



Basis Points – August 9, 2018

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Above the Fold

Tesla founder Elon Musk surprised the market on Tuesday when he tweeted his desire to take the company private at \$420 per share (the stock was trading at \$340 at the time). While many have debated the legality of the move and whether his actions would run afoul of SEC regulations, it is at best highly inappropriate for the CEO and founder of a public company, who owns 20 percent of the stock, who is engaged in a well-publicized war with short investors of his stock, to announce in the middle of the trading day, via only one social media platform, that he will buy all the company's stock, at a non-negotiated price that the board of directors has not yet approved. And to also claim that he has lined up \$70 billion in funding, with no proof. If all these actions are actually legal, then our securities laws clearly need to be updated for the times. The SEC actually ruled five years ago that a public company can release material news on a social media platform, as long as the news is released to normal news distribution services at the same time, which Musk did not do. Tesla stock jumped \$40 a share to \$380, before the stock was halted two hours later, but the company gave very little new information in their press release.

But putting the legal issues that could surround Musk and Tesla aside, the stock has since declined to \$360 a share. This 17 percent difference between where the stock trades today and the \$420 price that Musk mentioned shows that the market does not believe that this deal will happen anytime soon, or just needs a lot more information or confirmation before they bid the stock up. If the deal does happen, it would be the largest corporate take-private deal in history. The deal would probably need to be funded by a huge amount of private equity capital, as the large Wall Street banks all noted on Tuesday that they had not been contacted about providing large amounts of capital to Musk to complete this deal.

Three Things

- Dan Clifton, Strategas Research D.C. insider, reports that there is very little relationship between the strength or weakness of the U.S. economy and the results of midterm elections. Looking at historical midterm election results, there may even be an inverse relationship between economic growth and the number of seats a President's party loses in his first midterm election. In Dan's models, he predicts that Republicans will lose 23 seats in the House in November, putting the House at a near 50/50 split. Income growth has been a powerful predictor of presidential re-election, but the typical effect on midterm elections is minimal.
- The S&P 500 closed at 2,873 on Jan. 26, 2018. We are now within striking distance of that level, having closed at 2,857 last night. They are very similar levels, but the characteristics surrounding both market approaches of 2,873 are vastly different between late January and early August. In late January, the equity market was rising at a sharp angle, and a period of historically low market volatility was ending. And more importantly, there was very little, if any, worry about risk, volatility or equity declines. After seven months of market churning since then, there is now a more healthy respect for potential market volatility and risk. Most investors seem worried about a potential correction these days, even with two stellar corporate earnings quarters behind us, a subdued level of inflation, low unemployment and rising earnings estimates. A steady diet of trade war talk, flattening yield curve worries and concerns about the upcoming midterm elections have also tempered investor euphoria this year. At the start of 2018, street estimates for 2018 S&P 500 earnings hovered around \$155 per share (18.5x eps) and have since risen to a now consensus \$165 a share (17.3x eps). In January, 84 percent of stocks traded above their 50-day moving average vs. only 68 percent today, so there is room to run for stocks that have lagged since the January peak. Lastly, the yield on the 10-year T-bond increased 50 basis points in the first six weeks of the year, but has risen only six basis points since then.
- Toy Story: In last Friday's employment report, the economy added 157,000 jobs, shy of the 190,000 expected by economists, and one retailer may have been responsible for much of the miss. The category for toy and hobby stores fell by 32,000 workers, and economists say the closing of Toys 'R Us toy store chain could have been behind the miss. Toys 'R Us closed the doors on more than 800 stores on Friday, June 29, after filing for bankruptcy. Overall, the retail sector gained 7,000 jobs and the overall job report was strong, showing solid gains in professional and business services and in manufacturing.

Did You Know

With employers begging for workers in this low unemployment economy, *USA Today* reports that the California prison system is trying to prepare convicted felons for life outside their prison walls by teaching computer coding through its Last Mile job training program. Young inmates have been learning to write code through a first of its kind

program. Young inmates have been learning to write code through a first-of-its-kind pilot program at the Ventura Youth Correctional Facility in Camarillo, California. While other young people their age churn code in dorm rooms, these mostly black and Hispanic men and women, serving sentences for crimes like armed robbery and manslaughter, frequently come from neighborhoods where people go to prison more often than they go to college.

They're looking to break that streets-to-prison cycle by picking up new skills — JavaScript, HTML, CSS — that can lead to high-paying jobs after they're released. The program, started by technology industry veterans, is expanding to other prison populations and other states. Coding skills lead to jobs on the outside, and California inmates find work with tech startups in nearby San Francisco and Silicon Valley when they are released from prison. The coding program has graduated 393 students and boasts a zero-recidivism rate. One graduate works for Facebook CEO Mark Zuckerberg and wife Priscilla Chan's philanthropic venture.

Thalia Ruiz, a 20-year-old from San Jose at the Ventura Youth Correctional Facility, says The Last Mile coding program has set her on a new path. "I'm not gonna get out and keep doing what I was doing 'cause I'm just gonna end up in the same place that I started and that's not where I want to be." Zach Moore, 37, has been incarcerated since he was 15 and in the adult prison system since he was 17, for murder. He fought to get into The Last Mile, and he is scheduled to be released in November after 13 years of incarceration and marvels that he's going to work for a Silicon Valley company. "I didn't even think I'd ever get out of prison," he said.

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