PRIVATE ASSET MANAGEMENT, INC.
WEALTH STRATEGY ADVISORS

PARADIGM

November 2018

This is the third part of our four-part series. This month, we will quickly review the first two trends, plus we will look at the long-term trend of rising taxes. Next month, we will conclude by reviewing key concepts that investors can use to navigate long-term trends and maximize their long-term financial success.

Part one dealt with rising interest rates. This has been occurring for most of the past five years. The effect on bond fund returns, loan rates, and asset values has been felt, but most investors navigated these effects well.

Part two dealt with stock returns, both past and future. Hopefully, you gained an appreciation of the economic engine that propels earnings growth and stock prices over long periods of time.

These first two trends have evolved roughly along the lines that we thought they would.

Congressional Budget Office forecast

Forecast from Congressional Budget Office - in Billion $$

Budget Total	Actual 2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2018
Revenues	3,316	3,338	3,490	3,678	3,827	4,012	4,228	4,444	4,663	5,002	5,299	5,520
Outlays	3,982	4,142	4,470	4,685	4,949	5,288	5,500	5,688	6,015	6,322	6,615	7,046
Deficit	-666	-804	-980	-1,007	-1,122	-1,276	-1,272	-1,244	-1,352	-1,320	-1,316	-1,526
Nominal GDP	19,391	20,377	21,383	22,270	23,110	23,977	24,896	25,869	26,882	27,898	28,989	30,121
Deficit: % of GDP	3.4%	3.9%	4.6%	4.5%	4.9%	5.3%	5.1%	4.8%	5.0%	4.7%	4.5%	5.1%

This month, part three focuses on rising taxes. This trend is occurring, but not quite in the fashion that we initially thought. We will review past thoughts, why we think increasing taxes is still a material trend, and highlight that higher taxes are already occurring.

As the U.S. started digging out from the 2008-2009 Great Recession, reducing future deficits appeared to require both spending cuts and tax increases. The so-called “Grand Bargain” (spending cuts combined with increased taxes) never occurred, but these ideas made sense to us. Hence our thought several years ago for rising taxes.

In 2017, we saw tax changes that reduced corporate and personal taxes, although the latter had sunset provisions, which means that some personal tax cuts will end in 2025.

Some combination of spending cuts and tax increases still seems inevitable to us. The budget forecast reproduced here supports that thought. Deficits in 2017 and 2018 as a percentage of GDP are below 4%, not much above the long-term average. However, with no change in policy, deficits rise through 2025 ending up at 5% of GDP, a level most believe has negative long-term effects. As current provisions sunset, deficits as a percentage of GDP stabilize and decline slightly.

Remember, these projections assume current law, which is not likely to be actual law come 2025. Regardless, the idea of a need for increased taxes (income, gasoline) still appears to be a valid assumption for investors to plan for.

One area that highlights the fact that taxes are already heading higher is property taxes. Data from the Washington (State) Policy Center and a look at county records shows that property taxes for those of us that live in and around Seattle have increased at 8% per year over the past 10 years. We thought tax increases would occur at the Federal level. Turns out, tax increases have been more local.

Increased taxes are a long-term trend you will need to navigate, along with rising interest rates and return expectations. The final part of this series will review key concepts to help you navigate these trends.

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