



## Basis Points – September 18, 2018

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### Above the Fold

Apple staged its annual new product extravaganza last Wednesday, and displayed three new upgraded phones and a new Apple Watch with greater features related to monitoring consumer health. iPhone pricing came in at \$749 (XR)/\$999 (XS)/\$1099 (XS Max) for the three new models. The XR is now the low-end Apple model, made with less costly materials at a price that Apple hopes will appeal to lower-end budgets. At the higher end, analysts were skeptical last year that consumers would purchase a phone for \$999, but that model has been the company's best selling iPhone this year. Apple is adjusting its pricing strategy to steadily raise average selling prices for all its phones, and seems to be succeeding. Consumers still see the value in paying up for a better product with more applications and features. The upcoming holiday fourth quarter is the most important of the year, as phone sales in the quarter have averaged close to 80 million units over the past two years. The iPhone remains Apple's most important product, generating two-thirds of total Apple revenue.

Although most of the discussion this year regarding the strong stock market has centered around the strength of the mega-large tech stocks like Amazon, Netflix and Apple, the market gains have been very broad as well. Smallcap stocks have actually performed better than largecap this year, as the Russell 2000 smallcap index has risen 12.5 percent vs. the S&P 500's gain of 9.9 percent. Broad market gains are much better for the long-term health of stocks than a gain that is only concentrated in a few largecap stocks. Economic data and earnings growth have been widespread over many industries, so most smallcap sectors have gained from broad economic growth. Also, investors who are worried about global trade and tariff issues can gain exposure to more domestic-oriented companies with smallcap stock exposure.

### Three Things

- *Time Magazine* is being purchased for \$190 million by Salesforce.com co-founder Mark Benioff. Salesforce.com is a cloud software company that is the global leader in the very important category of Customer Relationship Management software. Salesforce.com revenue has grown sharply, from only \$1 billion in 2009 to \$12 billion in the last 12 months. Benioff will own *Time* as a personal holding, and states that he will not have any daily oversight of the magazine or its journalistic decisions. *Time Magazine* was founded in 1923, and grew strongly for most of its history, but the brand has fallen on hard times over the past decade as consumers have turned to the internet for their news and away from print publications. Benioff is the latest technology billionaire to buy a print publication, as Amazon's Jeff Bezos bought the *Washington Post* in 2013, and Lauren Powell Jobs bought a majority stake in *The Atlantic* magazine last year.
- The U.S. labor market is still very solid, as shown by the number of people who are quitting their jobs to take new positions elsewhere. The "quits" rate rose 2.7 percent last month, which is the highest level since 2001. The quits rate tends to lead wage growth, as companies begin raising pay to keep good workers on board. The high quits rate could be a positive for productivity in the economy, as job changes may mean better matching of workers with jobs. Job openings are also rising, up 1.7 percent last month to a 10-year high of 7 million jobs now posted but unfilled. Job postings is a leading indicator of job gains, as before a position is filled it must first be posted.
- Emerging markets have rallied lately. Emerging markets have been under pressure all year due to a combination of Fed tightening, U.S. dollar strength, falling commodity prices and global trade tensions. Countries with large current account deficits and declining currencies have been hit the hardest. We have seen particular weakness in Turkey, Argentina, Brazil and South Africa. However, this morning Turkey raised its benchmark interest rate to 24 percent, in order to aid its currency by targeting their very high inflation rate. The Turkish Lira has now rallied 10 percent from its low two weeks ago. Also, Argentina is in talks with the IMF to strengthen and accelerate payments from its \$50 billion bailout package. While we cannot assume that emerging market weakness has bottomed for the year, these are certainly positive developments and decrease the chance for a contagion effect on other markets.

## Did You Know

Be careful what you wish for: The sale of marijuana was previously one of the most pure forms of capitalism, as a voluntary trade between two parties without regulation. However, making the sale of marijuana legal has turned pot dealing into a much less sexy business than it used to be.

Although the sale and use of marijuana in the State of California became legal on January 1, the majority of pot sales in the state are still made from illegal dealers. Legitimate marijuana dealers who acquire state licenses and open retail stores to sell product are finding that the litany of rules and regulations of running an actual business are very onerous, expensive and time consuming.

Legitimate marijuana businesses are newly dealing with costs such as worker's compensation, legal fees to ensure compliance with a myriad of state regulations, required building and security upgrades, and costs to pass pesticide testing standards required by the state. Then there are the hefty taxes, which include a 15 percent excise tax in addition to sales tax and local fees that some say discourage customer spending and encourage illegal sales, where profit margins are wider. Accounting fees, human resources costs, and health and property insurance round out the business headaches for new pot business owners.

Many stores are suspected of running a legitimate retail outlet in the front, while selling illegal product out the back of the store, at much higher margins than the legal trade. The law enforcement effort has redoubled from trying to stop all marijuana trade in the state, to focusing on the still large illegal trade of the product. The laws have changed in many states, but the law enforcement challenges still persist. Fifty years after Woodstock, 2018 hippie crimes are now far less groovy: tax evasion, regulation non-compliance, non-payment of required employee benefits and business code violations.

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