1) the ability to earn sustainable profits in competitive markets large enough to provide returns on its investment base

(2) The ability to provide service at significantly lower cost than existing competitors, or the ability to produce much higher quality service at similar costs

(3) The creation of new sources of sustainable competitive advantages through major product redesigns and technology/process innovations that incumbent producers could not readily match

(4) Evidence that the newly dominant company will have strong incentive to pass on a significant share of those efficiency gains to consumers in the form of lower prices and/or increased service.

Since Uber's investors have been explicitly pursuing total worldwide industry dominance, the evidence of profits, efficiency, competitive advantages and consumer welfare benefits would need to be overwhelming and obvious.

Part one of this series focused on the evidence that Uber was a fundamentally uneconomic enterprise (e.g.2015 operating margins of negative 140% and $2 billion in actual losses) and that all of Uber's growth to date was due to billions in predatory investor subsidies that competitors could not match.

Part six presented new evidence confirming those findings, including reports that Uber's 2016 losses were likely to exceed $3 billion, and data showing all margin improvement had been due to unilaterally imposed cuts in driver compensation. It also discussed Uber's spectacular failure in China, which demonstrated that its business model could not be easily leveraged worldwide.

Part two gave data showing that Uber was the industry's high cost producer and lacked the scale/network economies other startups have used to "grow into profitability".

Part three showed how various claims that Uber's growth had been driven by competitively powerful innovations were readily refuted by evidence of actual industry economics. As a result, there was no basis to expect Uber could ever earn sustainable profits in a competitive market.

Part four discussed how Uber's investors had always seen quasi-monopoly industry dominance and the elimination of legal/regulatory barriers to the exploitation of anti-competitive market power as the key to earning returns on their $13 billion investment.

None of the findings rested on any single data point, and each of the conclusions was complemented and reinforced by evidence from the separate analytical approaches (financial results, cost structure, competitive advantage, industry dynamics). To encourage a discussion that could help improve the analysis part five of the series responded to many of the readers who had posed comments, questions and criticisms about precious posts. The finding that Uber would reduce economic welfare was based on the combination of its lack of efficiency advantage (so that its growth reflected an allocation of resources to less efficient uses) and the risk that a dominant Uber could exercise anti-competitive market power.

One objective of the Naked Capitalism series was to begin the process of refocusing the public discussion about Uber around economic evidence

As discussed in part three using the example of Amazon, the media coverage and public discussion of Uber has been markedly different from past startups.

Every major startup has had a PR story it wanted to tell to investors, consumers and competitors, but media coverage of past startups treated their reasonableness and accuracy as an open question. Amazon wanted to emphasize the power of its potential competitive advantages, but reporters sought input from independent experts in relevant fields (ecommerce, warehousing, distribution, traditional retailing) so that readers could better understand whether the claims were valid. Even as the power of Amazon's many efficiency advantages became widely understood, the question of whether Amazon could ever achieve sustainable profits remained widely debated.

Press reports on Uber, by contrast, show no effort to investigate whether claims about competitive efficiencies and technological innovations make any sense. Independent sources with actual knowledge of the economics of taxis or urban transport are never quoted.

Similarly, leaked information showing Uber's multi-billion dollar operating P&L losses first became available in mid-2015, but the overwhelming majority of media coverage completely ignored the question of whether the company will ever be profitable.

Journalists depict Uber's unstoppable march to industry dominance as established truth, although the basis for their certainty about Uber's overwhelming is never explained. Competitors like Lyft (with over $2 billion in funding) are treated as minor inconveniences, and every company that had served the industry prior to 2010 is treated as completely irrelevant. Even those who have been highly critical of specific Uber practices (false advertising, driver exploitation, journalist harassment, refusal to obey insurance and safety laws) typically assume that Uber's story is true. Worse, they take the view that the costs and/or business model changes needed to fix these problems are not significant, and that Uber would retain its yet-to-be-demonstrated efficiency advantages.

Later in this series, we will discuss in detail how Uber was able to dominate media coverage and effectively block any serious scrutiny of its business model. In simple terms, pro-Uber media coverage falls into two major categories. The first category includes advocacy directly financed by Uber's huge PR machine and/or provided by active Uber supporters with the help of Uber PR. Unlike any previous Silicon Valley funded startup, PR was a major strategic and spending priority for Uber since day one. So far, Uber has been able to overwhelm independent or dissenting views. These efforts included paying academics to publish major pro-Uber claims that do not hold up to even cursory scrutiny (including the Steven Levitt papers discussed in part six). Yet the press reports them as if they were independent, highly rigorous research. The active Uber supporters usually have political/ideological affinities with the company (i.e. favoring the elimination of any form of regulation including barriers to monopolization and the ability to exploit anti-competitive market power) and write pro-Uber papers to advance those objectives.

The second category is technology industry journalists and analysts. As in many other parts of the media, their ability to provide readers with critical insights may be compromised by things like their dependence on access to the senior executives of the prominent companies they cover. In its early startup days Amazon felt it had a powerful competitive story to tell and welcomed the business press.

By contrast, Uber went to great extremes to show it would ruthlessly attack any outsiders that dared question their official story.[1] At a more basic level, Uber's narrative was designed to tap into the technology writers' predisposition that "tech" is a powerful force for good in society and a major driver of "progress" and economic growth. There are obviously many examples of where technology companies have increased overall economic welfare, but many more cases where they haven't; you need to look at the economic facts in each situation.

But by wrapping itself in the mantles of "technological innovator" and "industry disrupter," and emphasizing the contrast between Yellow Cab companies based out of garages in unsavory locations and a glamourous startup funded by the Silicon Valley's best and brightest, Uber convinced most technology journalists that they didn't need to talk to anyone familiar with those garages, or to investigate the sources and power of Uber's claimed innovations and disruption.

Thus the biggest challenge here is not assembling and explaining the economic evidence, but to refocus the public discussion. There are technology journalists and analysts who aren't on the Uber payroll and don't see Uber as part of a broader ideological crusade. Can they respond to the type of economic analysis presented in the Naked Capitalism or has Uber's narrative become too deeply ingrained?

Unfortunately, most of the technology and the mainstream business media have been valorizing Uber for seven years. Even when confronted with hard evidence of $3 billion annual operating losses, they may be reluctant to suggest that they might have gotten the story badly wrong.

Criticism of the Naked Capitalism analysis could be an entirely constructive response as long as the criticism was based on economic evidence, for example finding more detailed Uber P&L data, new evidence about Uber's cost competitiveness, scale economies, or the efficiency impacts of specific business model features.

The two articles considered below illustrate the difficulty in truly shifting public discussion away from Uber's narrative and towards constructive debate based on economic evidence. They represent "best-case" examples of reporters who have been covering tech industry issues for years.

While neither author had previously published anything remotely critical of Uber, both are free of direct Uber influence and are not focused on an external political/ideological agenda.

The first was by Timothy Lee in Vox[2]. Over the years, Lee has also covered the technology industry for Forbes and the Washington Post. The second was by Ben Thompson in his tech industry newsletter Stratechery,[3] which has been published since 2013. Both reports started by recognizing that the recent reporting about Uber's continuing massive losses and the Naked Capitalism series represented major challenge to conventional wisdom about Uber. Both told their readers why they disagree with the major findings of the Naked Capitalism series, but provided links so their readers could examine the detailed arguments for themselves. ***But none of those disagreements were backed by any verifiable economic evidence that would materially affect any of the findings they disagreed with.***

Thompson's counter-arguments: the P&L evidence is incontrovertibly false, it is impossible to draw any conclusions about Uber's cost competitiveness, and Uber can easily exploit scale economies to grow into profitability

Thompson's most emphatic assertion pertains to the issue (that I discussed in both part one and six) of whether the leaked 2002-06 Uber Global P&L data fully incorporates all the operating revenue and expenses from Uber China.

First, Part 1 insisted that the financial figures excluded Uber China, which was **incontrovertibly false**. (*Thompson's emphasis*)That's a pretty big problem considering the scale of Uber's losses in China! Not only did that error make the all of the numbers (very) wrong, it also raised serious questions about the analysis as a whole, particularly given the fact it remains uncorrected.

This assertion grossly misrepresents what I wrote. Uber has refused to explain what is included or not included in the leaked numbers (or any other aspect of its financial results). I did not claim that the exclusion of China was a proven fact, but laid out multiple data points supporting my interpretation of the financial results. For example, the quarterly EBITAR contributions, as reported by Bloomberg[4]

2016	Reported Uber Global EBITAR contribution	Uber Global shareholding in Uber China
2nd Q	($ 800) million	Entire quarter
3rd Q	($ 800) million	Half of quarter
4th Q	($ 800) million	None (sold in August)

Uber has never published hard data about the losses of the separately organized Uber China operation, but multiple sources have reported claims that the losses were much worse than Uber experienced elsewhere, perhaps on the order of $1 billion. My assumption was that if the P&L results of an associated company with a different ownership structure making humongous losses had been fully incorporated in the parent's operating P&L, those results would show sudden, dramatic improvements when the subsidiary was sold, probably on the order of a couple hundred million dollars per quarter in this case. You not only don't see that in the 2016 numbers, but you don't see any of the 2014-16 margin volatility you would have expected to see as Uber China rapidly grew. And incorporating the P&L results for Uber China would have been a major violation of GAAP accounting rules. Uber not only had no incentive to violate GAAP rules, but would have had ample reason to keep the huge losses and awful margins separate. Would this constitute "proof" in a court of law? Of course not, but it is a fair attempt to back up an argument using data and logic.

Does Thompson back up his alternate view with data or logic? Nope. He ignores my evidence, presents no data of his own, and then makes the totally indefensible claim that his alternate view is an incontrovertibly proven fact. Why does he think his view is incontrovertibly true and mine is incontrovertibly false? ***Because of a single tweet from the Bloomberg reporter, suggesting that the Uber numbers might include China.*** A claim that the reporter didn't think was reliable enough to ever include in any of his Bloomberg articles.

No one has disputed the bottom-line operating P&L loss numbers (e.g. $3 billion in 2016). If Thompson believes that China losses are included, and distort attempts to evaluate whether Uber's business model is working well elsewhere, what alternate number should we use? He doesn't say.

The worst case guess would only reduce the 2016 losses to $2.5 billion (Uber China was sold in the middle of 2016). Thompson doesn't explain why this would significantly change any of the other findings about Uber's competitiveness.

How Uber did its accounting here is a simple factual question, and at some point we'll have a clear answer. It would be one thing if Thompson said that his strong hunch was that I was wrong and the numbers did include Uber China but neither of us yet had "proof". But Thompson is willfully ignoring the available evidence, insisting that his gut feel constitutes absolute truth, and telling his readers the contradictory evidence on this one point I've presented raises "serious questions" about the legitimacy of the entire Naked Capitalism series.

Thompson's second line of attack is to claim that it is impossible to draw any meaningful conclusions about Uber's competitive economics from aggregate P&L data.

Part 1 analyzed Uber's profit and losses at the company level. While that is certainly an important data point — as should be obvious, in the long run all companies need to be profitable — it's not particularly helpful when it comes to a company investing heavily in growth, particularly if they are investing in pursuit of an opportunity governed by not just network effects but also scale effects. What is required is an evaluation of unit costs: how much does Uber earn or lose on an individual ride? And, per the previous point, how did that number differ by city, level of market maturation, etc.?…. The issue with analyzing Uber is that we — including the author of these blog posts — simply don't know what the company's unit economics are; that the author attempted to make pronouncements about the company's financial viability anyways was, in my estimation, an error just as significant as falsely claiming that the numbers did not include Uber China.

This objection is simply silly. Would it be nice to base an Uber analysis on detailed, carefully audited tables of unit cost data broken down by city, product and time of day? Well yes, but neither Uber or any other privately owned startup in history has ever provided that kind of data. Analysts routinely evaluate the growth potential of new products and companies where there's less information available than there is here.

Thompson is also ignoring Uber's actual strategy and narrative. Uber did not get $13 billion in funding in the hope that its business model might be able to make money in some kinds of markets under some kinds of conditions. Uber raised $13 billion because it told investors that it had an invincibly powerful business model based on cutting edge technology that would work in any city in any country, and would rapidly drive its inevitable march to global industry dominance. Thus the Uber Global P&L data I focus on are entirely appropriate. That Uber Global's losses have been substantially greater than any venture capital funded startup in history—on both an absolute and margin basis–provides a powerful first clue that their business model might be terribly flawed.

Note that when Thompson doesn't like my analysis showing Uber's costs are uncompetitive, he insists that nobody should be allowed to draw conclusions unless supported by extremely detailed internal data that will never be made available, but when Thompson doesn't like that my finding that Uber's business model is fundamentally uneconomic is backed by both hard P&L data and industry cost analysis, he dismisses everything on the basis of a single tweet.

The third and most important area of disagreement is that although Thompson accepts my data analysis of the traditional industry cost structure he rejects my use of that same data to support the argument that Uber lacks the scale/network economies that would be needed to quickly achieve sustainable operating profits. My finding that Uber has no significant scale/network economies is central to my argument that Uber has been engaging in predatory competition in pursuit of monopoly. Unless one can demonstrate the growth economics that will quickly convert $3 billion annual losses to sustainable profits, Uber's behavior cannot be interpreted any other way.

Powerful scale economies only exist when the cost structure has a huge fixed cost component, so that growth rapidly drives down unit costs. I provided the example of Amazon, which did have significant fixed costs (its entire IT marketing infrastructure, warehousing/distribution) and thus could expand to new geographic and product markets at very low marginal costs. I demonstrated that fixed costs were a tiny piece of urban car services total costs (85% are the totally variable costs of drivers, vehicles and fuel) and only a small portion of the 15% corporate costs are truly fixed. ***Uber cannot expand into new markets at very low cost since it faces unique driver recruitment, political lobbying and competitive marketing challenges in each city.*** I also pointed out that in the hundred years prior to Uber there had been absolutely no evidence of a tendency towards market concentration (either within or across cities) that would naturally occur if significant scale economies existed in this industry

Does Thompson's criticism based on any evidence showing flaws in my analysis or showing where Uber had suddenly discovered significant scale economies? Not really. His criticism is entirely based on an argument that demonstrates that Thompson doesn't understand the difference between short-term tactical marketing issues and the question of longer-term strategic/financial viability. He correctly points out that marketing managers in a company with powerful growth economics (like Amazon) would rationally price below total cost in order to accelerate those growth economics. But he completely ignores the question of whether Uber actually has Amazon-like growth economics, and if so, where do they come from and how strong are they?

Thompson concludes with several other assertions that ignore the evidence I'd provided about those questions and are not backed by any supporting counter-evidence whatsoever. In each case he's doing nothing more than repeating portions of Uber's narrative.

He insists Uber achieved important efficiencies from the "leverage to rework decades-old regulations that artificially limited taxi service to the benefit of incumbents." Zero explanation beyond this single sentence. The economics of taxi regulations are somewhat involved and there's never been a serious analysis showing large, clear-cut impacts in a single direction. "[T]here is far more demand for Uber than there ever was for traditional taxis. It is bizarre — and perhaps telling — that Horan flatly denies this market expansion in Part 3." Like the claim of massive efficiencies from deregulation, Thompson imagines that Uber operates totally independently of the basic economic constraints every other company faces. Other companies cannot permanently expand the overall market unless the industry can (or will soon be able to) earn profits on all the added capacity, but Thompson thinks evidence of billions in losses could not possibly have any bearing on his claim the Uber has massively expanded demand. To claim that an industry that currently loses billions every year has permanently increased demand is akin to claiming that volume stimulated by a ruinous price war better is a better reflection of underlying demand than the lower volumes observed under stable, profitable market conditions.

Thompson is also ignoring Uber's explicit goal of driving traditional operators out of business; it is trying to displace existing capacity, not to add to the capacity traditional operators already provide.

Likewise, you cannot say that Uber's evasion of longstanding capacity regulations improved economic welfare without showing how a mature open entry industry can profitably provide more capacity and lower prices. Thompson's claim that "Uber's full potential is to replace personal car ownership" is similarly untethered to economic reality. This claim doesn't just require demonstrating that Uber is massively more efficient than Yellow Cab; it requires showing that Uber can achieve such astounding levels of productive efficiency that it could drive taxi prices down to a tiny fraction of what they are today.

Lee's counterarguments: Uber is much more efficient, Uber's scale economies will drive profits, and Uber's real strategy is driverless cars

In parts two and three of the Naked Capitalism series I lay out the reasons why Uber has higher costs than traditional operators, why nothing in its business model constitutes a powerful competitive advantage, and why it lacks the scale or network economies that digitally based companies could use to grow into profitability. Although Lee reasonably summarizes other parts of my argument, he simply ignores the evidence I presented on these points, asserts that Uber does have powerful competitive advantages and scale/network economies, but presents no actual economic evidence showing why he might be right and I might be wrong.

Lee correctly notes that I did not think that Uber's investors were too stupid to understand industry costs, but (as discussed in detail in part four) that I thought those investors thought they could convert urban transport into a "winner-take-all" game and earn returns from exploiting monopoly power. But he rejects my "Uber returns require industry dominance" argument. "The other possibility — one that seems more likely to me — is that Uber really has figured out ways to make the taxicab market more efficient… that Uber's model is superior to conventional taxicabs." I had addressed those issues in detail in parts two and three; what points does Lee see that I might have missed? "The most obvious one is that smartphone hailing is inherently more customer-friendly than having to call an old-fashioned taxi dispatcher." I had explicitly noted in part three that a lot of people seem to like Uber's app, but there was no evidence that whatever marginal advantages it might have had any material impact on overall cost efficiency (dispatching accounts for roughly 7% of the cost of a traditional taxi operation) or driver revenue utilization. "The Uber app gives customers a realistic estimate of how long it will take for a car to pick them up. And once a customer hails a cab, it allows him to track a car's progress."

The software in Uber's app can be readily copied (my local cab company in Phoenix has an app with the same functionality) so this can't be a source of powerful, sustainable advantage. More importantly, there are dozens of other industries with ordering apps even more sophisticated and customer friendly than Uber's, but none of them have any impact on market competition, and none helped create $68 billion in corporate value.

"And Uber's pickup times have gotten even shorter as the company's fleet has grown." Here Lee is simply ignoring all of the data clearly showing that the prices and service quality Uber customers like is due to massive multi-billion dollar subsidies, not superior efficiency. Customers like the Uber app because it shows them multiple empty cabs nearby who can quickly pick them up. My Phoenix taxi app often shows no cars nearby or long wait times before pickup. That's not because Uber's software represents an efficiency breakthrough, it is because my fare in Phoenix needs to cover the entire cost of the cars and drivers on the street, while Uber subsidies make it possible to offer greater (but unsustainable) capacity.[5]

Lee then claims that Uber somehow achieves much higher driver revenue productivity than traditional operators.

As Uber gets more customers, it reduces the average distance a driver must drive to reach a customer — and hence the amount of time they waste driving without getting paid….And this suggests one hole in Horan's argument: If Uber can use driver time more efficiently, that really could lead to a sustainable cost advantage…. In economics jargon, this is known as a network effect. It's the reason that eBay has a stranglehold over the collectibles market and Craigslist dominates online classified ads.[6]

Needless to say Lee has no actual evidence of this huge productivity advantage, but he is at least trying to come up with a hypothesis that has some logical relationship to competitive efficiency.

The first problem here is that driver revenue productivity is fundamentally driven by major demand differences by time-of-day and geographic location, not the problem of driving twenty blocks to find a new customer when there was another customer only ten blocks away. A dispatcher at a traditional taxi company has the same information on the location of people who want cabs as Uber's app, and as noted, traditional operators could adapt software with the same functionality as Uber's if the additional automation would have a big impact on productivity.

But drivers who have just dropped off a passenger at the airport at 6:30 am (or anywhere at 8 am on a Sunday morning), or in a distant low density residential neighborhood, are likely to have a long wait before their next fare and there is absolutely nothing in Uber's business model that solves this problem.

The second problem is that the customer perception of shorter waits for Uber cars actually means ***Uber has a driver productivity disadvantage***. I wait longer for my Phoenix cabs than Uber customers because fewer of them are sitting around empty.

And the third problem is that this is neither a scale or network economy, and ***any appearance of "efficiency" is an artifact of the unsustainable excess capacity Uber has been subsidizing.*** There is absolutely nothing in the business model of Uber that produces Ebay/Craigslist type network economies.

As noted earlier, if urban car services had powerful growth economics here you would have seen strong tendencies towards market competition in cities dominated by dispatch cab services long before Uber. Lee is arguing that the dispatch company with the most cabs would gain a huge cost advantage due much better driver productivity; not a 1-2% type improvement, but as much as a 30% advantage. If so we would have lots of historical evidence of bigger companies capturing most of the traffic from smaller companies with higher costs and longer customer wait times.
This ***never*** happened; taxi companies large and small needed to ensure a close balance between their driver/vehicle capacity and their revenue base. If the biggest company added capacity wait times would fall but profits would fall faster because the efficiencies Lee thinks are powerful don't actually exist.

As with Thompson, Lee thinks that Uber can rapidly eliminate multi-billion dollar losses because he imagines they have the exact same scale economies as Amazon.

"Amazon's unprofitability during the 1990s was an illusion created by Amazon's aggressive investment in growth. Amazon was spending a lot of money on things like warehouses and new software that were going to take a few years to pay off….thanks to economies of scale in software and warehousing, Amazon's costs per book kept going down as the company grew…[Uber is] just pursuing an even more ambitious version of Amazon's strategy — that Uber's core business is sound, but Uber is investing heavily in things like expanding to India and developing self-driving cars."

Needless to say Lee provides absolutely no economic evidence here, and does not explain why my analysis showing that urban car service costs are overwhelmingly variable might be wrong, he just baldly asserts that if this worked for Amazon, it must fully explain what Uber is doing.

Amazon's worst losses were $1.4 billion in its fifth year of operations, but shrank rapidly thereafter, while Uber losses have been steadily growing and will be over $3 billion in its seventh year. If Uber had huge scale economies, its profit margin would have been rapidly improving; in fact Uber had no margin improvement whatsoever between 2012 and 2015, and its 2016 improvement was totally driven by unilaterally imposed driver pay cuts, not growth economies.

As with Thompson, Lee does not seem to have a clear idea of what scale economies are, or how they work, makes no effort to explain how his imagined future scale economies could quickly achieve over $3 billion in savings, and does not seem to care that his argument is totally inconsistent with all of the available data.

Perhaps, Lee argues, none of this matters because the big payoff for Uber investors will come from driverless cars.

"The real prize in the ride-hailing wars, then, isn't the conventional ride-hailing market itself. Rather, it's the opportunity to become the customer's gateway to the emerging self-driving car market. There are good reasons to think that most self-driving cars will be hailed on demand rather than owned by individual drivers. If that's true, having the most popular ride-hailing app will be a huge strategic advantage in the self-driving car market."

That's Lee's entire driverless car argument, and Thompson had made a similarly unelaborated and unsubstantiated assertion. There's no explanation of how (or when) he thinks driverless technology and markets will develop, no explanation of what "winning" this yet-to-be-created market will actually involve, and no evidence as to why Uber is better positioned to earn billions in profits than the other major companies investing here.

Uber had raised $10 billion of its $13 billion cash base before it made driverless cars a strategic priority, so there is no basis for claiming its investors saw this as "the real prize." Rationally, companies should not expand into riskier, more capital-intense markets until a strongly profitable position in its core market has been completely secured. At this point the main reason Uber and its supporters seem to be emphasizing them is to distract attention from Uber's inability to make money in its core business.

Tech press coverage of Uber: ignore economics, keep repeating the Uber narrative

The focus here has been on the Thompson and Lee articles, in the interest of seeing whether they had raised any issues that the Naked Capitalism series had missed, or whether they had presented new economic evidence that could constructively contribute to the public discussion about Uber's business model and its potential impact on economic welfare. They had not, but I want to reemphasize that Lee and Thompson remain "best case" examples of tech press coverage of Uber. There are scores of articles in the tech and mainstream media much, much worse than these, but these "best-case" examples help illustrate the power of Uber's narrative.

Unlike many other reporters, they are free of direct Uber influence, make serious effort (as they have done here) to consider different viewpoints and I have always found their work to be worth reading. ***But neither is yet able to present analysis or engage in debate centered on economic evidence.***

Their willingness to acknowledge that hard evidence about P&L results and industry economics contradicts the narrative is limited and grudging. Thompson is sure there's evidence out there showing that Uber is actually profitable in most markets and that its costs aren't actually higher than traditional competitors, even though he can't produce any of it. Lee is sure there's something in Uber's business model that is powerfully efficient, but he can't point to anything that would actually create major cost advantages or help explain $68 billion in corporate value. Both insist that since they consider Uber to be a "tech" company it must magically possess Amazon caliber scale economies and/or Ebay type network economies, but see no need to demonstrate that these magical economies actually exist.

A key issue here is that "tech" has morphed from one element of a larger business toolkit into a quasi-ideological/religious "movement" based on inherent virtues that the "non-tech" world lacks. As the broader Silicon Valley world has convinced itself that it is the avatar of progress and economic growth, and that "industry disruption" is virtuous regardless of actual impacts, most of the journalists and industry analysts embedded in that world have devolved from critical, objective thinkers to advocates and cheerleadiers for "our side."

Uber's narrative was designed to evoke these emotive/tribal loyalties, by portraying itself as the heroic defender of progress, innovation and disruption, engaged in mortal battle with the "evil taxi cartel" and the corrupt government regulators fighting to prevent the entrepreneurs who were using advanced technology to provide the world with better taxi service at lower prices. Despite hard evidence ($3 billion losses in year seven, massive failure of Uber China, no efficiency or scale driven margin improvements) many find it difficult to abandon the framing they bought into years ago.

Tom Slee (I would highly recommend his book "What's Yours is Mine: Against The Sharing Economy") has been following Thompson's arguments and the overall Uber discussion over the years. When Brad DeLong posted links to the Naked Capitalism series, to Izabella Kaminska's Financial Times article and to Thompson's Stratechery piece at his website,[7] Slee posted the following comment, which captures the ongoing refusal to reconsider the Uber narrative in light of growing economic evidence nicely:

It sounds like Ben Thompson is falling for the Uber bait and switch. Stages of which:

– Uber has a nice business as a status product (Uber Black Car ~ 2010)
– Uber Black may not be profitable, but Uber will displace taxis and be hugely profitable because of technology-driven efficiencies (UberX: 2014-2015)
– UberX may not be profitable, but UberPool will lead to new efficiencies in mass transit (2015-2016)
– UberX may not be profitable, but Uber is a logistics company and will rewrite the rules of delivery (UberEats, various speculative stories, 2013-2015)
– UberPool may not be profitable, but when Uber displaces car ownership the scale of the market will make it profitable (2016)
– Uber with drivers may not be profitable, but driverless cars will make Uber profitable (2014-)
– Driverless cars may not be profitable, but Uber is looking into flying vehicles (2016)

The Uber makes losses while maintaining credibility for bringing "the future" in some form or other.

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[1] Uber executive Emil Michaels “suggested that the company should consider hiring a team of opposition researchers to dig up dirt on its critics in the media — and specifically to spread details of the personal life of a female journalist who has criticized the company.” Smith, Ben, *Uber Executive Suggests Digging Up Dirt On Journalists,* Buzzfeed, 17 Nov 2014. Lacy, Sarah, *The moment I learned just how far Uber will go to silence journalists and attack women,* Pando Daily, 17 Nov 2014.

[2] Lee, Timothy, *Why Uber lost $2.2 billion in 9 months*, Vox, 9 Jan 2017

[3] Thompson, Ben, *Uber Losses (but China Gains?), Uber and unit Economics, Reconsidering Uber,* Stratechery, 20 Dec 2016. Stratechery is a subscription-only tech industry publication, similar to Pando (which has published numerous articles strongly critical of Uber) and The Information (which has said nothing critical of Uber but was the primary source of the Uber financial data presented in part one.

[4] Newcomer, Eric, *Uber’s Loss Exceeds $800 Million in Third Quarter on $1.7 Billion in Net Revenue*, Bloomberg, 19 Dec 2016. 2nd and 3rd quarter results were actuals; the 4th quarter number was Uber’s mid-December expectation of what the actual results would be.

[5] There is published evidence that Uber can easily manipulate customer displays to show many more cabs than are actually available. Hwang, Tim & Elish, Madeleine, Uber’s Algorithms and The Mirage of the Marketplace, SLATE, 27 Jul 2015, Rosenblat, Alex, Uber’s Phantom Cabs, VICE, 27 Jul 2015. The larger issue is that Uber’s app was never designed as a passive conduit between independent drivers and customers; it was always designed so that Uber (particularly if it achieves industry dominance) could totally control all of the supply, demand and pricing information taxicab markets require in order to function.

[6] Although he did not claim that Ebay/Craigslist type network efficiencies existed, Thompson has laid out similar arguments about superior Uber driver productivity in the past (Thompson, Ben, *Why Uber Fights*, Stratechery, 24 Nov 2014) and repeated the general claim in the article discussed above.

[7] DeLong, Bradford, *There is a serious debate about “Uber, floor wax or desert topping?”–excuse me: “Uber: grift or technological and organizational breakthrough?*, Grasping Reality Blog, 20 December 2106. Kaminska, Izabella, *The Taxi Unicorn’s New Clothes*, Financial Times, 1 Dec 2016.

http://www.nakedcapitalism.com/2017/02/can-uber-ever-deliver-part-eight-brad-stones-uber-book-upstarts-prpropaganda-masquerading-journalism.html

Can Uber Ever Deliver? Part Eight: Brad Stone's Uber Book "The Upstarts"– PR/Propaganda Masquerading as Journalism

Posted on February 16, 2017 by Yves Smith

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Brad Stone's new book "The Upstarts," is subtitled "How Uber, Airbnb, and the Killer Companies of the New Silicon Valley Are Changing the World,"[1] is the first book-length treatment of these companies. Stone is senior executive editor for technology at Bloomberg News; his previous book was 2013's "The Everything Store"[2], a corporate history of Amazon. Stone relies heavily on published news stories and interviews with Uber CEO Travis Kalanick and Airbnb CEO Brian Chesky. The material in the book is split roughly evenly between the two companies, although the comments below will focus on its coverage of Uber.

Does "The Upstarts" provide any new information or thoughtful arguments for people who have been following the Naked Capitalism Uber series, or who are interested in the wide range of issues raised by Uber's rapid ascendency? Unfortunately not. The major deficiencies in Stone's argument illustrate why tech industry and mainstream business media coverage has not only failed to investigate seriously the reasons for Uber's unprecedented growth but also has abandoned any pretense of journalistic independence to become a de facto advocate for Uber's corporate interests.

Stone openly admits he is not an independent, objective observer, but is out to tell the story Travis Kalanick wants told.

Amazon executives declined to talk to Stone for his previous book, and Stone describes how he proactively sought the cooperation of Uber and Airbnb for this book. Airbnb readily agreed to cooperate, but Kalanick initially refused in early 2015 ("There's no way in hell I'm cooperating with a book about Uber right now") and had to be wooed. Stone quotes himself (p.13) as telling Kalanick "If you want people to embrace a radical future in which they give up their cars you have to allow journalists to explain and demystify your story. If you want to change the way cities work, Uber must be understood." Kalanick remains skeptical, so Stone goes on to describe a narrative featuring backward politicians and regulators protecting "the big taxi guys" while Uber struggles to roll out its innovative new product.

Thus "The Upstarts" cannot be considered journalism; ***it is Stone's personal contribution to Uber's ongoing propaganda program.*** This is not to say that Stone presents a whitewashed or otherwise warped depiction of events; numerous Uber criticisms and missteps are noted and Stone's story would have no credibility if he hadn't. But Stone suggests criticism of Uber is overwhelming driven by vested interests protecting an inefficient status quo and each mention of Uber missteps (e.g. journalist harassment, lying about potential driver earnings) is immediately followed by emphatic claims about Uber's true virtues.

Stone insists that the multiple reports about Uber harassment of journalist Sarah Lacy and Johanna Bhuiyan under the direction of executive Emil Michaels were all totally fabricated; Michaels only wanted to “create a coalition for responsible journalism.” (p.262). Stone elided the fact that Uber claims that its drivers made over $90,000 a year was willful dishonesty by suddenly focusing on how a Uber recruiter on Chicago’s South Side was creating wonderful opportunities for people short on cash.(p319-21). Willful refusal to obey existing laws is honorable because those obstacles would prevent Uber from “unlock[ing] the true potential of an on-demand transportation service.” (p.299)

As is often seen with writers whose stories are based on access to key insiders, they can help flesh out bits of the historical chronology, and provide some background color on the personalities and styles of those insiders. “The Upstarts” provides a perfectly good (and very readable) overview of the “when” and “who” aspects of the Uber (and Airbnb) stories, but is useless to any reader trying to better understand the “why.”

Much of Stone’s story directly follows Uber’s longstanding propaganda narrative

“The Upstarts” endorses every aspect of Uber’s propaganda narrative, without offering any hard evidence supporting any of the claims.

Uber’s growth was based on powerful technological innovation. “[Uber and Airbnb] have scrawled in the annals of entrepreneurship the most memorable stories of a third phase of internet history—the post-Google, post-Facebook era of innovation that allowed the digital realm to expand into the physical one”(p.7) “The idea was this:..if you opened up the service to anyone with a car and allowed him to pick up passengers using a smartphone app? You could fill empty seats in cars, reduce the chronic congestion on America’s highways, and allow drivers to make money on the side.” (p196). “Because the brilliance of this seamless transaction [via Uber’s App] is so widely accepted in the LCD-lit halls of Silicon Valley that it inspired a surge of similar businesses in the fields of food delivery, package pickup, babysitting services, and so on.(p.7).

Stone makes absolutely no attempt to explain the underlying innovations, but wants readers to believe that the ability to order and track taxis on a smartphone was the most powerful innovation in transportation history. Since Stone does not care about cost competitiveness, he cannot explain whether these innovations had any material impact on productive efficiency, cannot explain why they have not made Uber profitable, and cannot explain why no other company in any other industry has been able to achieve major competitive or financial impacts from them. Stone simply ignores the question of whether Uber’s growth might have been driven by predatory multi-billion dollar subsidies for uneconomical prices and service levels.

Uber’s ultra-powerful business model will work anywhere in the world and will eventually displace car ownership. “Even Uber’s most fervent supporters had not grasped the true potential of the business. Uber wasn’t just taking passengers out of yellow cabs, it was growing the overall market for paid transportation.” (p.251) “Kalanick introduced a more inspirational articulation of the company’s mission…to offer transportation as reliable as running water, everywhere and for everyone” (p.261). “Uber was only halfway to its goals..(quoting Kalanick:) “what if I said there’s going to be no traffic in any major city in the US in five years?” (p.330)

Stone notes that Uber was forced to abandon China after suffering staggering losses, but instead of seeing that the business model might not be universally powerful, or emphasizing that it had burned a billion dollars of the investors’ cash, he cited Kalanick’s characterization of the China venture as “romantic” and a chance to “do something interesting and beautiful.” Since Stone completely ignores Uber financial results, he does not consider the possibility that a business model that lost $2 billion in 2015 and $3 billion in 2016 might not ever earn sustainable profits in a lot of places other than

China. He also does explain how Uber could ever lower their costs to the point of being cheaper than car ownership if after seven years of operations they are still billions of dollars away from being cheaper than Yellow Cab.

Uber's survival depended on heroically fighting "the big taxi cartel" and corrupt regulators. "Uber's expansion also measured the will of local governments to update antiquated transportation laws for a service that many of its own citizens desperately wanted. This was a litmus test for democracy, exposing whether regulators and legislators were more beholden to their own people or to powerful taxi interests and unions." (p.300) "The meeting thrust Kalanick into the thick of the familiar battle between new technology and the old, outdated ways of doing things" (p.122) As noted, selling this idea was part of Stone's sales pitch to get Kalanick's cooperation on the book, and there are unsubstantiated anti-regulatory claims throughout the book.

The idea that a company with $13 billion in funding from Silicon Valley billionaires had to wage a difficult battle with ""powerful taxi interests" who were fragmented and struggling to survive is too absurd to consider seriously. Even though he acknowledges Uber's growing use of lobbyists, Stone fails to consider whether the question of whether local politicians and regulators might be more beholden to the interests of a rich, powerful company than the interests of their own people, and whether this might raise any questions about the nature of democracy. Stone tells his readers that unlike regulators, Kalanick was a dispassionate seeker of objective truth. "Facts and intellectual arguments, not charm were his weapons, and he wasn't about to kiss any political rings." (p.191) However readers were then told that Kalanick's factual intellectual argument was that regulatory demands that Uber obey existing rules about insurance and safety was just like the decision making in the Soviet Union that led to the rationing of toilet paper.

As with past startups, losses will soon give way to robust profits. "Uber had discovered what startup gurus call the virtuous circle, the links between various parts of its business. Lower prices led to more customers and more frequent usage, which led to a larger supply of cars and busier drivers, which enabled Uber to further cut prices and put more pressure on competitors." (p.251).

Stone has no evidence backing his assertion about superior driver utilization, or that overall Uber efficiency improved because of this "virtuous circle", and the claim is directly contradicted by Uber's actual financial results. If Uber was achieving significant efficiency gains, operating profit margins would improve. Actual margins showed no improvement whatsoever between 2013 and 2015, and only increased in 2016 because Uber unilaterally reduced driver compensation.

Stone explains much of Uber's growth by "Travis' Law" which combines the "powerful innovation" and "regulation is the enemy of progress" themes: "Our product is so superior to the status quo that if we give people the opportunity to see it or try it, in any place in the world where government has the responsibility to be at least somewhat responsive to the people, they will demand it and defend its right to exist." If true, this would strongly support the hypothesis that Uber was "good for society" but Stone has absolutely no interest in helping his readers understand whether it is actually true.

Uber might be good for society if this alleged huge product superiority can be explained on the basis of huge efficiency advantages that allowed Uber to profitably produce superior service at lower cost, but Uber clearly is nowhere near profitability, and Stone completely ignores all questions of productive efficiency or competitive advantage. If marketplace competition has been badly distorted by the ability of Silicon Valley billionaires to subsidize billions in losses in order to drive more efficient producers out of business (as the Naked Capitalism series had documented in detail) than Uber is more likely bad for society, but Stone also ignores questions about subsidies and the pursuit of monopoly.

Stone fails to ask, much less address many of the most important questions that have been raised about Uber

Uber is the most highly valued private company in the world. While it has received more attention in the technology and mainstream business press than any previous startup, its finances and competitive economics are largely kept secret and poorly understood. Unfortunately Stone makes no attempt to even consider (much less present any hard evidence about) a wide range of critical economic questions including:

- **Will Uber ever be profitable?** Stone completely ignores all published evidence about Uber's multi-billion dollar losses, even though his Bloomberg colleague Eric Newcomer has been one of the main sources for these reports.
- **Does Uber's $69 billion venture capital valuation reflect the type of growth and profit potential it might have in the future as a public company?** Stone spends two sentences (p.296) mentioning that Uber's valuation had rapidly grown from $14 billion to nearly $70 billion but makes no effort to explain why Uber became the most highly valued private company in history, or to consider whether the unprecedented valuation is in any way related to unprecedented competitive power or profit potential
- **Why did Uber raise $13 billion from investors, a staggering larger amount than any previous startup had ever raised?** The only "explanation" Stone provides is a Kalanick quote citing the demands of "operating globally" (p.329). Although he has now written books about both companies, Stone never explains why Uber has required 1600 times as much pre-IPO funding as Amazon, which also competes globally.
- **What did Uber's investors think would drive significant returns on that $13 billion investment?** Stone reasonably places Uber's funding in the broader context of the post-Facebook tech startup investment frenzy. However, just as he fails to consider why Uber got so much more funding than other companies caught up in that frenzy, he makes no attempt to evaluate why those investors think Uber will produce massively greater returns than those other companies
- **Why has Uber remained private much longer than past startups, and shown almost no interest in an IPO that might return cash to those investors?** At several points Stone seems to presume that Uber had near-term plans to go public, but never explains why they have stayed private much longer than any previous tech unicorn
- **Are the major investor subsidies that fueled Uber's growth (by allowing it to offer more service at lower prices) justified by powerful growth economics?** Stone completely ignores the fact that traditional taxis need to charge fares covering the actual costs of trips while Uber fares have been massively subsidized by Uber's billionaire investors. Hypothetically these subsidies might be justifiable if Uber could rapidly "grow into profitability" but he fundamentally ignores the question of how Uber might eventually become profitable, and never examines whether Uber has the growth economics that powered growth and rapid profit improvement at startups (like Amazon); issues such as scale economies are never mentioned.
- **Will Uber provide drivers with higher pay and better conditions than traditional taxi operators?** Uber's "independent contractor" drivers are integral to Uber's overall business model, but Stone makes no effort to consider whether drivers will be better or worse off in an Uber-dominated industry. Stone notes (p.185) that in 2012 when Kalanick was still focused on more-upscale black car services, he didn't think mass market taxi service would work if Uber took the same 20% it took out of black-car fares. But Stone ignores the fact (also first reported by a Bloomberg colleague) that Uber now takes 30% of all fares, ***suggesting that drivers are now worse off than they had been before Uber entered the market*****.**
- **How is Uber similar to (or significantly different from) past Silicon Valley-funded unicorns that became profitable public companies?** Any comparisons with past startups would depend on the issues that Stone completely ignores such as cost competitiveness, growth economics, profitability, sources of ROI. Stone makes no effort to explain Uber (or Airbnb) in the context of other companies.

- **Is there evidence Uber could earn sustainable profits in competitive markets or does Uber believe that investor returns require the quasi-monopoly industry dominance it has been explicitly pursuing?** In his epilogue Stone rejects the claim that Uber (and Airbnb) are "merely replac[ing] one set of dominant companies with another" but makes absolutely no effort to explain why readers should share his optimism. His quote misrepresents the situation. Uber is seeking quasi-monopoly dominance of an industry has been highly competitive for a hundred years. His history of Uber provides ample evidence that Kalanick and his investors have long been focused on complete industry domination, and have ruthlessly attacked any company, regulator or journalist that might possibly stand in the way of Uber dominance. Nonetheless Stone completely ignores the question of how Uber would behave with quasi-monopoly dominance, or whether the loss of meaningful competition could be justified on the basis of substantially better service at substantially lower prices.
- **Are driverless cars critical to Uber's future success? On what basis could one Uber to become a major, profitable player in a future driverless car industry?** Stone usefully explains that Uber had never considered driverless cars until Google (an Uber investor) demonstrated their own development projects, and never thought to make serious investments in driverless cars until the Google-Uber relationship soured. But Stone does nothing to help readers understand whether driverless cars are now a secondary/incremental opportunity for Uber or (as Kalanick has said) an "existential challenge," or to understand any of the issues that will affect how a driverless-car industry might develop.

Stone does pose one of the most important questions about Uber, but fails to answer it, and fails to provide any of the evidence that might allow his readers to draw their own conclusions

The central question considered in the Naked Capitalism series on Uber is whether the shift from the pre-Uber urban car service industry to one dominated by Uber would improve overall economic welfare—would overall industry efficiency be significantly greater, would consumers in cities across the world have significantly greater service at significantly lower costs, would the risks from reduced competition clearly be offset by other gains.

Stone poses his own version of this central question about the impact on overall economic welfare. "Did the benefits of their [Uber and Airbnb's] dominance outweigh the well-publicized drawbacks? What was their true impact on cities? Were they good for society or bad?" (p.243).

Stone clearly wants his readers to believe that Uber has been good for society, but he is unwilling to explicitly say so, unwilling to clearly lay out how he thinks the tradeoff between benefits and drawbacks should be calculated, and unwilling to explain why he thinks the evidence justifies a positive conclusion.

It is impossible to answer Stone's "is Uber good for society or bad?" question without hard evidence about all this issues that Stone steadfastly ignores–productive efficiencies, the economics behind Uber's business model and expected investor returns, the sources and magnitude of competitive advantages over the operators Uber has been driving out of business, the sources and magnitudes of any scale or network economies, and evidence as to how Uber might at some point in the future be able to earn sustainable profits in competitive markets.

The issues directly relevant to answering the "is Uber good for society or bad?" are readily quantifiable—how much more service can Uber profitably provide than traditional operators, how much lower are the prices that Uber can sustainably offer, how much did Uber's innovations reduce the cost of providing taxi service? Readers cannot draw their own conclusions from Stone's evidence because he ignores all the major economic issues (Uber prices and services currently depend on massive subsidies—what price and service levels could Uber offer on a sustainably profitable basis?), and the pro-Uber benefits he emphasizes are vague (people really like the convenience of Uber's ordering app) and/or totally unsubstantiated (Uber has reduced urban congestion).

Stone's objective in "The Upstarts" is to sell his readers on his own version of Uber's PR narrative, a propaganda story that is not supported by any hard, verifiable economic evidence.

In Parts Six and Seven of this series, I presented a preliminary overview of longstanding Uber efforts to publicize a PR/propaganda narrative, and how it had enlisted a wide variety of outside journalists and tech industry observers to help them promulgate that story.

Nothing in the Uber narrative was based on any objective evidence of actual industry economics, and every aspect of the narrative is contradicted by the industry economic evidence presented in Parts One through Four of this series, e.g. the lack of profitability, the lack of powerful competitive efficiency advantages; the spectacular failure of Uber China and Uber's limited penetration of other international markets; the dependence on massive predatory investor subsidies and so forth. Thus the focus of this series has shifted from "What does the economic evidence tell us about the impact of Uber?" to Uber's narrative and the question of "Why has the public discussion of Uber almost completely ignored economic evidence."

I have deliberately used "propaganda" (instead of terms such as "marketing") to describe Uber's communication strategy, because one of Uber's key objectives is to frame public discussion around emotive tribal/ideological issues in a way that creates an us-against-then, good guys-versus-bad guys dynamic that blocks any attempts to investigate or debate issues based on objective economic evidence. Stone's belief that he can "explain" the growth of Uber without using any objective economic evidence needs to be understood in that context.

As discussed in Part Seven, one key element of Uber's effort to block objective economic analysis of its business model and competitive growth is its aggressive effort to suck tech industry analysts and journalists into this good guys-versus-bad guys dynamic so they will want to become active allies in Uber's fight against competitors and regulators. Uber has framed its market entry as a heroic battle between innovative technologists fighting to provide consumer a vastly superior product against a backward industry and the corrupt regulators protecting them from competition.

This framing engages the tribal loyalty of many in the technology industries who see themselves as avatars of progress and economic growth. Stone and the analysts cited in Part Seven (to use an expression Stone uses multiple times) clearly seem to have drunk this industry Kool-Aid, and was eagerly enlisted in Uber's fight. Unlike those analysts, who are willing to consider outside viewpoints and often produce critical analysis, Stone is a committed Uber partisan.

Stone uses extensive interviews with Uber (and Airbnb) executives to flesh out the company point of view, but his 335 pages do not include a single interview with anyone who has any understanding of urban transport economics or anyone who has critically examined any aspect of Uber's behavior. The Airbnb sections reflect the same tech enthusiast myopia and arrogance—it is not just that you don't need to evaluate any economic evidence to conclude that Uber and Airbnb are the good guys, you don't even need to think about the history or cost structure or competitive dynamics of the industry they will inevitably disrupt.

Stone's book also suffers from the structural problems of "access journalism." Journalists who focus on cultivating big-name inside sources (such as Kalanick and Chesney) will not get that access (and the cover stories and book contracts it makes possible) unless those sources have complete confidence that they will present the story that the sources want told.

By not focusing on business model economics, Stone incorrectly implies that much of Uber's strategy was hastily improvised in reaction to unexpected threats

In its early years Stone depicts Uber as strongly focused on developing a niche premium product that was not directly competitive with traditional cabs, and was ideally tailored for large, wealthy cities like San Francisco, New York and the capital cities of Europe. All of Uber's pricing (roughly double taxi fares plus surge markups on days like New Years' Eve), product standards (Lincoln town cars) branding ("Everyone's Private Driver") and regulatory approach (we should be governed by limo rules, not taxi rules) supported a business model focused on establishing a higher-quality taxi/larger-quantity limo service.

In less than two years Uber had clearly transitioned to a company that wanted to serve all urban car service customers everywhere, and totally displace all incumbent operators, and achieve global industry dominance. Stone, who has focused heavily on Kalanick's personality and style, and not attempted to explain the economics of Uber's business model, suggests these major changes in strategic direction were unexpected and haphazard, driven by Kalanick's sudden reaction to moves by regulators and competitors like Hailo, Zimride and Lyft.

Stone also suggests that little of the early investment in Uber had much to do with the (constantly shifting) understanding of market opportunities, and was mostly an intuitive sense that someone with Kalanick's personality would remain obsessively focused on investor returns through whatever market challenges unexpectedly occurred.

Stone is clearly correct that investors appreciated Kalanick's monomaniacal style, and that some investment may have been motivated by a sense of what was currently hot in venture capital circles. But Stone's hypothesis that Uber lacked an underlying strategic vision and was winging it in reaction to sudden, unexpected threats is contradicted by a lot of the evidence he ignores (and even some of the evidence he presents).

A company narrowly focused on providing limo service in a handful of big cities would not have gotten major attention from major Silicon Valley venture capital investors. That community can display herd mentality and is often guilty of the tech myopia/arrogance discussed earlier where the presumed power of "disruptive innovation" preempts the need to understand the economics of the industry you are trying to disrupt. But historical evidence strongly suggests they are extremely focused on possible sources of outsized returns, and would not have invested these staggering sums into a company unless its strategic vision was sharply focused on potential sources of outsized returns.

Stone's argument that the investors were simply wagering on Kalanick's style implies that business models and strategic visions are relatively unimportant and Kalanick would have been just as successful had he run Zimcar, Cabulous, Taxi Magic or any of the other failed ventures that preceded Uber.

A much more likely hypothesis is that Kalanick and his investors always had a global dominance strategy in mind; the initial focus on the upscale niche was always a preliminary step that would avoid serious competitive and regulatory pushback before a stable market position could be secured. Stone even notes that Kalanick's initial reluctance to commit to Uber full time was because he thought the limo model "was a good idea, just not necessarily a big one" (p.7) quotes Kalanick as early as 2010 as saying "I'll stop at nothing to see Uber go to every major city in the US and the world" (p.123) and notes that by early 2011 he had "expelled from his inner circle anyone he thought might stand in the way of Uber's manifest destiny to conquer the world."(p.153) The transition to a global, mass-market strategy may have been accelerated by those unexpected competitive moves, but was always part of the plan.

Uber's early investors would have been strongly attracted by the profit potential of eventual quasi-monopoly market dominance, and the idea that Uber's smartphone linked software platform might serve as the basis of that market dominance. Sherwin Pishevar, formerly a managing director at Menlo Ventures, became an original investor in Uber because he believed the company's platform could provide the basis for sustainable rent-extraction and the company's model could scale globally. "Uber is building a digital mesh–a grid that goes over the cities…Once you have that grid running, in everyone's pockets, there is a lot of potential for what you can build as a platform. Uber is in the empire-building phase."[3]

By focusing on personalities instead of competitive economics, Stone misses the fact that Kalanick and his investors have always had a clear and strongly coherent focus on the outsized returns that would be possible if they achieved quasi-monopoly dominance of the global car service industry. Kalanick could not have made the rapid responses to new threats that Stone described unless the longer-term global mass-market strategy already had the full support of his major investors, and no company can grow this rapidly without strong strategic alignment between owners and senior management.

By focusing on personalities instead of competitive economics, Stone misses much of the evidence showing that Uber's growth has not and will not be good for society. Kalanick's ruthlessness is not a mixed blessing that produced a series of damaging mistakes while the company was still an immature adolescent. Every one of those "missteps" (competitor sabotage, lying about driver salaries, journalist harassment, willfully disobeying laws, etc.) was fully aligned with Uber's overall efforts to defeat anything that might be an obstacle to its pursuit of global dominance. No Uber executive was ever disciplined and no Uber investor ever publically criticized any of these actions. They were all fully aligned with Uber's overall efforts to reframe public discussion around a heroic battle against the enemies of innovation and progress in order to block public discussion of Uber's extremely weak competitive economics. "The Upstarts" lays out a great deal of the history showing that quasi-monopoly industry dominance was always Uber's central strategic objective, and Stone fails to provide any credible evidence as why that outcome will not be bad for society.

[1] Stone, Brad, The Upstarts: How Uber, Airbnb, and the Killer Companies of the New Silicon Valley Are Changing the World, Little, Brown 2017

[2] Stone, Brad, The Everything Store, Back Bay Books, 2013

[3] "Uber doesn't just set passengers up with drivers. It's a company starting to dream of becoming a logistical nervous system for cities." Lagorio-Chafkin, Christine, *Resistance Is Futile*, Inc. Magazine, Jul 2013

http://www.nakedcapitalism.com/2017/03/can-uber-ever-deliver-part-nine-1990s-koch-funded-propaganda-program-ubers-true-origin-story.html

Can Uber Ever Deliver? Part Nine: The 1990s Koch Funded Propaganda Program That is Uber's True Origin Story

Posted on March 15, 2017 by Yves Smith

Yves here. For those of you who are late to this series, the underlying reason that Uber is not a bona fide tech success is that the fact that it has cars available at affordable (cheap) prices is solely the result of massive, unsustainable investor subsidies. There are no network economies in running any transportation network because beyond a baseline service level, there is an inherent tradeoff between service frequency (size of fleet and staff) and profits. Uber's app is trivial technologically and does not create a barrier to entry or confer scale advantages.

Even though Uber's long-term investment success would require it to achieve a monopoly or dominant position in an oligopoly, local transportation services do not have high barriers to entry. In fact, ironically, Uber's war against local licensed cabs is lowering barriers to entry. But if Uber were to achieve a dominant position in some markets, its end-game would require it to jack up prices considerably to cover its full current costs plus recoup past losses plus achieve an adequate profit level. That level of price would drive many current users away plus create a price umbrella that would encourage new competitors to jump in.

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Uber's business model is radically different from past tech unicorns and has (and will continue to) massively reduce overall economic welfare

Most of this series has focused on the economics of Uber, and how the growth of Uber has, and will continue to massively reduce overall economic welfare. Earlier posts presented a wide range of evidence documenting Uber's hugely unprofitable operations and how its growth had been driven by predatory behavior, its uncompetitive costs, its false claims about innovation and competitive advantage, and that investor returns always depended on industry dominance and anti-competitive market power.

The growth of Uber is massively misallocating resources because Uber is a ***less*** efficient producer of urban cars services than the operators it has been driving out of business. Uber cannot achieve sustainable profits or investor returns without achieving the quasi-monopoly industry dominance it has been aggressively pursuing and exploiting anti-competitive market power

The original growth of companies like Google, Amazon, Ebay and Facebook was driven by powerful competitive efficiency advantages and natural scale/network economies that generated massive consumer welfare benefits, although these welfare gains were somewhat offset by the ability to exploit market power once they achieved industry dominance.

Uber is radically different from these past unicorns because its business model is focused entirely on the second (exploit anti-competitive market power) part of this equation[1]. It skipped the difficult first part, which requires creating a totally new product that consumers value, or finding major efficiency breakthroughs so consumers can enjoy much more service at much lower cost.

As a result, Uber required a massively greater investment base than any prior unicorn in order to fund years of predatory subsidies. Amazon could fund much of its growth out of the positive cash flow generated by legitimate competitive advantages and scale/network economies. Uber's growth required $13 billion in cash — 1600 times Amazon's pre-IPO investment funding.

While these massive subsidies may have provided some temporary benefits to consumers and drivers they are not sustainable. In reality, they are hugely welfare-reducing because they are designed to destroy more efficient industry capacity and create the anti-competitive market power Uber's investors need in order to eventually earn returns on that $13 billion.

Achieving sustainable profits requires going beyond taxi "deregulation" so that Uber's investors seize full control over the laws governing taxi markets

Since its inception, Uber has understood that its biggest challenge was not the marketplace battle between Uber and Yellow Cab over taxi passengers, but between Uber's Silicon Valley investors and local citizens over control of the laws governing the urban car service market. Given the billions in profit improvement Uber needs just to reach breakeven, its investors cannot take the risk that cities respond to Uber dominance by reimposing pricing and service requirements, or other steps designed to restore meaningful competition.

Many have incorrectly referred to this process as a fight for taxi deregulation. In past transport deregulation processes, industry and government officials debated whether alternate industry structures (levels of competition and government oversight) would maximize overall economic welfare. Past reforms considered the needs of operators (taxi owners and drivers needed to make money) but also recognized that unregulated taxis would underprovide welfare enhancing benefits such as safety, insurance and access to jobs and housing that were poorly served by public transit.

In certain cases reforms designed to increase competition between independent providers subject to "level playing field" rules were judged to be the best way to increase industry efficiency and overall welfare. However, the importance of the government oversight to protect the public interest in maximizing welfare was never questioned.

Uber's objective was not to maximize competition subject to "level playing field" rules, but to seize control of the entire playing field and to eliminate meaningful competition. Uber was not presenting evidence showing how an unregulated monopoly provider would greater overall economic welfare than a competitive industry subject to regulations. It wanted to establish the absolute preeminence of its pursuit of shareholder returns over any public interest, such as protecting competition, safety, consumer protection, employee rights, or any other welfare enhancing benefits.

Uber's quest for market control faces both "factual economic" and "democratic process" obstacles. No one can legitimately claim that consumers would achieve Google/Amazon type service/pricing gains under Uber dominance. Uber dominance cannot be defended as something that resulted from the impartial judgement of the "market" since Uber has not shown that it can profitably produce better taxi service under competitive conditions. A battle between fragmented, poorly capitalized incumbents and Silicon Valley billionaires supplying billions in predatory subsidies is not neutral market competition.

All independent academic analysis has rejected the hypothesis that Uberesque *laissez-faire* taxi competition would improve industry efficiency or consumer welfare, findings that were confirmed when test cases of milder forms of deregulation in 17 cities failed to produce any public benefits.[2]. No democratically elected city government accountable to voters would openly eliminate all citizen oversight of local taxi service (including protections against monopoly power abuses) and grant total control of that service to private investors.

How could Uber's investors seize full control of urban taxi markets given uncompetitive economics, given the clear evidence that taxi deregulation would not benefit consumers, and given that no government accountable to voters would openly agree to major industry changes without compelling evidence of consumer pricing and service benefits?

The answer is that Uber is attempting to implement an innovative and disruptive strategy for achieving market control — a strategy radical different from every prior tech oriented startup — ***but those disruptive innovations have nothing to do with technology or the efficient production of urban car services.***

From its inception, Uber correctly understood that the battle between its Silicon Valley investors and local citizens over control of the laws and regulations governing the urban car service market was a political fight, and had to be fought using the techniques that had proven successful in political fights.

Luckily for Uber, pro-corporate/libertarian/objectivist oriented think tanks had conducted a major taxi deregulation campaign in the 1990s advocating the same complete elimination of all forms of legal/regulatory restrictions on the freedom of capital accumulators that Uber is seeking, and laid out a detailed communication program that Uber copied, almost word-for-word, when it began its fight for market control.

Most tech companies have "origin stories"; Uber usually points to times when Garrett Cook and Travis Kalanick could not immediately summon a taxi (a Paris tech conference, the Obama inaugural) when the idea "push a button, get a car" crystalizes. Brad Stone points to the time Cook noticed the graphical tracking software on James Bond's phone in the movie *Casino Royale*.

But Uber's growth was not driven by the user interface on its app; it was driven by its political strategy to take over an industry that it could not win on the basis of competitive economics. Thus Uber's real origin dates to the political strategy these think tanks established when they set out to eliminate all forms of government oversight over the taxi industry.

The 90s think tanks based their campaign on the type of political propaganda commonly found in large scale partisan campaigns, designed to obscure underlying agendas and motives. Relevant definitions of propaganda include a deliberate, systematic attempt to shape perceptions, manipulate cognition and direct behavior in ways that block interactive discussion in order to further the objective of the propagandist,[3] and communications designed to win over the public for special interests through a massive orchestration of attractive conclusions packaged to conceal both their actual purpose and lack of sound supporting reasons.[4]

Other tech companies convinced the world they would achieve industry dominance by providing independent outsiders with objective evidence of huge efficiency and scale advantages and demonstrating that they could profitably produce better service at lower cost.

Uber used its massive predatory subsidies to create the appearance of better service at lower cost, and a propaganda narrative that convinced journalists and industry analysts that not only was it hugely competitive but its eventual success was so inevitable that there was no need to investigate its actual competitiveness or financial results. Uber supplemented its propaganda narrative with actions establishing a hyper-ruthless corporate image, designed to convince any competitors, local governments or unconvinced journalists that any efforts to resist Uber's inevitable dominance would be futile.

The think tank taxi deregulation campaign blocked discussion of industry reforms based on economic evidence of potential impacts on efficiency and welfare with an emotive/tribal battle framing that precluded compromise.

Neither the think tank campaign nor the earlier 17 city deregulation push was the result of local citizens organizing to address local transportation issues. Both were entirely organized and financed by external interests who systematically repeated its key messages across a range of contexts and publications.[5]

The descriptions of the think tank taxi deregulation campaign below are based on twenty-nine articles from this period, twenty of which were published between 1993 and 2000.[6] Twenty-two of the pieces were published by pro-corporate/libertarian/objectivist oriented advocacy groups that received major funding from Charles and David Koch, including 6 by Reason and 5 by the Institute for Justice and 8 by similar state-level groups.[7] The others were opinion pieces in mainstream outlets that uncritically publicized the claims of those advocacy groups.

The higher-level political objective these papers was defined as the "liberty principle" ,[8] a belief that only a very narrow range of governmental activities were legitimate, fully consistent with the Uber/Silicon Valley political view that any governmental actions limiting the freedom of capital accumulators are illegitimate.[9]

The campaign worked to shift all industry discussion from a technical economic efficiency/consumer welfare frame based on industry economic evidence to a narrative where a single simplistic change could solve all industry problems. Attractive conclusions were highlighted — their central claim that regulation is the cause of all of the industry's problems is endlessly repeated – but none of the papers presented any supporting evidence based on actual taxi industry economics. For instance: "…[M]ore could be done to improve the quality of urban transportation and perhaps abate the current fiscal shortfall through the process of deregulation than through almost any other policy strategy."[10]

The papers all claim that ending economic regulation of taxis will lead to better quality service, lower fares, shorter wait times and increased employment. But since none of the papers even mentions concepts such as operating efficiency, utilization or productivity, they fail to consider, much the less explain, where these gains will come from, or how existing regulations might have caused these problems.

The papers assert that deregulation will solve the problems of long wait times in peak periods and poor service to lower-income neighborhoods, but none of the authors had any understanding of the actual costs of those services and nor made an attempt to explain how deregulation would reduce those costs. Regulation is attacked as an obstacle to innovation, but no one can cite any specific innovations that have been blocked.

The papers reframed all industry issues around an emotive black-and-white, us-versus-them ideological/tribal battle narrative. The fictional hero was the "entrepreneur", often portrayed as a struggling immigrant anxious to embrace the free market, who would transform taxi service but for the evils of regulation. This reimaged a fight for greater corporate freedom, funded by billionaires, into a fight to help an oppressed underdog. The impact of regulation on these storybook entrepreneur wannabes "is devastating. It impairs their ability to earn a decent living for themselves and for their families. It limits their opportunity to work for themselves, instead of for others. It destroys their dream of a brighter future."[11]

In reality these thwarted entrepreneurs were close to non-existent and consumers had not been harmed, since the few that did enter were not competitive with incumbents and quickly went out of business.[12] The fictional villains were the malicious forces of the "Cab Cartel" working in cahoots with corrupt government regulators. "The current regulatory scheme in Boston benefits no one but the existing medallion holders, their lobbyists, and their lawyers".[13] Framing the "heroic entrepreneur vs corrupt regulator" fight as a battle for progress, innovation and economic freedom precluded reasoned, factual discussion about alternate paths forward based on actual industry economics.

Having first reframed regulatory issues into a moral battle where data was irrelevant and compromise was unacceptable, the think tanks then expanded the scope of supposedly deleterioius regulations from the pricing and entry restrictions that had been the focus of every previous "deregulation" debate to *any* rule that might ever constrain the freedom of capital.

These papers specifically rejected calls "for more or "better" regulations [but] that an improved taxicab market can arise by removing regulation"[14] including regulations designed to prevent monopoly or protect public safety.[15] The think tanks insisted that giving the owners of capital complete, unfettered control of the industry would automatically eliminate any externalities and inefficiencies, implying there was no actual need to protect competition. "If it weren't for government interference, the laws of supply and demand would govern the taxi trade with almost frictionless efficiency: cabs would be plentiful, fares would be reasonable, and service would be available nearly everywhere it was wanted."[16]

The think tanks claimed they were just like the airline deregulation reforms of the 80s in order to obscure their much different objectives and to falsely imply taxi deregulation would produce the same large efficiency and consumer benefits. The papers included assertions such as "eliminate medallions and fares would drop, just as they did when the airlines were deregulated"[17]and "there is no reason, however, why the same [airline deregulation] principles cannot be successfully applied to urban transportation as well."[18] In addition to the false claim that medallion values had been directly extracted from consumers[19] (claims refuted in part six of this series), it claimed that the failed 17 city taxi deregulation test had actually been a great success.[20]

The 90s think tank taxi deregulation campaign failed to generate any support outside the ideological/political circles already predisposed against most forms of governmental activity, and thus failed to overcome the "democratic process" obstacles. Local governments and taxi industry participants may not have grasped the radical nature of the changes proposed in these papers, but knew that past deregulation efforts had failed to produce any benefits, knew that these papers had not provided any credible evidence of potential public benefits, and knew that any explicit political decision to totally abandon public oversight of taxis would be rejected by the public.

Uber adopted the think tank propaganda approach almost word-for-word as the foundation for its market control battle

Uber immediately adapted the 90s think tank propaganda narrative as its communication template because it directly addressed the obstacles Uber would face in its pursuit of full market control.

Uber needed to reframe all public discussion around an emotive, ideological/tribal narrative that would limit scrutiny of its uncompetitive economics and would also enlist a base of dedicated supporters, who would see Uber's battle against longstanding laws and regulations as a moral battle where compromise was unacceptable.

Uber needed a simple regulation-based explanation for the industry problems it would allegedly solve, but did not want anyone to reexamine the actual history of taxi deregulation, or to understand the huge difference between pricing/entry liberalization and the total market control they were seeking.

Uber needed to establish the image of a battle between cutting-edge technologists fighting to disrupt a backward industry so that people outside of its core of supporters would view Uber as the heroic good guys.

Uber needed to create a strong association between its disruptive innovation and its meteoric growth in order to create the impression they were following the proven model of Amazon and other successful unicorns and thus would inevitably achieve strong profitability and industry dominance just as they had. Establishing Uber as an innovative good guy with a business model just an innovative as Amazon would eliminate the need to investigate whether they actually had similarly powerful inventions, or to figure out why the losses investors were subsidizing were so large and persistent.

To build a base of ideological/tribal supporters Uber CEO Travis Kalanick emphasized the company's affinity with the tech industry and its libertarian/objectivist values. He highlighted his famous Silicon Valley investors, his use of Ayn Rand as his Twitter avatar, and described himself as a "trustbuster" and a "freedom fighter." "It's like Braveheart. Like, 'freeeeeduuuuuuuuum."[21]

Uber evoked the same us-versus-them imagery with entrenched and corrupt political forces, but substituted the heroic technology innovator for the heroic entrepreneur the think tanks had used. Kalanick described Uber as an avatar of progress "a transportation technology innovator, boldly going where no man has gone before;" its loyal supporters would be amply rewarded in the end because "ultimately, progress and innovation win."

Despite massive funding from Silicon Valley billionaires, Uber faced overwhelming disadvantages in its battle against a powerful "Taxi Cartel" (alternatively the "Taxi Medallion Cartel"). "Over the years, what I've come to realize is that this controversy exists because we are in the middle of a political campaign and it turns out the candidate is Uber" and the opponent is "an asshole named taxi." "Our opponent — the Big Taxi cartel — has used decades of political contributions and influence to restrict competition, reduce choice for consumers, and put a stranglehold on economic opportunity for its drivers". "When we do so, we don't do so fighting anybody. The fight is brought to us by those who don't want to have to compete, don't want to innovate and who like the status quo for what it is, which is not to the benefit of consumers or drivers."

Given the long-term objective of total market control, the propaganda narrative made the uphill battle with the evil Taxi Cartel into a struggle over core values where total annihilation of the enemy was a moral imperative. "Nobody likes him, he's not a nice character, but he's so woven into the political machinery and fabric that a lot of people owe him favors…We have to bring out the truth about how dark and dangerous and evil the taxi side is." Kalanick made it clear that truth and justice were totally on Uber's side and any accommodation with incumbent operators or taxi regulators was out of the question. "If you're operating from strong principles, you can compromise when the person on the other side is operating from principles you respect," he says.

Despite Uber's transparent interest in destroying all incumbent operators in order to establish global industry dominance, Kalanick insists Uber is just trying to increase competitive options. "When it's about protecting incumbent industry, when it's about providing less choices for citizens to get around the city, then there's less to talk about."

Following the think tank template, Uber emphasized attractive outcomes (e.g. hiring Uber would soon be cheaper than buying a car, Uber would eliminate waiting for cabs on Saturday night, and the company had “generat[ed] 20,000 new driver jobs every month” that had no factual basis and were totally inconsistent with actual industry economics.

Uber insisted that the emergence of an unregulated, Uber dominated industry had nothing to do with multi-billion dollar subsidies but was strictly the result of the free choices of consumers in a competitive market and therefore must reflect the efficient results that markets always produce. But as law professor Eric Posner points out, “…[this] is a response that any monopolist could make…But whether or not Uber does overcharge people now, sooner or later — once it displaces taxis and dominates markets —it will.”[22]

Echoing the struggling immigrants in the think tank narrative, it valorized its “driver-partners” as “small business entrepreneurs” who had been generously granted a unique opportunity. Uber forced drivers to bear much greater costs than traditional taxi drivers faced, could fire their “driver-partners” at will, and aggressively lied to them about their true earnings potential. In 2016, once drivers were locked into vehicle financing obligations, Uber slashed their compensation by over $1 billion.[23]

But Kalanick perversely defended a business model whose economics and service standards are controlled tightly by Uber as a way to empower workers. “When you empower drivers to own and operate their own vehicles, they can take control over their own income, their hours, and they can improve their lives.”

Uber’s public claims quickly coalesced into a PR/propaganda[24] narrative that can be readily summarized. Uber’s huge valuation was justified by its powerful business model that was based on cutting-edge technological innovation; it has created a totally new product category (“ridesharing”) an industry (the “on-demand” or “sharing economy”) that is totally different from traditional taxis; its meteoric demand growth was the result of consumers freely choosing their vastly superior product in open, competitive markets; resistance to Uber’s growth was due to the coalition of the evil Taxi Cartel and corrupt regulators who were willing to block major innovations and job creation in order to protect an inefficient status quo; that startup losses will soon give way to strong profits, just like past unicorns that rapidly grew into profitability; robust long-term growth is certain because its business model is so powerful that it can overwhelm competition in any city and any country and inevitably achieve global industry dominance and because it will become so efficient that it will significantly displace car ownership.

Uber’s PR/propaganda narrative was powerfully amplified by journalists following the tech industry

There is no legitimate, verifiable economic evidence supporting any part of Uber’s PR/propaganda narrative. But the effectiveness of propaganda campaigns does not depend on analytical rigor. It depends on their ability to get seemingly objective outsiders to amplify the message and give it greater credibility.

The media had completely ignored the 1990s think tank propagandists’ explicit attacks on all aspects of taxi regulation, but when the exact same narrative was repackaged in the context of an epic power struggle where cutting edge technologists backed by the best and brightest in Silicon Valley would inevitably overwhelm a backward industry, it became widely repeated in the tech industry and mainstream business press as if it was established truth that had been independently verified.

Uber's narrative exploited the myopia of tech industry journalists embedded in a Silicon Valley tribal culture that sees itself as the avatar of economic progress, who readily embraced Uber's framing of a heroic battle against a backward industry.

Given the awesome benefits that Silicon Valley-led "disruptive innovation" would inevitably bring, there was never any need to interview anyone knowledgeable about the industry being disrupted, or consider whether the Uber's claimed innovations had ever transformed any other industry.

Journalists focused on the wealth and status of Uber's Silicon Valley investors within the venture capital world. The presumption they must know what they are doing eliminated the need to find evidence that would explain how they had found tens of billions of economic value no one else had ever seen, or whether their interests coincided with any broader economic interests.

Part eight of this series uses Brad Stone's recent Uber/Airbnb book as an example of tech journalist bias. Stone, the senior executive editor for technology at Bloomberg News, manages to endorse every element of Uber's narrative while finding excuses for everything contradicting it (e.g. the massive failure of Uber China). Stone fails to mention Uber's multi-billion dollar losses or any other aspect of its uncompetitive economics, and cannot explain where profits or returns to investors might come from. Part seven of this series provides examples of much more open-minded, independent tech journalists, willing to acknowledge contradictory evidence and obvious Uber flaws Yet even they maintained that Uber it an ideal example of how the tech industry is the avatar of innovation and progress.

Since Uber's narrative provided a fully self-contained explanation of its inevitable success, even journalists without strong tribal tech industry ties had little need to undertake any independent investigation. Given Uber's overwhelming financial advantage, one could assume the battle had been decided before it started, and thus there was no need to dig into complicated competitive issues. The press treated Lyft (with a mere $2 billion in funding) as an also-ran and the entire incumbent taxi industry as a complete irrelevancy. Given its rapid growth, journalists accepted the Uber narrative implication that it was following the exact model that Amazon and Ebay had followed.

The huge industry-wide losses caused by the massive increase in less efficient capacity was never considered newsworthy, and was never blamed on Uber; since Amazon and Ebay had converted large initial losses to sustainable profits there was no reason to doubt that Uber would as well.

Uber's successful creation of the perception that it was the new Amazon/Ebay caliber tech winner created a virtuous circle, increasing the amount of highly favorable press Uber received. Aside from being locked out of access on one of the biggest stories on their beat, Silicon Valley journalists would also risk reputation in fighting the image version of a massive momentum trade.

It also meant that the press ignored the question of whether Uber actually had the Amazon-like scale economies needed to eventually achieve profitability, and ignored the arithmetic showing that an Uber recovery from its multi-billion dollar losses would constitute one of the greatest corporate turnarounds in history.

Uber's us-versus-them narrative also provided built in-responses to critics; people who raised questions about reduced driver earnings or whether the app was actually a technological breakthrough or Uber's eventual profitability could be dismissed as an Luddites who opposed empowerment and progress. Those who complained about Uber's ruthless behavior and disregard for legal requirements were bleeding hearts who did not understand what was required to create billions in corporate value. The combination of Uber's aggressive PR efforts, and a weak, disorganized and marginalized opposition created the impression that there was only one side to this story.

Of the thousands of Uber stories in the mainstream press, none included any interviews with independent experts on urban transport, none investigated the pros and cons of the longstanding taxi regulations Uber was disobeying, and none investigated whether “innovations” like Uber’s app or surge pricing practices had ever driven major competitive changes in any other industry.

Since Uber was popular (and traditional cab service was decidedly unpopular) with many of the urban elites who were a major audience for these media outlets, there was little motivation to expose the unsustainable subsidies that popularity possible, or to point out that the service they liked was reducing the already poor working conditions of drivers and also threatened affordable late night taxi service for low-wage workers.

Uber’s hyper-ruthless corporate behavior powerfully complemented its PR/propaganda strategy

Space does not allow the full story of Uber’s strategy for market control to be told here, but its highly effective PR/propaganda program was the key (in conjunction with its $13 billion investment base) to convincing the world that success was inevitable. By capturing the tech industry and mainstream business media, Uber rendered any local politicians that might have wanted to enforce longstanding regulations powerless, and ensured that outside critics questioning Uber’s business practices or competitive economics were never taken seriously.

To summarize briefly, the other key component to Uber’s market control strategy was the development of a highly ruthless corporate image. While the PR/propaganda campaign told the world that success was inevitable, Uber’s vicious behavior towards local politicians, competitors and critical journalists told the world that resistance was futile.

Recent articles about Uber’s rogue culture, exemplified by Susan Fowler’s descriptions of systemic protections for sexual harassers within management, the Greyball software used to obstruct local law enforcement and the Google/Waymo intellectual property theft lawsuit treat this type of behavior as aberrant and fixable because they consider it totally outside the context of Uber’s operations. In fact, this behavior and Uber’s monomaniacal focus on total market control is an absolutely central part of its business model. Change the culture, and you destroy what made Uber’s growth to date possible.

In an ideal world, competitive markets help allocate resources efficiently because consumers, workers and investors respond to information indicating which companies have better products, efficiency and profit potential. Uber’s pursuit of industry dominance and market control has been based on massive distortions of market information. Its multi-billion dollar predatory subsidies grossly distort competitive pricing and service information. It has gone to great lengths to hide the financial and competitive information capital markets require, and in several cases it has resorted to blatant dishonesty about things like driver earnings potential and market performance. Its PR/propaganda program was designed to replace legitimate economic evidence markets need with a narrative explaining its inevitable success that had been manufactured out of thin air.

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[1] The outside returns Silicon Valley venture capital community that funded Uber seeks has always focused on the monopoly power that could support significant rent-extraction and supra-competitive profits. For example Peter Thiel said “Always aim for a monopoly. It’s one big transgressive idea,

and you're not allowed to talk about it… From society's perspective, it's complicated. But from the inside, I always want to have a monopoly." Cook, J., *Peter Thiel: 'Always aim for a monopoly. I always want to have a monopoly*', Business Insider, 2 May 2015 Separately Thiel argued that "Actually, capitalism and competition are opposites. Capitalism is premised on the accumulation of capital, but under perfect competition, all profits get competed away." Thiel, Peter, *Competition Is for Losers*, Wall Street Journal, 12 Sep 2014

[2] The history of academic taxi deregulation analysis and test cases, with citations to original sources can be provided on request

[3] Jowett, Garth & O'Donnell, Victoria, Propaganda and Persuasion, Sage Books, 1,6,24 (1999).

[4] Sproule, J.M., Channels of Propaganda ERIC Press Indiana University, 8 (1994).

[5] A review of deregulation in Seattle noted that no local consumer or civic groups had been advocating deregulation; the chief proponent was a libertarian-leaning City Council member who argued that "the best way to improve taxi service to the public was…for the government not to interfere with private industry" and justified the move in terms of the recent success of airline deregulation. Leisy, C., Taxicab *Deregulation and Reregulation in Seattle: Lessons Learned*, International Association of Transportation Regulators (2001).

[6] Berliner, D., *How Detroit Drives Out Motor City Entrepreneurs,* Institute for Justice*,* (1996)*;* Boroski J, & Mildner G., *An Economic Analysis of Taxicab Regulation in Portland*, Cascade Policy Institute (1998); Bullock, S. G., *Baltimore: No Harbor for Entrepreneurs*, Institute for Justice (1996)*;* Cervero, R., *Deregulating Urban Transportation*, Cato J., 5, 219 (1985); Corcoran, T., *Taken For A $1 Billion Taxi Ride,* Toronto Globe and Mail, 5 May1997 (author was employed by the Consumer Policy Institute); Filley, D., *Taken for a Ride: How the Taxi Cartel and the State Are Disserving Denver's Economy*. Independence Institute Transportation Policy Center (1993); Goldsmith, S., *Regulation and the Urban Marketplace*, Regulation, *17*, 76 (1994); Gordon, P. & Richardson, H. W., *The Counterplan For Transportation In Southern California: Spend Less, Serve More*, Reason Foundation (1994); Hardaway, R., Taxi and Limousines: The Last Bastion of Economic Regulation, Hamline Journal of Public Law and Policy, *21*(319) (2000); Harris, L., *Taxicab Economics The Freedom to Contract for a Ride,* 1 GEO. JL & PUB. POL'Y, 195 (2002); Jacoby, J., *Break Open The Taxicab Monopoly,* Boston Globe, 5 Dec 1995; Kramer, J. E., & Mellor, W. H., *Opening Boston's Taxicab Market,* Institute for Justice (1996); Lephardt, G. & Bast J., *The Economics of Taxicab Deregulation*, The Heartland Institute (1985); Lopez, N. *Barriers to Entrepreneurship: How Government Undermines Economic Opportunity*, Institute for Policy Innovation (1999); Mellor, W. H., *Is New York City Killing Entrepreneurship?*, Institute for Justice (1996); Mellor, W & Kramer, J., *Open the Door To Portland's Taxi Entrepreneurs*, Cascade Policy Institute (1997); Moore, A. T. *Indianapolis's Road to Regulatory Reform: A New Path in Licensing and Permits*, Regulation, *21*, 49 (1998); Moore, A. T., *Competition and Entry in the Market for Taxis, Limousines, For Hire Vehicles and Related Services*, Liberty Justice Center (2013); Moore, A. & Balaker T., *Do Economists Reach a Conclusion on Taxi Deregulation?*, Econ Journal Watch, *3*(1), 109-132 (2006); Moore, A., & Rose, T., *Regulatory Reform at the Local Level*, Reason Public Policy Institute Policy Study, (1998); Novack, J., *Regulation at its Worst*, Forbes (1988); Selzer, I., *Abolish The Taxi Medallion System*, American Enterprise Institute (1996); Seymour, D., *The Case For Taxi Deregulation*, Frontier Center for Public Policy (2009); Staley, S., *Taxicab Regulation in Ohio's Largest Cities*, Buckeye Institute for Public Policy Solutions (1996); Staley, S., *How Cities Put the Brakes on Taxicabs: Stifling Regulations Thwart Entrepreneurs and Economic Growth,* Foundation For Economic Education, *48*, 147-150 (1998); Staley, S., *Toward A 21st Century Taxicab Regulatory Framework: The Case of Madison*, Reason Foundation (2000); Staley, S., *Taxi Regulation and the Failures of Progressivism*, Foundation for Economic Education (2012); Staley. S.,Husock, H., Bobb, D. J., Burnett, S., Crasy, L., & Hudson, W., *Giving a Leg Up to Bootstrap Entrepreneurship: Expanding Economic Opportunity in America's Urban Centers,* Reason Public Policy Institute (2001); Styring, William, *How Indianapolis won the War of the Taxis*, Indiana Policy Review, 31-35 (Spring 1994).

[7] The establishment of these think-tanks as political advocacy groups by the Koch Brothers is described in chapter 5 of Mayer, Jane, Dark Money, Random House (2016); the role of Mellor in the establishment of the Institute for Justice is described at 232-3.

[8] The "liberty principle", and the role these papers played in supporting it was defined by the editor of the Moore & Balaker paper (*supra* note 117) as the belief that any governmental activity outside the realm of police and military protections (including taxi regulation) must bear the full burden of justifying their existence, while any reduction in government activity (such as taxi deregulation) does not bear any burden of proof. "Certain interventions [including taxi regulation] that are hallowed and important to statist ethos and mythos are wrongheaded and fail to meet the liberal burden of proof." Klein, D. B., *The Forsaken-Liberty Syndrome: Looking at Published Judgments to Say Whether Economists Reach a Conclusion*. American Journal of Economics and Sociology, 71(5), 1250 (2012)..

[9] *Supra* notes 77 and 78.

[10] Cevero,

[11] Mellor & Kramer, but every article discussing "entrepreneurs" uses similar language.

[12] And could not have existed, given the dominant industry model of taxi owners leasing to independent contractors. When Indianapolis allowed open entry, only one person that wasn't already working in the industry applied for a license.

[13] Kramer & Mellor

[14] Boroski & Mildner

[15] Berliner, Bullock and Kramer attack regulations for mechanical inspections of taxicabs and the requirement that cab drivers obtain commercial licenses.

[16] Jacoby.

[17] Seltzer and Hardaway also argued that taxi regulation was justified by the success of airline deregulation.

[18] Cevero

[19] Kramer, Hardaway, Moore & Balaker;

[20] Most papers ignored the 17 city tests, but the ones that mentioned them cited the initial expansion of capacity, but failed to mention that the new entry was unsustainable, and that almost every city restored previous regulations. Cevero, Moore (1998), Seymour, Styring,.

[21] Citations for Uber's public statements are omitted here but are available on request

[22] Posner, Eric, *Why Uber Will—and Should—Be Regulated*, Slate, 5 Jan 2015. http://www.slate.com/articles/news_and_politics/view_from_chicago/2015/01/uber_surge_pricing_federal_regulation_over_taxis_and_car_ride_services.html

[23] See 2016 financial data summarized in part six

[24] The focus on "propaganda" is designed to highlight the enormous differences between Uber's communication program, designed to serve broad objectives related to industry structure and control and "marketing-based" corporate communication, focused on tangible product attributes (price, features) serving much narrower objectives related to consumer purchase decisions in competitive markets, or investor decisions in capital markets. The term "propaganda" is often misused to disparage communication serving objectives one dislikes, even though it is commonly deployed on behalf of all types of political objectives, likeable or not. Edward Bernays argued that propaganda was simply the "mechanism by which ideas are disseminated on a large scale," was central to all public relations practices, and (like all of education, business and politics) was not inherently ethical or unethical. Bernays, Edward, Propaganda, Routledge (1928) 20, 133.