

Timely insights from portfolio managers and industry experts on key financial, economic and political issues.

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Equities

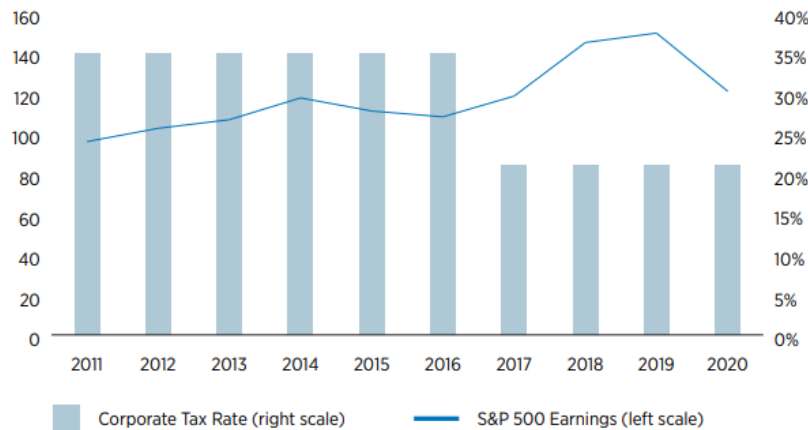
Contending with the possibility of higher corporate and capital gains tax rates

Boston - For all the focus on the reopening of the global economy and the potential for higher inflation, one risk that may not be getting enough attention from investors is higher taxes.

The Tax Cuts and Jobs Act of 2017 reduced the federal effective tax rate on corporate earnings from 35% to 21%, putting the U.S. more in line with other developed countries. S&P 500 earnings jumped 22.5% in 2018, the first year with the lower tax rate.

Falling tax rates have driven earnings growth

Corporate earnings growth versus corporate tax rate



Sources: FactSet for earnings, Trading Economics for corporate tax rate. Data from 2011 to 2020.

As Congress takes up President Biden's tax plan for possible passage later this year, we see the potential for a partial reversal of the cut in the corporate tax rate, with a rate of 28% proposed. In addition to the statutory rate, raising the minimum tax on foreign-sourced earnings from 13% to 21% is also on the table. This would likely have a disproportionate impact on U.S.-domiciled multinationals with high levels of intellectual property — for example, Big Tech and Big Pharma.

Along with a tax hike's hit to corporate earnings, certain shareholders would have to contend with the possibility of higher capital gains tax rates. These tax increases are likely to be focused on higher income earners, whose capital gains rates could rise to 28% or even 40%.

Bottom line: If those tax rate hikes are implemented with an immediate effective date, we think investors could be well served to consider tax planning moves in the first half of 2021.

Picture of

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S&P 500 Index is an unmanaged index of large-cap stocks commonly used as a measure of U.S. stock market performance.

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