



One Big Beautiful Bill

By Eduardo Cortes, CIO

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On Tuesday July 1, the Senate passed President Trump 2.0's signature legislation, the House ratified it quickly, and the President signed it into Law on July 4. Improperly named the One Big Beautiful Bill Act, the legislation delivers one essential policy victory for the U.S. economy, the extension of the corporate tax cuts enacted during Trump's first administration, the Tax Cuts and Jobs Act (TCJA). Many adjectives may be used to describe the rest of the bill, although beautiful might not be one of them.

The bill was opposed by every democrat and 3 republicans. A legitimate criticism is that it does not do enough to reign in the deficits Washington willfully ignored over the last decade. However, that complaint should be leveled at the unwillingness to chip into entitlement spending, not the avoidance of a massive tax hike for the economy.

In our Q4 2017 letter after the passage of the TCJA, we wrote, "we believe this legislation will prove to be a seminal measure for the U.S. economy based entirely on the reduction in the corporate tax rate." In addition, we cited the capital investment benefits countries like Ireland enjoyed because of their low tax rates. Despite the onset of Covid in 2020, the level of domestic non-residential fixed investment rose at a healthy clip as the economy exited the pandemic. The assurance of a competitive tax rate will likely continue to entice investment.

Corporate tax rates are a critical policy tool globally. In an article titled Corporate Taxes Around the World, 2022 by Cristina Enache of the Tax Foundation, she notes that corporate taxes have been declining. The global GDP weighted average statutory tax rate was 46.52% in 1980 and only 25.43% in 2022. Not surprisingly, the weighted average dropped significantly after 2017 when the TCJA reduced the U.S. federal rate from 35% to 21%. Even after that huge drop, the U.S.'s effective rate is only near the global average and still higher than most of Europe and Asia. The author writes, "Prior to the U.S. tax reform in 2017, the United States was largely responsible for keeping the weighted average rate higher given its relatively high tax rate, as well as its significant contribution to GDP." More striking, had the statutory rate increased above 25% upon expiration of the TCJA, the U.S. tax rate would have been higher than 203 of the 224 countries analyzed for the report.

Despite the temptation to tax large, profitable, and amorphous organizations, we believe lower corporate taxes make for better policy. In a simplistic manner corporations can be seen as "pass-through" vehicles between consumers and corporate stakeholders – employees, shareholders, creditors, suppliers, and tax authorities. The more the government takes, the less that is available for the others. Governments have many sources of revenue, and the contribution of each source varies. In the U.S., personal income taxes constitute the largest source of revenues. It should be intuitive that with high employment and robust wages, the government's take increases. Similarly, incentivizing investment increases employment which boosts consumption and GDP.

Critics argue low corporate taxes are a gift to the rich because they own or manage the companies and pay themselves handsomely. Also, lower taxes boost net income and returns to shareholders, who are often associated with wealthier people. According to the Bureau of Labor Statistics, wages and salaries for private industry workers grew steadily from 2017 through 2024. In addition to the pandemic disruptions, part of that period included a spike in inflation. Nevertheless, workers experienced low levels of unemployment and growth in real wages that helped power consumption and a robust economy over the last few years.

The stock market also benefited from the tax cuts, as would be expected. From the end of 2016 through the end of 2024, the S&P 500 returned an impressive 12.77% per annum. This occurred despite a 34% collapse during

the first month of the pandemic in 2020. Given the stimulus thrust at the economy by both the Federal government and the Fed, it is hard to attribute the performance to tax policy. However, from the end of 2017 through the end of 2019 the stock market rose nearly 10% per annum. Healthy equity and bond markets become a key source of stimulus for the economy by boosting consumer confidence and lowering the cost of capital.

A defining feature of the U.S. economy is the vibrancy of the private sector. History has shown that the most reliable paths to development, growth, and wealth accumulation come from investment, innovation, and entrepreneurship. According to the Census Bureau new business applications surged over the last five years. Again, the pandemic likely influenced behavior, and the rapid evolution of technology likely propelled new business formation. Still, policies that promote private sector growth by containing regulation and limiting taxation should contribute to the economy's dynamism and continued growth.

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