Joe Quinlan:
Good morning. This is Joe Quinlan from the CIO Office. It's November 12th and today I have a couple of guests with me. Mitch Drossman, who's going to talk about the Build Back Act from Washington and then Kirsten Cabacungan who's going to talk about The Book of Greats: Some Lessons Learned so we've got two great guests that are going to join us shortly. I'm just going to be real quick with some upfront comments. The big news this week - the headline CPI numbers much stronger than expected from The Street. If you saw the CPI, headline number increased 29% month on month and it's running now at almost a 12% annualized rate. We also saw a big jump month to month in annualized with the core CPI as well. So clearly inflation is top of mind when it comes to the markets and how the fed is going to approach this whether it's transitory, is it more persistent. No doubt about it, inflation is front and center. On the jobs front, the numbers continue to improve. Jobless claims came down this week, so the employment picture continues to improve. Average hourly earnings is picking up albeit real terms they're still negative. So when you kind of look across the landscape here in the United States late into '21, inflation is top of mind. Through the earnings season we saw a lot of companies pass on these costs but the costs are going to be persistent into '22 and that has The Street thinking about their earnings estimates for '22, '23, and beyond. It also has The Street very focused on the tapering could lead to tightening in the second half of next year, so there's a lot of cross currents but when you step back, the real economy, the US economy is plowing forward. We're looking for a re-acceleration in GDP in the fourth quarter offered off that soggy Q3 number. Growth is going to be led by consumers, capital expenditures, and we still have some spending which Mitch is going to talk about coming from Washington so it's a very kind of dynamic situation across all components of the economy whether it's the inflation outlook, the employment gains, increases in wages overlaid with a lot of consumer spending pent up demand as we head into the holiday season. Seasonally, we're in the part of the year where equities do well, whether it's share buybacks and dividends, we expect that to continue. In terms of portfolio construction from the CIO and the latest viewpoint and it's the pivotal year coming up in front of us but it's really more about that reflation trade, it's about the cyclicals. We still like energy, materials, financials but on the growth side we still like technology. Technology innovation still the United States/US companies being leaders in that space. So we're still much very focused on US large cap. We're looking at small cap as well as opportunistically as we head deeper and finish out this year and deeper into next year, but in general, the call remains to be in equities versus fixed income and to be in the quality names. We do think earnings are going to surprise on the upside to finish out this year and have good momentum going into the first half of next year. Albeit no doubt about it, inflation – where we go next is top of mind for the markets and what this means for the Federal Reserve. So speaking of the Federal Reserve and Washington, we have Mitch Drossman on today. Mitch is going to give us an update on the Build Back Better Act. So Mitch, can you just kind of take us through the last couple of weeks the White House has unveiled a framework for the social policy bill. What are some of the kind of nuts and bolts, some of the key tax measures that you're watching and investors should pay attention to?

Mitch Drossman:
Sure. Thanks, Joe. Let me just kind of a second introduction, Mitchell Drossman. I'm Head of National Wealth Strategies within the Chief Investment Office. So over the last week or so there's been kind of a flurry of activity and it feels like a sprint to the finish line but in actuality, it's really a marathon. We can go back well over a year ago when it was candidate Biden and he

had made some numerous tax proposals and we've continued on. There's been tax proposals, there's been kind of a formal budget, the house had a formal bill, and then just about a week or so ago, the White House in Treasury released their framework only to be outdone by the house's framework which was then updated the day after the house released its framework. So kind of feels like we're in the 25th mile of the marathon and we're almost at the finish line and that's awfully tough so hopefully nobody trips and falls before they make it to the finish line but I think the framework, what we're talking about now is really it's the house's framework. I think what it's known for is what is not in that framework. I want to go over a couple of things because it has dramatically changed the way we were in mid-September. No longer are there any changes to individual marginal tax rates on ordinary income. No longer are there changes to capital gains and qualified dividend tax rates. No changes to the estate and gift exemptions. There's no modification to the step up in basis. There's no billionaire's tax or let's call it the unrealized appreciation anti-deferral accounting. No change to valuation discounts. No change for domestic corporation rates and a number of other provisions - no changes to carried interest and no ban on private investments and IRAs to name just some of the items that were left out. So question really is what is in it? Well, it raises almost the same amount of revenue as the original September proposal, about $800 billion from corporations but it's much narrower in scope. On the corporate side there would be a proposal for 15% corporate minimum tax for large corporations, a 1% excise tax on stock buybacks, and lots of other provisions that really affect multinational corporations. On the individual side, the tax increases are proposed to raise approximately about $640 billion of revenue and again, those two are much narrower, affecting a much, much narrower set of individuals and trusts. That's a two tier surcharge, 5% if income is above $10 million and then an additional 3% if income is above $25 million, so somewhat kind of rarified air but for trusts those thresholds would be much lower, both, they would be set at $200,000.00 and $500,000.00 so you can see lots of trusts can get caught by this surcharge. This surcharge would apply to all income so it doesn't matter if its wages, capital gains, interest income, other than tax exempt income and they would not be able to be offset by itemized deductions for charitable deductions unless it comes to a trust that can have some of those offsets. Another proposal on the individual side is to expand the 3.8% net investment surcharge to active business income for high income individuals and then make a number of changes in retirement planned areas - forced distribution for large retirement accounts, restrictions on Roth IRA conversions, changes to the tax treatment for qualified small business stock, and then expansion of watch sale rule and constructive sale rules to include cryptocurrency. So that's just a quick rundown. Not a fully inclusive rundown but that's in general where we stand now with the latest house's framework. Joe?

Joe Quinlan:
So Mitch, having said all that, are there any potential tax changes that could still be added to the list? Is there anything that's definitely off the table because as you said, this is a moving target?

Mitch Drossman:
Yeah. These tea leaves are really tough to read. Nobody really saw this coming where all of those individual tax provisions were jettisoned. There was some talk of senate democrats that they were unhappy with marginal rate increases, but this was kind of a little bit out of left field to see such a tremendous restructuring and it changed and it changes quickly. We had the billionaire's tax in there for I don't know, not even 24 hours. So I think that these tax provisions,

I think that this is a really good base that the senate has to work off of. I don't think that there will be a lot of changes. Where I potentially see some changes, which was this was a surprise to me that they left out the changes in the estate tax exemption that's going to change in just a couple of years in 2026, so my thinking is I'm not quite sure why they gave up on that revenue and why they did not accelerate that change, so that's one perhaps that can be in there. The other is around state and local tax deductions. The house kind of expanded that. I neglected to mention that earlier and the house's proposal is to allow a deduction or to increase the cap from the current $10,000.00 up to $80,000.00 for tax payers and have that remain in effect through 2030. I think the senate is going to have their own kind of opinion on what SALT tax is or what the deduction should be. I think that there'll be some pressure whether to means test it or maybe to kind of right size that exemption but other than that, I think corporate and individual changes I think are largely going to stay in somewhat of the same parameters as we're seeing them in the house current framework.

Joe Quinlan:
Okay. Then Mitch, following up on that, do you see any proposed tax changes reverse from the tax cuts that we saw from the previous administration? So any proposed changes that reverse or respond to what we saw under the Trump Administration?

Mitch Drossman:
Yeah. I think that's going to be left for another day and so let me kind of just go back a bit here and I'll put the framework around this. In 2017 we saw the Trump tax changes. They lowered top marginal rates and kind of expanded the tax base by eliminating lots of itemized deductions and significantly curtailing the state and local tax deduction. So that remains in place. We don't see it change in the rate where we don't really see much other than the proposed change for the SALT deduction, so that's going to be needed to be addressed at some point in time. Remember the Trump tax changes sunset at the end of 2025 and automatically we would see a reintroduction of itemized deductions and we would see higher tax rate so congress will need to address that at some point in time but other than that, it's largely left in place. There is one provision that the Trump tax changes set in there again, to expire at the end of 2025 and it is being extended permanently in the proposed legislation from the house and that is the limitation on excess business losses for individuals that was set to expire again and that will continue on a permanent basis. So there's a lot of work that congress will have and perhaps it's just too much to tackle at one time but they will get around to this and kind of usually somewhat last minute but I think that they will get around to this in whatever 2025 or maybe even 2026.

Joe Quinlan:
Okay. Mitch, then just to quickly wrap it up before we turn it to Kirsten, so what are the next steps in the process to get this framework too and then what are the key risks to getting this bill passed? Where are we in that kind of time sense?

Mitch Drossman:
Yeah. Well this is the kind of question we're hearing kind of most is what is the timing of this? Just because the house has a framework and just because the house is likely to vote on that framework on November 15th doesn't mean a heck of a lot because it then has to go on to the senate. Even the November 15th vote is not certain. There are several democrats that say we

don't want to vote on this until we have an accurate revenue estimate and the CBO, the Congressional Budget Office, just released some news on November 9th saying that they are going to be releasing lots of revenue estimates by the end of the week but there are some other items that are far more complex and those will be perhaps following next week. So if we take some of these house members that were, they may not be able to vote on this next week because they may not have the full revenue estimate but nonetheless, right now it's proposed that the house would vote on this on the 15th, the next step it would go on to the senate. The senate would take a look at this really with a fresh set of eyes. I think more so on the spending side than on the tax side and I think on the tax side I think they will have their own opinion when it comes to the SALT deduction. So the senate will have also other obstacles in the way. Remember, we have to fund the government. That funding of the government expires on December 3rd. There will be a defense bill the senate will need to address and there's also the debt ceiling that may be an issue in December once again. So there may be some distractions before the senate kind of fully addresses it but once they do, it then needs to go back to the house. Remember, it's tax legislation pursuant to our constitution must originate in the house and that's why it started there, it's going to the senate, and it will make its way back. We are not at the finish line. Even if the house votes on this next week, it's still probably several weeks away. Joe, you asked. Let me just finish up. Some of the biggest risks. Well I'd say the biggest risk is that given the narrow or actually the split senate, every senate democrat has veto power over the Build Back Better bill and so it needs to be to everyone's liking and that's where things are going to get quite delicate, so there's lots of risks ahead in many different areas particularly on the spending side which we did not address but there's equally as well I would say on the tax side. It's going to get interesting.

Joe Quinlan:
Yeah, to say the least. A lot of drama yet to come from Washington. So thanks Mitch, for kind of helping us unpack that and also kind of laying out where we need to go next in terms of what to expect. That's the Washington drama. Let's turn it over to Kirsten. Kirsten has done a lot of work on The Book of Greats. She'll talk a little bit about that but Kirsten, tell us about the latest installment in our The Book of Greats series.

Kirsten Cabacungan:
Yeah. Thanks, Joe. Thanks for having me on this week. I think before I really jump into our latest installment, it makes sense to back up a bit and speak to our CIO workout process for a second. So at the start of the pandemic we had chartered out this path for the recovery which we believe included several phases starting with the liquidity phase where we saw the federal reserve jump in then we've had the bridge and the economic recovery phases where the fiscal side really matched that response that we saw from the central bank in response to all of the shutdown measures and restrictions that were put into place at the start of the pandemic and now we've entered this fourth phase out of five which we call the consumer pent up demand phase where we've seen the power of vaccines, the power of greater understanding of the virus, really support consumers, re-emerging into the economy over the last several months, and really seeing consumption shift not solely on goods, but also start to pick up within services and so now we're thinking about what does the longer term look like? What is the next phase of our recovery process look like? What does that new frontier look like? So over the course of the last 20 months or so we published many chapters within our CIO Book of Greats series where we

explored some of these developments/explored some of these phases during the recovery and in our latest installment which we call The Book of Greats: Lessons learned and the path ahead, we really wanted to revisit and take a look at some of these ideas and think about what were some of the key lessons that we learned over the last almost two years and really help frame those lessons out and use them as an anchor in our framework for what we think the path might look like ahead given everything that has unfolded over the course of the pandemic.

Joe Quinlan:
So Kirsten, having said that, what are some of the top lessons then from your list? What would you like to highlight?

Kirsten Cabacungan:
Yeah. We outlined seven lessons but I'll highlight just a few. One lesson that really I believe came into focus during the pandemic was human activity has profound effects on nature. I'm sure we've all read at length about the role humans have played in the climate crisis and their contributions to the increase in atmosphere concentration of greenhouse gases especially carbon dioxide, but what the pandemic really demonstrated was how profound the effect of human activity has been on nature. During that pandemic we saw periods of time where we saw many of these greenhouse gas producing activities pause – so that's transportation pause with planes grounded, we saw manufacturing pause with factory shutdowns, we saw the reduction in some electricity consumption with these giant offices in cities and large buildings effectively closed with people sheltered at home. During this short period of time we got to really experiment and see what the effect of the shift in human activity, what that effect might be on the climate crisis, but while over the in some cases a few short weeks and in some other cases a few short months, we did see some positive effects. What we really got to see was that the contributions from human activity that have compounded over a century or even more than that are much greater than what short term behavior shifts might be able to reverse. Really the pandemic has unveiled the magnitude of the challenges of the climate crisis and so despite these short term changes, we ultimately saw global temperatures in 2020 increase and really round out the last five years coming in at the hottest on record since 1850. So this really brings us to now and what this lesson means. It means that we need bigger and greater and more expansive changes in human activities to really match what's happening in nature. I think it also ties into your discussion with Mitch about the latest spending packages that are being discussed in government with a lot of the focus yes, about building back better but it's also building back greener. The CIO recently put out a piece with the sustainable impact investing team called Climate Change and Portfolio Construction: A Q&A on what investors need to know and it talks about despite the push over the last several years toward renewable energy, renewables still only account for a very small share of global primary energy consumption. I think it's about 5.7% of that share, and so there's still much more run rate to go and it means that clean energy related investments should become key beneficiaries in the years and the decades to come. I think this lesson also ties into another lesson that we highlight in this latest piece which is that we're all stakeholders now. I think we've seen more and more companies shift focus towards the social and sustainability issues in one part driven by the greater availability of an environmental social governance, ESG data and metrics, that have been used to measure companies on certain standards but also I think the other driver of this shift has been that the pandemic gave consumers and workers really time to reflect on how they want the businesses they interact with work for and invest in to look like and to

operate and it's brought more emphasis to the S within the broader ESG and it's really built this strong case for companies to embrace stakeholder capitalism where they owe not only a responsibility to their shareholders but also to the overall stakeholders, and so I think this will continue to transform the business landscape and even the goals of investors in the years and decades ahead. One last lesson I'll highlight. Shifting gears a little bit is this – it's the US-China rivalry no turning back. It's this idea that the relationship between the US and China, the tensions are far from resolved. I think there was much debate about what the position the new administration might take in the US - China relationship especially after the last several years of high tensions between the two super powers but with the inauguration of the new administration earlier this year, what became abundantly clear is that this rivalry between the US and China is far from resolved and has really ultimately reached a point of no return. The current administration had taken steps even further from what the last administration was focused on. The administration is not just focused on trade issues, but they're more broadly focused on the overall protection of democracy and who is ultimately going to set the tone along economic, geopolitical, and technological lines. So we've seen China make great progress towards making a claim towards this global leadership with various projects like the Belton Road Initiative and the Made in China 2025 initiative but at this point, this rivalry between US and China, it's really now focused on innovation technology competition and who will invest more, who will innovate more, and really sort of stake that claim to that leadership. So those are a few of the lessons and the ideas that we talk about in the latest piece.

Joe Quinlan:
Okay. Great, Kirsten. Remember, The Book of Greats: Lessons learned and the path ahead. It was authored by Kirsten. I highly recommend it. You can find it on our social media sites and other places. Kirsten, one final question. As we look ahead, how do these lessons come together and what picture are we drawing for the path ahead in the new frontier? Can you just talk a little bit about that?

Kirsten Cabacungan:
Yeah. I think what ties all of these lessons together is this idea of transformation and really technology as that ticket to get there. What the world in the next several years to decades will look like is obviously, ever evolving and it's hard to really give you the perfect picture of what it might be but what remains clear is that technology and the trends that were further embraced during the pandemic will likely continue to accelerate from this point. Like I mentioned, we'll see more investment in clean energy, we'll see more companies shifting from shareholder capitalism to stakeholder capitalism, we'll see greater thought about innovation especially from a geopolitical standpoint, and we've also entered this new policy era following these massive injections of stimulus from both the monetary and fiscal side, so there's a lot of transformation underway and I think technology is really at the core of that.

Joe Quinlan:
Very good. Kirsten, I might come back to you shortly with your one final comment but Mitch, let me pitch it over to you. Last question. So where you sit Mitch, and what you look at every day and people you talk to, what should be the main take away for advisors and investors and what are the investment implications from your point of view?

Mitch Drossman:
I'd say one, get an understanding of what it is being proposed and then thoughts about how to react to it. In terms of a potential surcharge for next year, there's a couple of easy things that you may want to think about either kind of smoothing income, accelerating gain or other income into this year. Again, keep in mind this is proposed and it can change but somebody needs to remain nimble because if these are enacted, it will be closer to the end of the year and not a lot of time to react to it. In terms of from a broader investment perspective, I can say is that given that there is no increase in marginal tax rates on domestic corporations - this is generally positive for corporations and corporate earnings given that most of the tax changes are affecting multinational corporations, they will slightly greater headwind for them as opposed to a domestic corporation. A number of other provision in terms of retirement accounts. Some of those do not go into effect until about six or seven years out so there's time to do some planning between now and then but for the most part, it's a general kind of wait and see as we see what steps the senate will take and then ultimately how the house bill will be reconciled with the senate bill. Quick overview.

Joe Quinlan:
Okay. Thanks, Mitch. Excellent. So Kirsten, same question for you. in terms of where you're sitting in The Book of Greats: Lessons learned, what are some of the key takeaways for advisors and investors and what are the investment implications for portfolio construction and that whole gamut?

Kirsten Cabacungan:
Yeah. Thanks, Joe. I think there are two things that I'll leave off with. One, like I mentioned earlier, this crisis just like every crisis that we've seen in the past, has really significantly accelerated trends and so that's really going to be technology, that's going to be digitalization of the economy, so there'll be more investments in this type of infrastructure – 5G, artificial intelligence, cloud computing, e-commerce platform. So we'll also see more investments in the cyber security infrastructure and these other technologies that sort of build off of these, so that's one component of it and that's one main take away. The second one is really more geared toward portfolio strategy and how a long term investor should think. It's a mantra that we've recycled time and time and again is that it's not about timing the market but time in the market and the market during the pandemic truly demonstrated the challenge with market timing investment decisions. So as of the end of Q3 of this year if an investor had missed the 10 best days since the start of 2020 then they would've seen a negative return of 24% instead of a 33% gain even with disruptive clients from February and March of 2020. So all this is to say that these trends in technology and these trends in lessons that we've learned over the course of the pandemic will continue to play out over the longer term horizon and we believe staying invested as long term investors is a key to that portfolio strategy.

Joe Quinlan:
That's excellent, Kirsten. It's a great way to kind of end it. So Kirsten and Mitch, thanks very much for your time and your insights today. I want to thank everyone that dialed in this Friday and have a great weekend ahead.

Thank you very much. That concludes the program.

Operator:
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