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THE OUTLOOK FOR INFRASTRUCTURE

FEATURE

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As we emerge from the pandemic, it's important to reflect on the past year and acknowledge the essential role—for better or worse—that government must play in preparing for (and dealing with) similar events in the future. In much the same fashion, infrastructure is another area where government must take the lead.

An increase in federal funding could create millions of jobs, improve the quality of essential services such as water, transportation, and communication, and make the U.S. economy more adaptable to challenges going forward—from climate change to technological disruption.

But, what exactly is the current state of infrastructure in our country? And more topically, what are the prospects for President Biden's infrastructure agenda?

The state of infrastructure

Talking heads in the media often cite our nation's 'crumbling infrastructure.' In reality, there's some truth to this talking point. Over the last 60 years, federal spending on infrastructure as a percentage of total spending has decreased from 5.8% to 2.5%.[1]

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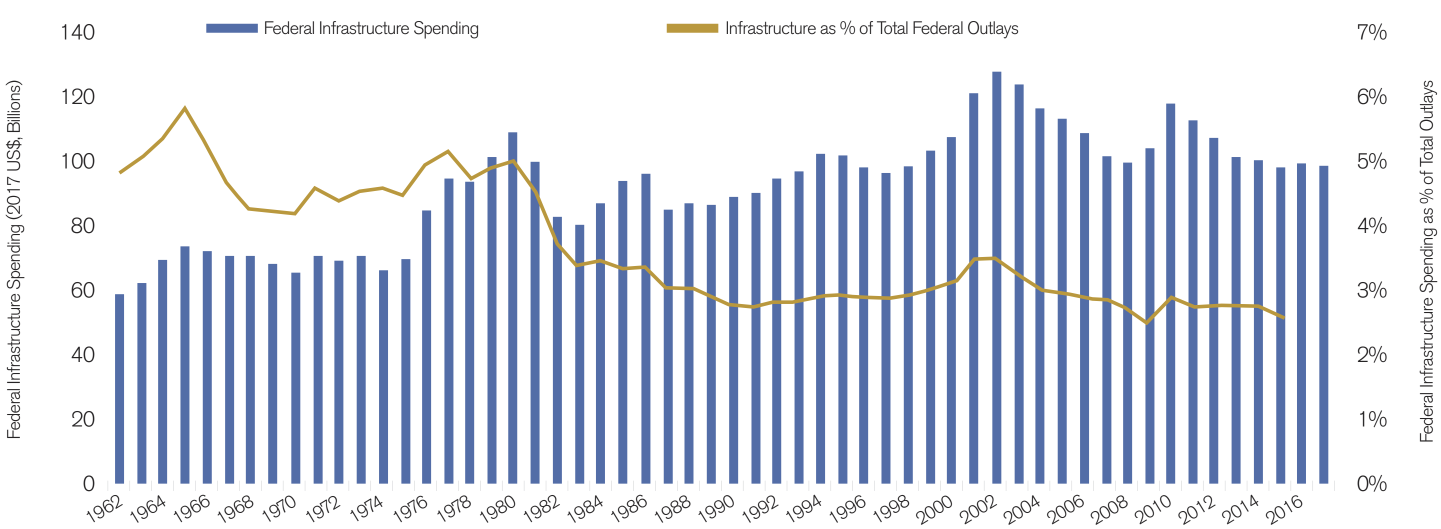
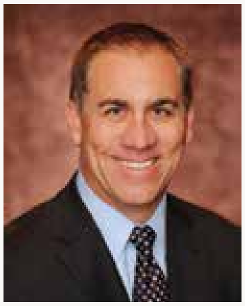
FEDERAL SPENDING ON INFRASTRUCTURE (1962-2017)



1 Congressional Budget Office, Goldman Sachs Investment Research

INFLATION - WHAT DO CONSUMERS NEED TO KNOW?



BY **Deron McCoy**
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Chief Investment Officer

The Consumer Price Index (CPI) came in red hot last month at 4.93%—marking the largest year-over-year increase since the summer of 2008. But if you recall, that brief era marked a time when oil prices were north of $120/barrel. If we strip out those high oil prices, we have to go all the way back to 1991 to see CPI prints in excess of 5%. Even if you alternatively chose to look only at the 'CPI ex Food and Energy' (which posted a 3.79% year-over-year increase) it serves to confirm the magnitude of the increase, as it's the largest posted increase since May of 1992.

But...

Something to keep in mind for the balance of the summer is that here in 2021, annual changes and year-over-year data points all need to come with an asterisk. Why? Well, it was just twelve short months ago that many were afraid to even emerge from their homes. There's no rocket science required to understand that as the world sheltered in place during the spring and summer of 2020, consumer spending was far from robust. At the time, many were even worried about deflation!

Now, fast forward a year and economies are reopening. Summer vacations are coming alive—with massive amounts of both pent-up energy and pent-up demand. Furthermore, consumers are flush with a massive amount of unprecedented stimulus. We want to have fun!!! And we've got the money to do it!

What does it all mean? The year-over-year comparisons make for easy, attention-grabbing headlines; juxtaposing today's mini euphoria to the dismal gray days of the early pandemic. No wonder the numbers are through the roof!

But fortunately, we can solve data feed errors. By simply comparing current data to pre-pandemic data from two years ago, and repeating for the entirety of the series, we see that the two-year base effects (comps) are much more in line with recent historic norms and ***less than half of the inflation we saw in the early 1990s***.

What's the takeaway? Current inflation isn't anywhere close to a repeat of the late 1970s (nor even the early 1990s), but merely a return to normal after the near deflationary experience we all suffered thru in 2020. While we may get some sticker-shock this summer as the globe squeezes two years of demand into two short summer months of supply, prices will tend to return to normal as the economy and society fully returns to normal in 2022.

Even though this inflation isn't terrifying, it's still a move higher from the recent past. What effects will it have on individuals and their portfolios?

In 2020, the emphasis was on 'working from home' at the expense of 'having fun'. Therefore, prices for laptops and desks (and home improvement) were the key beneficiaries. But here in 2021, expect prices to run up most in areas tied to leisure and entertainment, as we all seek to reintroduce some fun back into our lives.

Looking further out, expect interest rates to rise even further after already posting a sizeable increase over the last twelve months. Why? As society gets back to normal, we expect markets to get back to normal as well. And a normal functioning bond market (specifically intermediate-term interest rates) entails positive yields after accounting for inflation. In other words, bond yields should be higher than inflation prints. Also, monetary policy (short-term interest rates) should follow along and move higher as well. While it might be a bit premature this year, perhaps in late 2022 or 2023 investors can expect some modest levels of income on both bank accounts and money markets, with subsequent annual increases thereafter.

But on this path back to normal, investments tied to ***current*** levels of interest rates might suffer some setbacks. Unlike your mortgage where locking in today's low rate for 30-years might make sense, locking in today's low rate for a 30-year investment certainly doesn't. Instead, investors will want to use shorter dated bonds that will be able to mature in that higher interest rate environment in order to repurchase and lock in the then higher level of rates. Or better yet, own bonds today that have a floating coupon which will ratchet higher in the years ahead.

Outside the bond market, consider seeking out investments that do well in a higher inflationary environment. Commodities and commodity stocks (i.e., natural resource equities typically found in the Energy and Materials sectors) tend to do well. The machinery (typically found in the Industrials sector) needed to mine those commodities should also benefit. Additionally, financials and bank stocks should continue to outperform since the sector is most closely correlated to

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I believe successful wealth management is the result of an ongoing collaboration between investor and advisor, built upon trust and maintained according to the highest standards of integrity and expertise.

Brian D. Holmes,
MS, CFP®, CMFC, AIF®, *President & CEO*

ABOUT SEIA

Signature Estate & Investment Advisors, LLC® (SEIA) is a Registered Investment Advisor firm offering Investment Supervision and Financial Planning Services tailored to align the unique needs of affluent individuals and corporations. Fundamental experience and professionalism enable the financial advisors, with SEIA's research and support staff, to design a financial plan or investment portfolio to align the client's goals.

Welcome Back

SEIA is planning to welcome back our clients after the Labor Day Weekend. Please check with your financial advisor for further details.

INFLATION *continued from page 2...*

higher interest rates. These four sector stalwarts dominate the Value index—so perhaps look for the next leg of the cycle to reward these names rather than the dominant themes of the last cycle—namely Growth, Technology and FANG+.

While betting against the dominance of Apple, Microsoft, Google, and Amazon seems like a fool's errand, it's this exact dominance that might put those firms in the crosshairs of Washington D.C. But no matter the political outlook, the inflation and monetary outlook argues for at least a balanced approach to your asset allocation for the next leg of the business cycle.

A MUCH NEEDED RETURN TO NORMALCY

While it feels like a lifetime, just twelve short months ago we were firmly in the teeth of the COVID pandemic—with little but uncertainty on the horizon. A year later, 172 million Americans (more than half the country's eligible population of ages 12 and up) are now fully vaccinated, and nearly two-thirds (61%) have received at least one vaccination.[1]

For all intents and purposes, the country has fully opened up for business, with most states dramatically easing (and in many cases completely eliminating) their pandemic restrictions. Restaurants, nightclubs, and sports venues are scrambling to hire staff as the entertainment industry comes back online. Kids will be heading back to school in person come the fall. And the nation continues to add

1 U.S. Centers for Disease Control (CDC), June 8, 2021

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A LARGE PERCENTAGE OF U.S. INFRASTRUCTURE WAS BUILT IN THE MID-20TH CENTURY AND SIMPLY DOESN'T HAVE THE CAPACITY OR RESILIENCE TO MEET CURRENT DEMAND.

Since 1998, the American Society of Civil Engineers has graded the condition of U.S. infrastructure by category, and attempted to estimate the cost of repairs and needed upgrades. In 2021, the nation received a C- (defined as 'mediocre and requiring attention'). Categories receiving the lowest marks include dams, levees, roads, storm water, and transit. Ports and rail systems, on the other hand, received the highest marks.

A large percentage of U.S. infrastructure was built in the mid-20th century and simply doesn't have the capacity or resilience to meet current demand. For example, the average age of our nation's dams is 57 years. Similarly, most of the electricity grid was constructed in the 1950s and 1960s, and wasn't engineered to meet today's demand or sustain the effects of severe weather events.

Looking beyond our borders, the U.S. lags behind other major economies in both infrastructure quality and level of investment—ranking 13th globally as of 2019.[2] Of even greater concern is that in an increasingly internet-dependent economy, we currently rank 27th in information and communication technology adoption.[3]

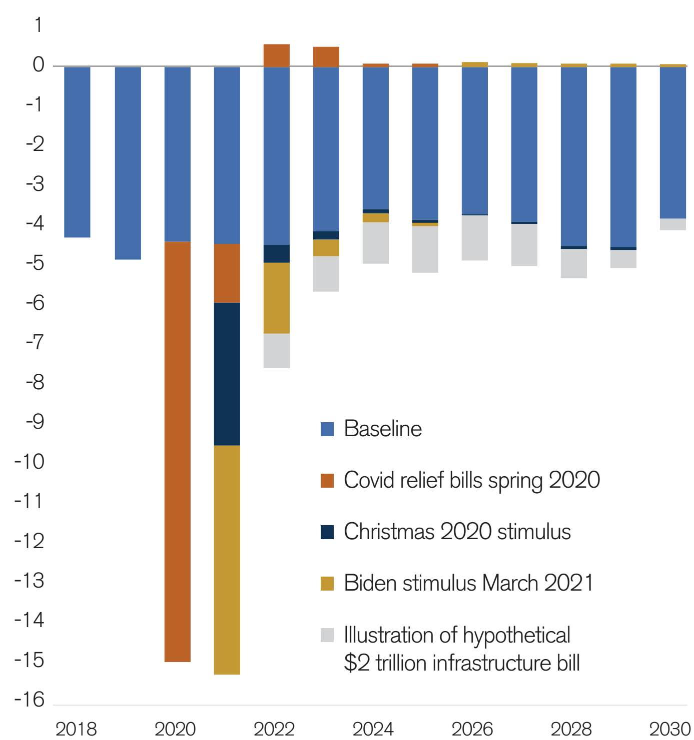
Of course, infrastructure needs have evolved over time. In the 18th century, rivers and canals were the most important modes of transportation. Those were supplanted by railroads in the 19th century, which in turn gave way to highways and aviation in the 20th century. In the 21st century, however, physical travel has become less critical as 5G and telecommunications take center stage—requiring significant ongoing investment to remain globally competitive.

The *American Jobs Plan*

Spending on infrastructure is inevitably linked to politics. Most people agree that infrastructure spending is necessary, but there can be great disagreement around the details—which brings us to the proposed American Jobs Plan. The Biden administration introduced this $2.3T spending package back in March. The plan includes a combination of traditional infrastructure spending (for roads, transportation, and other shared public facilities) along with nontraditional infrastructure—projects not historically funded by the federal government or considered within the definition of infrastructure. These include expanding care for the elderly and people with disabilities, producing or retrofitting affordable housing, green initiatives, health insurance affordability, access to community college and more.

The Biden administration proposed paying for the American Jobs Plan by reversing large parts of the Tax Cuts and Jobs Act implemented during the Trump administration. In summary, the plan would bump up tax rates on corporations and make it more difficult for companies to avoid taxes by going abroad. Unlike other recent stimulus bills where the goal was to boost economic activity as quickly as possible, the proposed infrastructure spending would take place over the course of years rather than months and would extend well beyond Biden's current term.

Change to US federal budget deficit as a percentage of potential GDP[4]



Negotiations are ongoing between the Biden administration and Senate Republicans. Recently, Republicans countered with an infrastructure proposal of their own carrying a much lower price tag and excluding all of the non-traditional infrastructure items. While we expect negotiations to continue through the summer months and many details to change between now and the passage of any legislation, the bottom

2 World Economic Forum
3 World Economic Forum
4 Congressional Budget Office (CBO) and BNP Paribus

line is that Democrats have unified control of government (albeit by a razor thin Senate majority) for the first time since 2010. There's a good chance they may take advantage of this control while they have it.

WE BELIEVE OVER THE LONG TERM, BETTER PROSPECTS FOR FUTURE GROWTH SHOULD HELP TO OUTWEIGH ANY INCREASE IN CORPORATE TAXES.

As we know, few major proposals ultimately get done without a deadline or a sense of urgency to push the process along and force politicians to compromise. In this case, there are some key dates in late summer or early fall related to when recesses occur and current transportation funding expires.

Winners and losers

In a vacuum, increases in taxes reduce cash flows for corporations, so act as a headwind for stocks on the surface. But, the burden of tax increases will not be equal across companies. For example, pharmaceutical and semiconductor companies have the greatest tax risk from higher taxes on worldwide income. Conversely, companies already paying a high tax rate with most of their revenues generated domestically have the least to lose. This includes companies like railroads, financial exchanges, and apparel. Beyond immediate tax effects, traditional infrastructure companies involved in building materials stand to considerably benefit from increased investment. If we examine the big picture, infrastructure investment should boost the productive capacity of our economy as a whole. We believe over the long term, better prospects for future growth should help to outweigh any increase in corporate taxes.

In summary, there's a great deal of room for improvement as far as our infrastructure is concerned. Not only do traditional roads and bridges need upgrading, but also technology, as we try to keep our systems safe from cyber-attacks, plan for the future, and try to remain competitive globally. Negotiations will continue to heat up in Washington over the summer months. There will certainly be some modifications along the way. The winners and losers will likely change depending on the ultimate details—so we will continue to closely monitor the situation and manage client portfolios accordingly.

RETURN TO NORMALCY *continued from page 3*

airline capacity (to 18.7 million seats); operating today with more than 80% of the capacity it had pre-COVID.[2]

Of course things will never entirely go back to the way they were in 2019. Considering 1 in 5 of us has lost someone we know due to this pandemic,[3] we'll never be exactly the same people we were before. But many of us have come to the realization that perhaps in a lot of ways things can be better.

Embracing a fresh perspective

Working remotely isn't just feasible for countless professionals, it's preferable—simplifying our lives, saving time and money, and eliminating the stress of our daily commute. The past year's mainstreaming of video platforms such as Zoom will greatly reduce the need for extensive business travel. And many of us have used the past year as a chance to slow down, breathe, and reconnect with our nuclear families.

Of course there will be speed bumps along the way—in our personal lives, in our work lives, and in the economy and investment markets. After more than a year without socializing or participating in everyday tasks, it will take time for many people to readjust and reacclimate. Only time will tell whether a year-plus of remote learning has any lingering impact on our kids. And we've witnessed first-hand the incredible power of technology to connect us during the worst of times.

Yet despite all of the struggles we've endured, here we are coming out of the tunnel into the sunlight. More than 6 million Americans traveled during the recent Memorial Day weekend. Both searches and reservations on Airbnb have spiked in Q2 as travel restrictions get lifted and people yearn to travel again. Bars and restaurants are near capacity. The beaches are packed. And a late-May study conducted by CNN Business and Moody's Analytics shows the U.S. economy is 90% of the way back to where it was before the pandemic began over a year ago.

That sense of hope and optimism you're currently feeling? It's not only justified; it's well-deserved. We wish all of you and your families a joyful, safe, and adventurous summer.

2 OAG Aviation Worldwide Ltd, June 7, 2021
3 Associated Press-NORC Center for Public Affairs Research, March 2021

SIGNATURE FUND *for* GIVING

The Signature Fund for Giving ("Fund") is dedicated to enhancing SEIA's relationship with our partner organizations to empower our community's youth.

SEIA and SFFG are proud to announce our partnership with the Foundation for Financial Planning where our CERTIFIED FINANCIAL PLANNER™ (CFP®) designated Advisors will provide pro bono financial planning to our communities most financially vulnerable members. We share in the Foundation's mission in providing access to financial literacy in an effort to create financial stability and are excited to be a part of their phenomenal platform.

We invite you to learn more about the Foundation's mission through their website – www.ffpprobono.org.

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If you have any questions regarding our fund or how to participate, we invite you to contact Hayley Wood at 310-712-2323 or hwood@seia.com.

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