Bell
Institutional Investment Management

EQUITY & FIXED INCOME OUTLOOK JUNE 2021

Taxation has been a hot news topic lately, often including the phrase, "paying your fair share." I grew up in a home with seven kids. Money was always tight. When there was only one apple, and we all wanted our fair share, Mom cut it up into seven equal parts. When the last bit of Kool-Aid was rationed, you can bet the glasses were placed side by side to make sure they were all even!

In terms of taxation, "fair share" seems to have a much different meaning than what I recall from my upbringing. As is the case in most developed countries, U.S. income tax rates have long reflected a progressive tax policy ("those that have more pay more"), rather than a flat tax policy ("everyone pays at the same rate"). The 2017 data from the Tax Foundation (data which does not reflect the impact of the Tax Cuts and Jobs Act (TCJA) signed into law by President Trump on December 22, 2017) shows that households earning $83,682 or higher (the top 25%) were burdened with paying 86.1% of federal income taxes. The 2018 data, which does reflect changes enacted by TCJA, shows this same group now paying 87% of federal income taxes. It seems that the tone from Congress toward these generous taxpayers should be more along the lines of appreciation – perhaps something like, "Thank you for already paying more, but we have to ask for even more." Demonizing this group does not seem like the way to cultivate harmony for all. Gratitude is probably out of reach, though, because 70% of Americans under the age of 30 feel the distribution of wealth is unjust. I wonder if this same percentage feels the distribution of effort, sacrifice and risk is also unjust?

Have economists reached a new level of understanding? Are we at the point where fiscal policies stimulate demand, while the risk of inflation, supply challenges and federal budget deficits remain irrelevant? A growing number of experts and politicians are claiming a new economic paradigm – even though, it must be said, it has always been risky to claim something has reached a new paradigm. The tech stock revolution of the late 1990s elicited this very declaration. In the aftermath, it was 13 years before the market sustained levels higher than those before the bubble popped.

In the end, I believe we will find that economics has *not* reached a new paradigm. In fact, I think it's only a matter of time before we find that it is "SSDD" – a phrase the seven of us Sweeney kids used among ourselves meaning, "same stuff, different day." While this is definitely not an official economics term, it's likely very accurate. Time will be the official arbiter of the debate.

Time is our key word here. As an investor, do I want to wait 13 years before sustaining an invested asset balance above where I started? Not really, especially if that period includes the stock market selling off 50% – twice (from March 2000 to April 2013, for those who want to visualize the time period on a stock market chart). To help during times of drought, investors often have had the shelter of fixed income bonds as part of their allocation. Back in March 2000, the yield on the 10-year U.S. Treasury bond was near 6%, offering an attractive source of income. That type of bond yield is nowhere to be found today, even in the riskiest junk bond indexes – but that has not kept investors from reaching for that income. Those investors who have done so have taken on an aggressive amount of risk in their portfolios. The Federal Reserve even released a statement recently noting their concern about the risk investors are taking in reaching for yield. This warning seems a bit disingenuous. The Fed, the master manipulator of low rates, continues to purchase $120 billion in U.S. Treasury and mortgage bonds each month.

Make no mistake about it: Capturing a source of income yield for clients is a regular topic at our weekly strategy meetings. There are pockets such as real estate, preferred stock, equity income and some bonds that offer a bit of shelter, but not to the degree that we would like to see as portfolio managers. To that end, we never give up doing the best we can for clients who have entrusted us with their future goals. A thousand "thank yous" for your business and your continued trust!

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