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Biden’s Tax Plan Spooks the Markets

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ANALYST INSIGHT

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On April 22, Bloomberg released a report detailing President Joe Biden's forthcoming Capital Gains Tax ('CGT') proposal. The report noted an almost doubling of CGT for wealthy individuals (those earning at least US$ 1 million annually) from 20.0% to 39.6%. Coupled with an existing surtax on investment income, the increase implies that federal tax rates for investors could be as high as 43.4%. The official proposal is expected to be released this week as part of the tax increases needed to fund the President's "American Families Plan". This comes as no surprise within the current political environment as President Biden made his intentions clear during his campaign. Notwithstanding, the speed at which the Biden administration will initiate the proposal and the high rate of the tax caught many market participants off-guard last Thursday. Today, we assess the implications of this tax increase for markets.

Short term market moves

Within minutes of the news, stock indices plunged as investors and traders alike quickly reacted and "sold the news". The reason for the decline is quite simple, a CGT means each time an investor buys/sells financial assets, the government gets a cut. An increase in the CGT therefore increases the government's share of the gains and reduces the investor's portion. Consequently, many investors sold these assets to take some of their profits now, as opposed to later and risk sharing a bigger piece with the government.

Perspective

While the markets reacted suddenly and severely to the news, it's important to note that policy requires negotiations and Biden won't start at a low point – he'll start high so when the negotiations are really underway, he can compromise without "giving up too much". Within that vein, most analysts believe that the democratic "sweet spot" is 30%. Of course, 30% is still well above 20% but similarly, it's significantly lower than 39.6%. Additionally, if we put this into greater perspective, at 30%, it just brings markets back to the pre-2018 tax rate. Once the market digests the potential change, it should occur to investors that the increase isn't unchartered territory.

History

What's also quite important to note is that in matters of this nature, history comes in handy. If we go back to the last major CGT increase in 2013, the way the market handled the impending increase is quite instructive. Specifically, once investors were certain that a CGT was imminent, the S&P 500 fell in late 2012. However, it then rose slightly, closing the year just above where it peaked in April 2012. In 2013, the year of the CGT increase, the S&P 500 boomed; growing by 29.6% and has continued to boom up until the pandemic-induced decline in March 2020. Consistent with this, Goldman Sachs' Chief strategist, in October last year, affirmed the bank's view that any sell-off in equities from a CGT increase would be short-lived and reversed in subsequent quarters, as history has shown.

Options are few

The next major consideration in our view, are options. The simple truth is that the COVID-19 pandemic has shifted the investment landscape in such a way that risky assets have become the bedrock of many portfolios globally. Will this change? The possibility exists but investors are somewhat boxed in. As rates remain anchored to Central Banks' low short-term policy rates, the fixed income market, which had typically been the other side of the coin as it relates to portfolio weightings, has become less attractive from a relative return perspective. Additionally, cash has become increasingly worthless in a portfolio, particularly in the short term where we see inflation expectations rising. With that said, how does an intelligent investor sell equities to avoid a CGT increase without consideration for the opportunity cost of no longer being invested? We believe the short answer is that they do not. The major nuance here, however, is stretched valuations, particularly among tech companies. Essentially, while history has pointed to a quick rebound and options are few, elevated valuations in some sectors may cause some additional volatility as we draw closer to an actual tax increase.

Concluding Thoughts

In closing, we note that while the S&P 500 displayed increased intraday volatility on April 22 and declined by just under 1% at the end of the day, the Index recovered the losses by April 23. With that said, we believe the historical precedence combined with the limited options should buttress markets. Notwithstanding, some sectors could witness some pullback as imminent taxation weighs on already stretched valuations. Finally, regardless of the near to medium-term market moves, Barita continues to assess the global markets and express our thesis on global equities through the FX Growth Fund which our clients can benefit from directly.

LOCAL EQUITIES MARKET

For the week ended Friday, our local stock market increased week-over-week. The JSE Combined Index increased by 1.44%, the Main Market Index improved by 1.28%, the JSE All Jamaican Composite Index grew by 1.30%, the JSE Junior Market Index improved by 3.12%, and the JSE USD Equities Index improved by 1.12%.

During the week, Knutsford Express Services Limited was the largest gainer, rising by 40.47% to close at J$8.92. The biggest loser was Consolidated Bakeries (Jamaica) Limited which fell by 13.71% to close at J$1.51

During the Month of April, we continue to see Junior Market Equities (+5.6% Month to date) outpacing their Main Market counterparts (+2.1% Month to date.)

As of Friday April 23rd, the Overall Market activity resulted from trading in 109 stocks of which 52 advanced, 36 declined and 21 traded firm. Market volume amounted to 102,354,381 units valued at over $517,281,453.49. Wigton Windfarm Limited Ordinary Shares was the volume leader with 13,600,119 units (13.29%) followed by Transjamaican Highway Limited with 12,880,729 units (12.58%) and Sagicor Select Funds Limited - Financial with 7,430,676 units (7.26%) .

Revisiting relevant news during the week:

Even against the backdrop of COVID-19 and the entry of Izizzi and Luck Play to the gaming market during its first quarter ending March 31, 2021, Supreme Ventures Limited (SVL) saw a 33 per cent increase of gross ticket sales to $23.8 billion in its 20th anniversary year. This while managing to achieve a record total gaming income of $10.7 billion which was six per cent higher than the prior quarter.
https://www.jamaicaobserver.com/business-report/supreme-ventures-achieves-highest-revenue-on-20th-anniversary_219884?profile=1056

With the publication of its abridged statement on the Jamaica Stock Exchange's (JSE) website on Tuesday last and subsequent publication in the Business Observer, Guardian Holding Limited (GHL) will list by introduction by May 5 after a seven-year hiatus from the JSE.

https://www.jamaicaobserver.com/business-report/guardian-holdings-to-list-on-jamaica-stock-market-through-introduction_219844?profile=1056

Local cigarette distributor Carreras Limited said that while it will continue to actively pursue expansions within its core tobacco business, the company is not opposed to tapping into new opportunities in the cannabis dispensary market, preferably those medically related.
https://www.jamaicaobserver.com/business-report/carreras-not-opposed-to-exploring-opportunities-in-cannabis-market_219805?profile=1056

As the country seeks to recover from the fallout caused by the novel coronavirus pandemic, Finance Minister Dr Nigel Clarke has reiterated the need for the Government to prudently conduct its economic affairs and manage debt if it is to successfully navigate the crisis.
https://www.jamaicaobserver.com/business-report/we-need-to-steer-clear-of-debt-finance-minister-says-jamaica-cannot-afford-a-third-debt-restructuring_219835?profile=1056

Index	23/04/2021	16/04/2021	31/12/2020	Week/Week	Year-to-Date
JSE Main Market	402,842.60	397,747.50	395,614.93	1.28%	1.83%
JSE Junior Market	3,150.55	3,055.12	2,643.38	-0.10%	19.19%
JSE Combined Market	404,542.48	398,815.66	392,435.92	3.12%	3.08%
JSE USD Equities Market	211.60	209.26	186.3	1.12%	13.58%

INTERNATIONAL DEVELOPMENTS

Weekly unemployment claims fell to a new pandemic-era low for a second week, suggesting the labor market's recovery is picking up steam and that the April employment report could be strong.

First-time claims totaled 547,000 for the week ending April 17, about 50,000 lower than forecast. The week is also the same one in which the government collects data for the April employment report.
https://www.cnbc.com/2021/04/22/the-labor-market-is-starting-to-rip-as-fewer-seek-unemployment-benefits.html

Federal Reserve officials next week are likely to paint a robust picture on the economy while simultaneously not even hinting at policy changes ahead.

Investors increasingly have come to trust central bankers when they say that even with the economy running at its hottest pace in nearly 40 years, they won't start taking away policy accommodation until it's clear the recovery is on solid ground.
https://www.cnbc.com/2021/04/23/the-fed-is-unlikely-to-hint-at-policy-change-despite-stronger-economy.html

Stocks took a decided turn lower in trading on Thursday on news headlines that President Joe Biden plans to propose nearly doubling the long-term capital gains tax rate for taxpayers who earn more than USD 1 million a year. The tax hike would be used to fund some of the measures in Biden's American Families Plan, which could be formally proposed next week and may involve free community college tuition, child-care subsidies,
https://www.troweprice.com/personal-investing/resources/insights/global-markets-weekly-update.html

Top Things to Watch This Week:

1. **Earnings Season Continues**

2. **U.S. Conference Board Consumer Confidence Index (April)**

3. **FOMC Meeting:** The Federal Open Market Committee (FOMC) of the Federal Reserve meets next Tuesday and Wednesday on interest rates and monetary policy. We should not expect the Fed to make any changes to the federal funds rate because it keeps telling us that will happen in 2023. Still, more FOMC members have tightened their timelines about when that should happen, given the strength of the economic recovery. Inflation is still lower than where the Fed would like it, even though almost everything we buy is more expensive today than it was six months ago. Investors will want to hear that the Fed will keep up its $120 billion of government bond purchases every month, which has laid a nice safety net under capital markets.

4. **Personal Income and Spending:** On Friday, we'll get reports on U.S. personal income and spending. Retail sales spiked last month as the first round of stimulus checks hit bank accounts. Another wave went out in the past two weeks. Are consumers putting that back into the economy, or are we still not ready to spend again like its 2019? We'll find out.

Index	23/04/2021	16/04/2021	31/12/2020	Week/Week	Year-to-Date
Dow Jones	34,043.49	34,200.67	30,606.48	-0.46%	11.23%
S&P 500	4,180.17	4,185.47	3,756.07	-0.13%	11.29%
NASDAQ 100	13,941.44	14,041.91	12,888.28	-0.72%	8.17%
FTSE 100	6,938.56	7,019.53	6,460.52	-1.15%	7.40%
Euro Stoxx 50	4,013.34	4,032.99	3,552.64	-0.49%	12.97%

Local Economic Conditions

Local Foreign Exchange Market

- Our local currency depreciated by 2.06% against the U.S. Dollar week on week to settle at $154.74 as at close of trade Friday, relative to $151.62 per US$1.00 at the end of the prior week. Year to date, the Jamaican dollar has depreciated by approximately -8.48%.

Interest Rates and Inflation

- Since the onset of the pandemic in March 2020, market volatility has declined significantly. Notwithstanding, the BOJ maintains its position; supportive of the wider economy and continues to hold the policy rate at 0.50%.

- At this rate, based on its assessment, the BOJ notes that inflation will generally continue to remain within the target of 4.0% to 6.0% over the next two years.

- As at March 2021, point-to-point was recorded at 5.2%.

- Barita's Collective Investment Schemes ("CIS") offer the opportunity for investors to remain invested in the market at this delicate stage of the market cycle; moreover, there is a diversification benefit and opportunity to have a professional portfolio manager make the best-in-class professional judgements on your behalf.

- The F.X. Growth Fund, which is benchmarked against the S&P 500, has increased by 2.25% year to date.

- As at April 21st, 2021, the Capital Growth Fund has delivered a YTD return of 5.63% relative to the JSE Combined and Main Market Indices which posted a returns of 3.08% and 1.83%, respectively.

- The FX Bond Portfolio remains an attractive fixed-income portfolio, particularly when viewed within the context of global interest rates which have declined significantly as central banks maintain low policy rates to drive the economic recovery.

Currency Pair	23/04/2021	16/04/2021	31/12/2020	Week/Week	Year-to-Date
JMD: USD	154.7432	151.6201	142.6493	-2.06%	-8.48%
JMD:CAD	124.2084	121.5685	111.4117	-2.17%	-11.47%
JMD:GBP	212.5374	211.7740	193.6657	-0.36%	-9.74%

Unit Trust Performance

- Year to Date, The Money Market Fund has increased by 1.40%, the FX Bond Portfolio has decreased by -0.13%, the F.X. Growth Portfolio increased by 2.25%, the Real Estate Portfolio has increased by 2.22% and the Capital Growth Fund has grown by 5.63%.

> "The individual investor should act consistently as an investor and not as a speculator."
>
> — Ben Graham

Unit Trust

Unit Trust Fund	21/04/2021	14/04/2021	Week/Week Return	Year-to-Date Return	1 Year Return	Yield
Capital Growth	89.6498	88.0280	1.84%	5.63%	15.44%	-
Money Market	14.9829	14.9421	0.27%	1.40%	2.92%	1.54%
Income Portfolio	100.0000	100.0000	0.00%	-	-	2.32%
FX Bond Portfolio (US$)	1.3544	1.3496	0.36%	-0.13%	7.10%	2.22%
Real Estate Portfolio	5,964.6917	6,010.9752	-0.77%	2.22%	-6.66%	-
FX Growth Portfolio	1.0211	1.0201	0.09%	2.25%	22.20%	-

"There are at least three significant reasons we resist contemplating our personal financial goals: it can be stress-inducing, we dislike numbers, it is socially taboo, and we are slaves to "right now."

– Daniel Crosby, Personal Benchmark: Integrating Behavioral Finance and Investment Management

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Investment Playbook

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Equities

Stock Ticket	Stock Information (As at April 23, 2021)	Analyst Outlook
WISYNCO Wisynco Group Ltd	P/E: 22.37x P/B: 4.08x Price: J$15.88 Div Yield: 1.13%	**OVERWEIGHT** The local fiscal support to both households and businesses was instrumental in maintaining individuals' consumption capacity, particularly those furloughed and made redundant, which supported the demand for consumer staples distributed by manufacturers and distributors Wisynco. We expect that with continued fiscal support through either direct household support or government spend on projects to stimulate employment, Wisynco's business will thrive in this environment.
LASM Lasco Manufacturing	P/E: 16.92x P/B: 2.77x Price: J$5.02 Div Yield: 1.21%	**OVERWEIGHT** The local fiscal support to both households and businesses was instrumental in maintaining individuals' consumption capacity, particularly those furloughed and made redundant, which supported the demand for consumer staples distributed by manufacturers and distributors LASM. We expect that with continued fiscal support through either direct household support or government spend on projects to stimulate employment, LASM's business will thrive in this environment. Given that more restrictive curtailment measures do not seem likely, LASM is likely to perform better than in the April - June quarter. The national curfew measures were particularly restrictive and, therefore, negatively impacted LASM's revenue growth.
LASD Lasco Distributors	P/E: 15.23x P/B: 2.16x Price: J$4.00 Div Yield: 1.28%	**OVERWEIGHT** The local fiscal support to both households and businesses was instrumental in maintaining individuals' consumption capacity, particularly those who were furloughed and made redundant, which supported the demand for consumer staples distributed by manufacturers and distributors as LASD. We expect that with continued fiscal support through either direct household support or government spend on projects to stimulate employment, LASD's business will thrive in this environment.

Ratings Definitions

OVERWEIGHT/BUY
Exposure to this asset should be between 5% and 10% of your total portfolio

UNDERWEIGHT
Reduce exposure in your portfolio to less than 5% for this particular asset

MARKETWEIGHT/HOLD
Exposure to the asset should be equal to 5% of your total portfolio

SELL
Reduce exposure in your portfolio to zero

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Equities

Stock Ticker	Stock Information (As at April 23, 2021)	Analyst Outlook
SEP Seprod Limited	P/E: 20.99x P/B: 3.57x Price: J$82.30 Div Yield: 0.36%	**OVERWEIGHT** Seprod has undergone significant structural changes within the last 5-years aimed at improving the underlying performance of the company. Within this period, particular emphasis has been placed on optimizing the distribution, warehousing and logistics capabilities of the company. This gradual, multi-year, improvement was accomplished through reinvestment within the organization coupled with strategic acquisitions aimed at increasing the distribution reach and quality of the company. Another major change was the closure of the Group's loss-making sugar division; a move that enhanced shareholder value. These changes have positioned Seprod to deliver robust growth through an expansive product mix and access to consumer markets both locally and regionally.
PROVENJMD Proven Investments Limited	P/E: 18.84x P/B: 1.20x Price: $37.71 Div Yield: 3.28%	**OVERWEIGHT** Given the current economic environment, characterized by low interest rates and increased uncertainty, PIL has shifted from the carry trade business to more private equity and real estate ventures, thereby allowing for diversification benefits to be realized - particularly as it relates to the "spreading" of risk. Given the business model of PIL wherein capital is used to acquire strategic assets, this APO is expected and should make the stock accessible to a wider pool of investors. At present, only a small subset of listed companies pursue private equity investments which makes PIL an attractive security for investors who want the liquidity the stock market provides as well as exposure to non-listed companies that can provide value.

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Stock Ticker	Stock Information (As at April 23, 2021)	Analyst Outlook
PROVENUS Proven Investments Limited	P/E: 18.53x P/B: 1.18x Price: US$0.26 Div Yield: 3.03%	**OVERWEIGHT** Given the current economic environment, characterized by low interest rates and increased uncertainty, PIL has shifted from the carry trade business to more private equity and real estate ventures, thereby allowing for diversification benefits to be realized - particularly as it relates to the "spreading" of risk. Given the business model of PIL wherein capital is used to acquire strategic assets, this APO is expected and should make the stock accessible to a wider pool of investors. At present, only a small subset of listed companies pursue private equity investments which makes PIL an attractive security for investors who want the liquidity the stock market provides as well as exposure to non-listed companies that can provide value.
SCIJMD Sygnus Credit Investments	P/E: 23.06x P/B: 0.50x Price: J$14.94 Div Yield: 2.40%	**OVERWEIGHT** Sygnus provides funding to Mid-Size firms within the lending market, which is considered to have a higher risk and generally overlooked by providers of traditional financing forms. This provides a largely untapped/under-tapped niche market within the Caribbean lending space for Sygnus, a few direct competitors. The flexibility in the financing terms offered by the Company is a clear advantage to borrowers, and it allows SCI to manage its credit risk to generate double-digit risk-adjusted returns on investments, which, consequently, bolsters shareholder value.
SCIUSD Sygnus Credit Investments	P/E: 26.67x P/B: 0.52x Price: US$0.12 Div Yield: 2.08%	**OVERWEIGHT** Sygnus provides funding to Mid-Size firms within the lending market, which is considered to have a higher risk and generally overlooked by providers of traditional financing forms. This provides a largely untapped/under-tapped niche market within the Caribbean lending space for Sygnus, a few direct competitors. The flexibility in the financing terms offered by the Company is a clear advantage to borrowers, and it allows SCI to manage its credit risk to generate double-digit risk-adjusted returns on investments, which, consequently, bolsters shareholder value.

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CCC Caribbean Cement Company	P/E: 19.72x P/B: 5.47x Price: J$74.14 Div Yield: 0.00%	**Overweight** Throughout the COVID-19 pandemic, all industries have been affected by what has been a significant downturn in aggregate demand as the pandemic has created a need for persons to reduce travelling and physical interaction. Despite this setback which predominantly materialized in Q2 of 2020, the construction industry has rebounded significantly (7.0% in Q3 2020 and 6.2% in Q4 2020), ahead of many other industries and well ahead of the overall economy. This strong growth over the last two reported quarters has been a significant tailwind for Caribbean Cement and the company has consequently seen a significant increase in the demand for its product, well in excess of previous years. On the heels of what has been a great year for the company, management expects demand to increase further, fuelled by upcoming government projects that will require substantial cement deposits. The recent government budget lends to this expectation as one of the main components of the government's SERVE Programme is infrastructure development. With that said, the company is positioning itself to meet this demand while maintaining its more efficient cost structure which was displayed in 2020, chief among these was the reduction of debt, which in turn reduced the company's cost of debt.

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