Goldman Sachs Asset Management

US Political Perspectives

April 2021

Executive Summary

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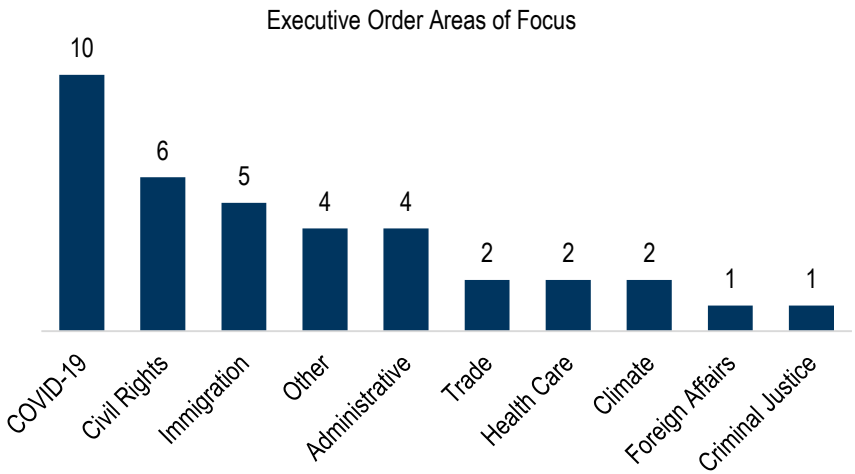
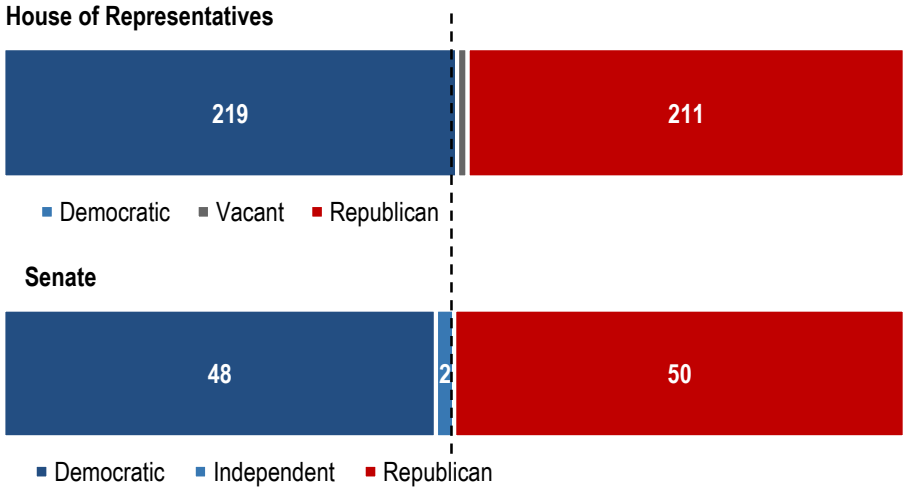
- **100mn doses in 100 days:** Vaccine rollout has accelerated and the country is on track to have 50% of the population inoculated by May.
- **Prioritizing Plans:** The $1.9 trillion American Rescue Plan was the first legislative priority for the new administration. As negotiations for more initiatives go on, we expect policy to continue to come via executive order – Biden's 37 EOs outpace 21st century Presidents' average of 20 in the first 100 days.
- **Fiscal Impulse:** The next $2-4 trillion in spending that the Biden Administration has proposed in the form of infrastructure, climate transition, and healthcare will likely take longer to work through Congress and be spent over the next 10 years.
- **Talking Taxes:** At multi-decade lows, tax rates are likely to move higher, although moderately so. We expect any additional revenues to be spent on fiscal programs.
- **China Challenge:** Broad public support for a "tough on China" stance likely means policies towards China won't change, though they may become more multilateral.
- **Polar Opposites:** Ideological polarization between parties in Congress is as wide as it has been in decades, potentially limiting or moderating legislative outcomes.
- **What Comes Next:** Historically midterm elections have proven challenging for the party in power, with potential Republican gains in the House and Senate posing a counterbalance for the second half of President Biden's term.

Executive Orders by President Biden



Narrow Congressional Composition



Source: Goldman Sachs Global Investment Research, Federal Register, and GSAM. As of March 28, 2021.

COVID-19 Containment

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Controlling COVID-19 will be critical to getting to recovery stages

The US is racing vaccinations against variants

Cases

>30mm

Total confirmed cases in the US

Virus

~20%

Known US COVID-19 cases caused by UK, SA, or Brazilian variant

Herd Immunity

60-70%

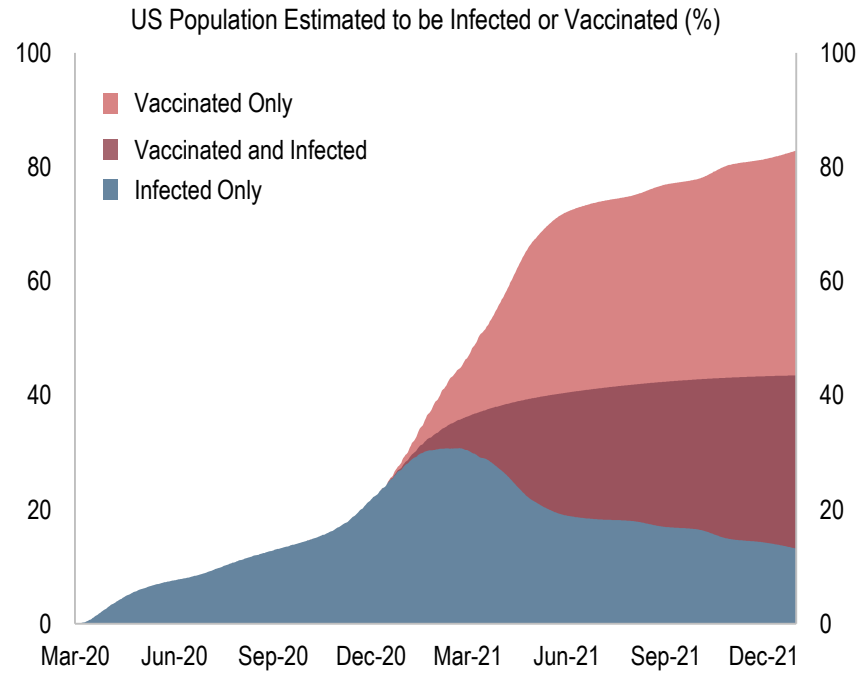
Of population with antibodies needed to reach herd immunity

Vaccine

98%

Probability 200 million people vaccinated in US by 2H 2021

But the country is on track for herd immunity by summer



Source: Bloomberg, Goldman Sachs Global Investment Research, Good Judgement Project, World Health Organization, and GSAM. As of March 28, 2021. For illustrative purposes only. The economic and market forecasts presented herein are for informational purposes as of the date of this presentation. There can be no assurance that the forecasts will be achieved.

COVID-19 Relief

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The first major legislative package was the $1.9 trillion American Rescue Plan

State fiscal aid	$350 billion
Education grants	170
Public health	125
Stimulus payments & child tax credit	520
Unemployment insurance	246
Rental/ homeowner assistance	42
Child care	48
Safety net programs	53
Health insurance	103
Business assistance	72
Pension relief	51
Transportation	57
Broadband	7
Farm subsidies	9
Business tax provisions	-70
Federal emergency management fund	50
Other	12
Total cost	**$1,844 billion = 8.4% of GDP**

Source: Goldman Sachs Global Investment Research and GSAM. As of March 28, 2021.

2020 Policy Support

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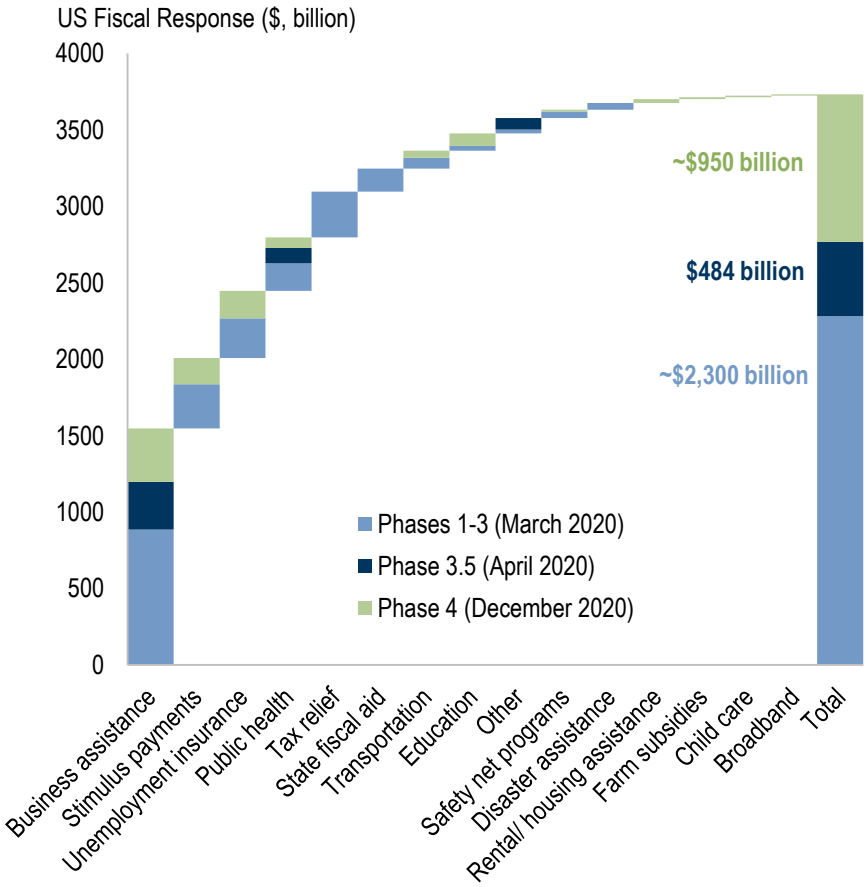
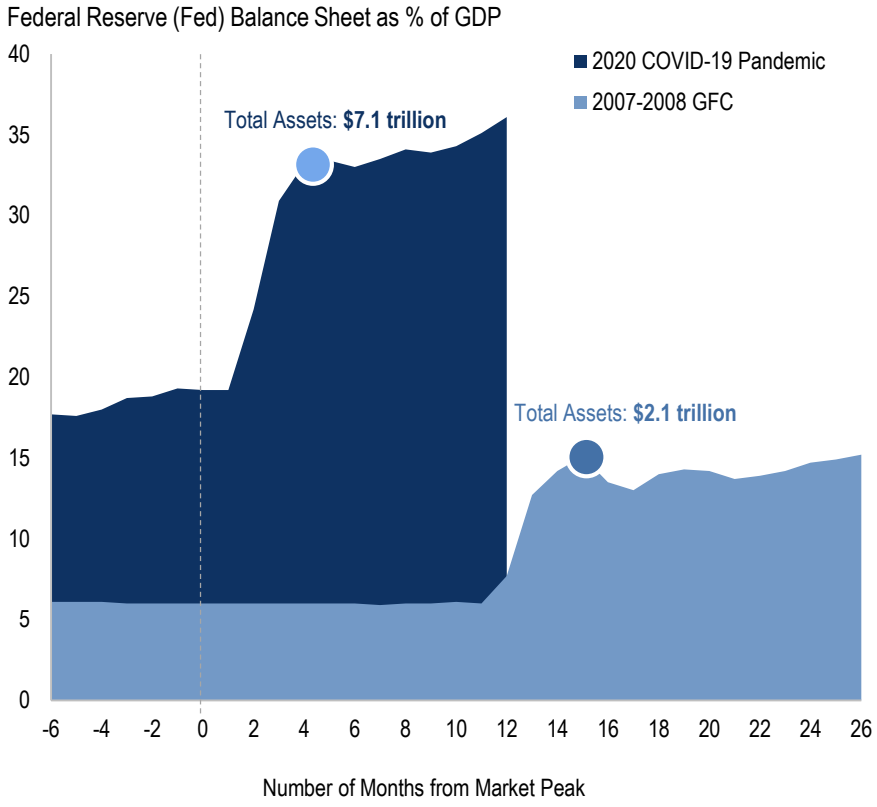
The American Rescue Plan followed on 2020 policy responses that were swift and sizable

Fiscal policy helped provide a bridge to recovery



Monetary policy provided liquidity



Source: Bloomberg, International Monetary Fund, and GSAM. As of March 28, 2021.

Policy Proposals

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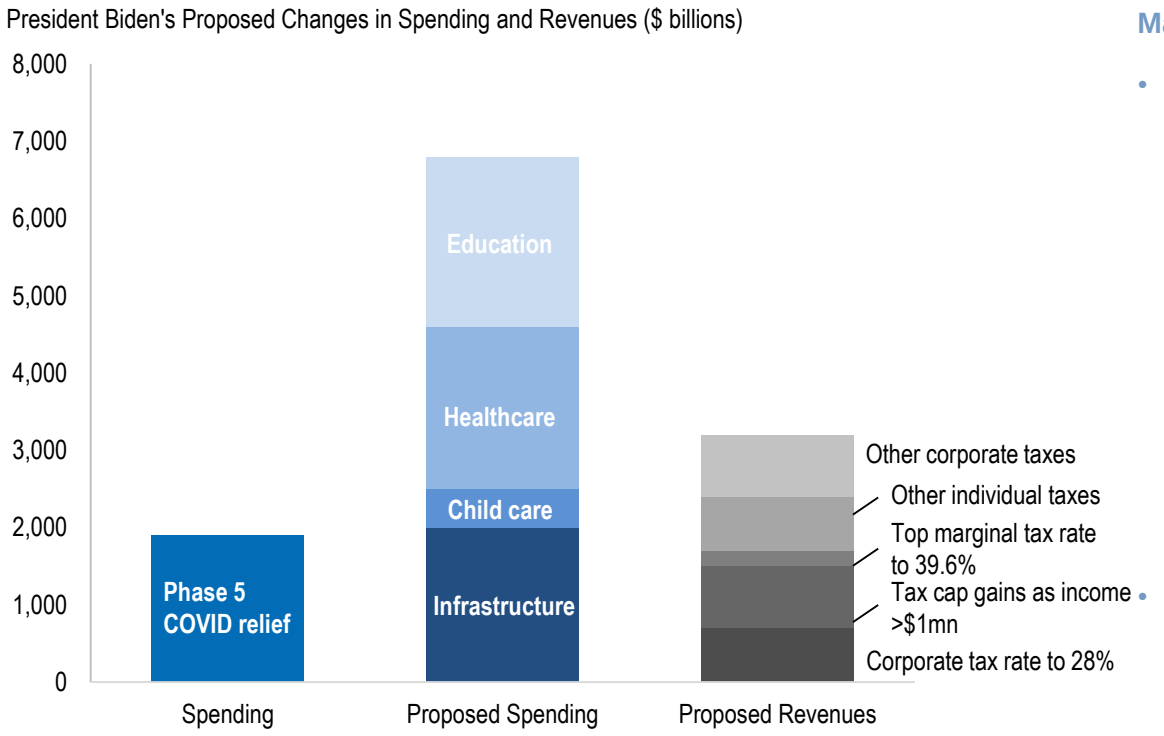
The Biden Administration has proposed several trillion dollars of new spending partially offset with tax increases



Macro and Market Implications

- Current impulse will likely accelerate near-term growth and inflation, while raising interest rates and lowering unemployment
  - 2021 & 2022 GDP growth forecast: 7.1% & 5.0%
  - 2021 & 2022 US 10-Year forecast: 1.9% & 2.1%
  - Core PCE to reach 1.9% / 1.9% / 2.1% / 2.2% at the end of 2021-2024
  - U3 unemployment rate to decline to 4.1% / 3.5% / 3.3% / 3.1% at the end of 2021-2024
  - Expect first Fed funds rate increase in 1H 2024
- Additional spending would likely be phased in over time, with more modest impact to annual forecasts

Source: Goldman Sachs Global Investment Research and GSAM. As of March 28, 2021.

Policy Proposals: Infrastructure

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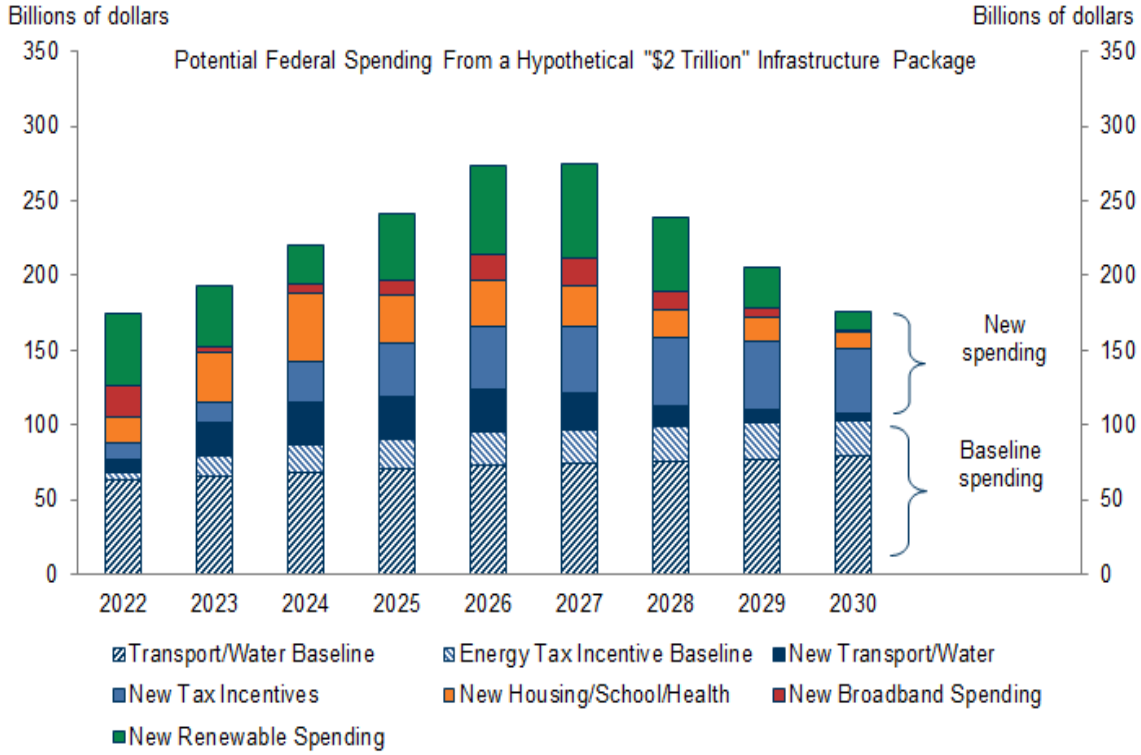
Infrastructure is a generally bipartisan topic, with current proposals for $1.5 – $2 trillion in spending over the next 10 years



Proposals & Perspective

- Congress is likely to take up infrastructure as the existing five-year plan expires this summer and current spending likely undershoots need
- Although "infrastructure" has bipartisan support, the usual disagreements over where to invest and how to pay for it persist

Macro & Market Implications

- A large infrastructure program would likely benefit commodity prices and sector-specific equities such as industrials and materials
- Expect additional focus on green infrastructure, including investments and tax incentives

Source: Goldman Sachs Global Investment Research and GSAM. As of March 28, 2021.

Policy Proposals: Renewables

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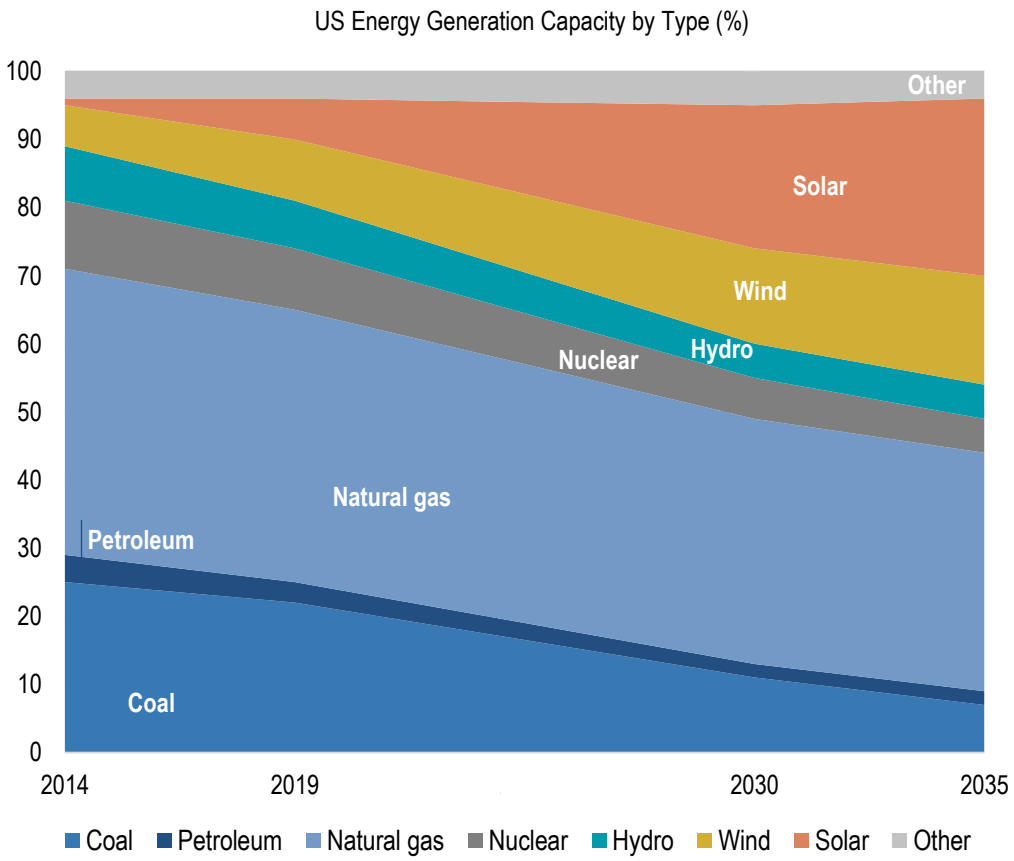
Infrastructure proposals may prioritize the climate transition

Proposals & Perspective

- **Clean energy:** Proposed an unspecified amount of tax incentives and financing mechanisms to invest in clean energy, with a goal of carbon-free electricity generation by 2035
- **Electric vehicles:** Proposed investment in 500,000 vehicle charging stations and the conversion of school buses to zero emissions, as well as an unspecified increase in fuel economy standards
- **Environmental remediation:** Proposed investment to clean up oil, gas, and coal extraction sites

Macro & Market Implication

- Incentives will likely support the renewable theme, but the capital-intensive transition may also benefit commodities in the near-term



Source: Goldman Sachs Global Investment Research and GSAM. As of March 28, 2021.

Policy Proposals: Healthcare

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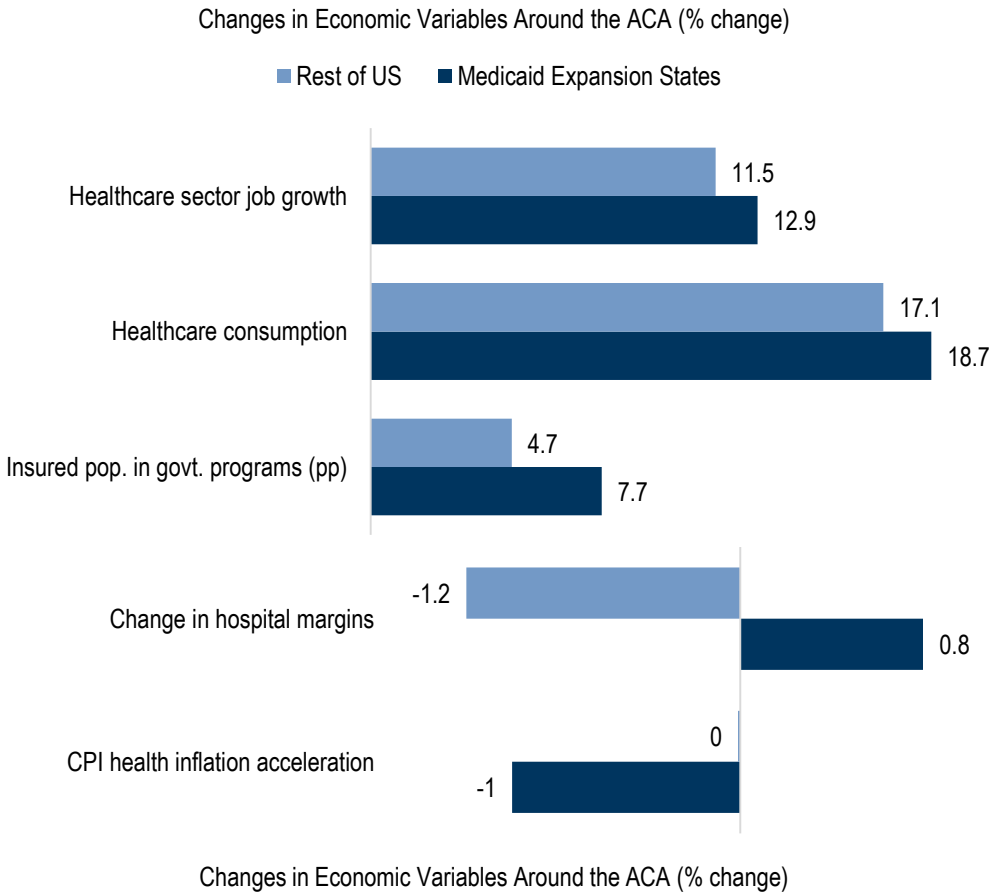
The Biden Administration has proposed to expand on the Affordable Care Act

Proposals & Perspective

- **Insurance:** Propose broadened eligibility for health insurance premium subsidies under the Affordable Care Act and make them more generous; lower Medicare eligibility to 60 and open to a public option
- **Drug Pricing:** Direct Medicare negotiation of drug prices, setting Medicare payment for new drugs without competition using international pricing and an independent board
- Could be enacted via reconciliation

Macro & Market Implications

- States that took up the 2014 ACA Medicaid expansion saw faster growth in healthcare consumption and employment, and lower prices
- Expansion of healthcare coverage and usage likely benefits healthcare equipment, suppliers, distributors, services, facilities, and technology
- Biotech and pharmaceuticals may face headwinds in price pressures or regulatory scrutiny



Source: Goldman Sachs Global Investment Research and GSAM. As of March 28, 2021.

Policy Proposals: Taxes

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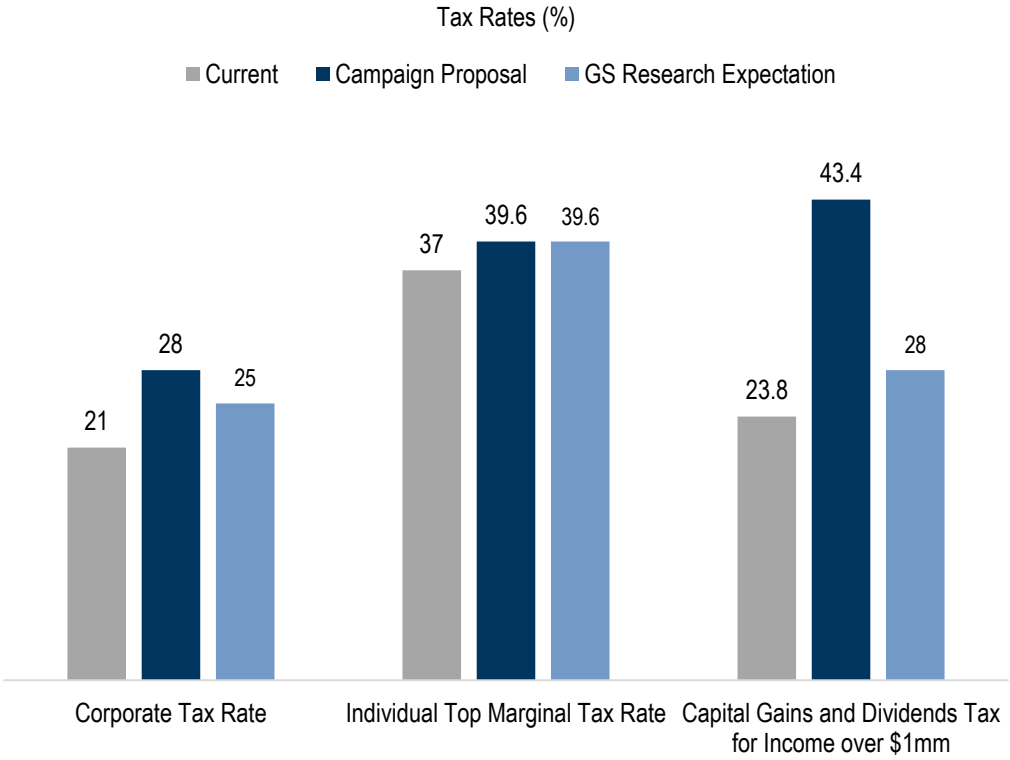
Tax rates are likely to move higher, but narrow Congressional margins will likely moderate increases

Proposals & Perspective

- **Corporate taxes:** Biden has proposed a 28% rate, while GIR expects an increase to ~25% and for an incremental increase in taxation of international corporate income earned by US-based companies
- **Individual taxes:** GIR expects the administration to revert the top marginal tax rate to pre-TCJA levels, raise the top capital gains rate, and potentially increase estate taxes on assets over $1 million
- Could be done via reconciliation, but expect all to take effect in 2022 at the earliest

Macro & Market Implications

- Growth impact depends on what, if anything, an increase in tax rates is used to finance
- Corporate tax rate increase to 25% would represent a 3% reduction in 2022 S&P 500 EPS, with higher impact on multinational companies
- Capital gains tax changes may create more focus on asset allocation and tax loss harvesting
- Shifts in individual tax policy may impact supply/ demand dynamics in the municipal bond market



Source: Goldman Sachs Global Investment Research (GIR) and GSAM. As of March 28, 2021. 'TCJA' refers to the 2017 Tax Cuts and Jobs Act. 'EPS' refers to earnings per share.

Policy Proposals: China

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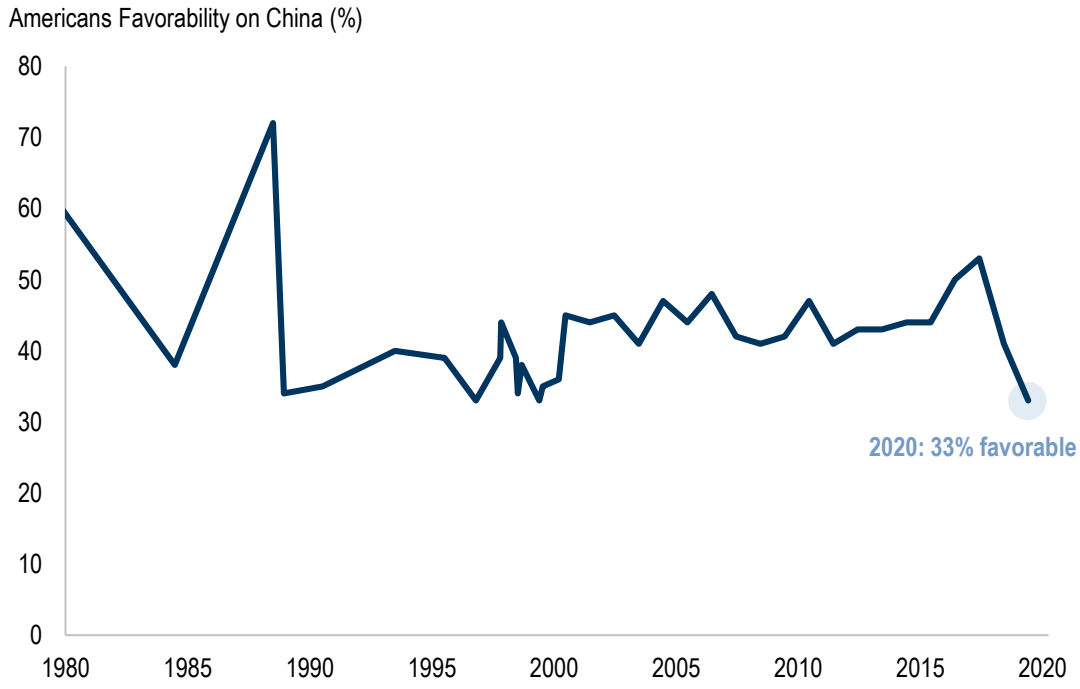
Broad support for "tough on China" policy, though the Biden Administration may adopt a more multilateral approach

Proposals & Perspective

- There is broad support for the US to take tougher stands on Beijing's behavior, particularly with respect to trade practices and human rights concerns
- **Legislation:** Senate may propose a bipartisan "China package" that would aim to shore up US supply chains, expand American production of semiconductors, create 5G networks nationwide, and pour billions into R&D investments
- **Tariffs:** Expect to stay in place

Macro & Market Implications

- Competition that turns into conflict remains a risk, particularly for emerging market equities and the Chinese renminbi, but if markets perceive that negative surprises have been removed there may be more room for EM to rally
- China-exposed companies may see domestic and international regulatory headwinds



Source: Gallup, Goldman Sachs Global Investment Research, and GSAM. As of March 28, 2021. 'R&D' refers to research and development.

Legislative Logistics

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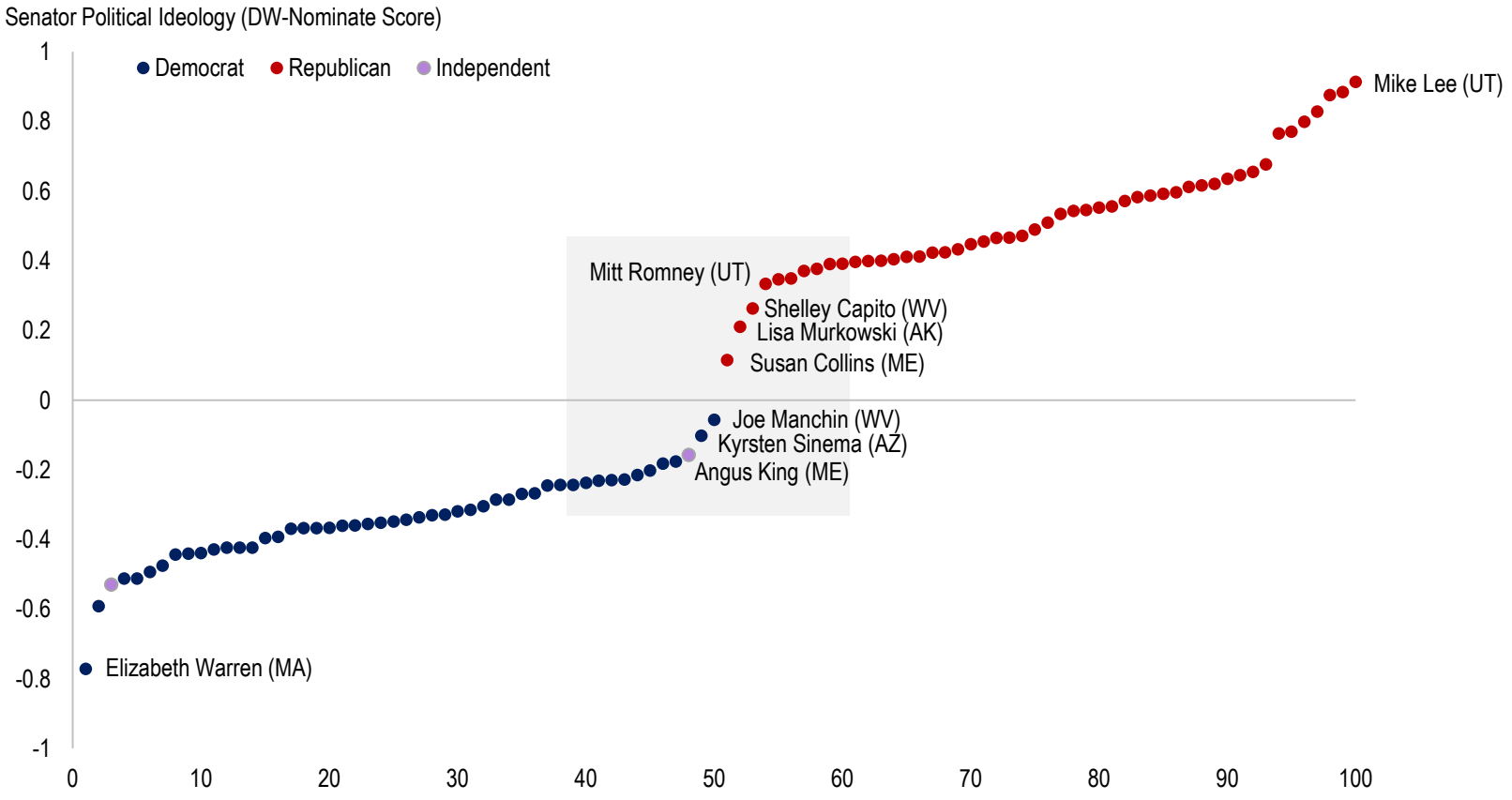
The legislative agenda will likely be moderated by narrow Congressional margins



Source: VoteView and GSAM. As of March 28, 2021. Chart shows the ideology of members of the 2020-2022 Senate based on their voting history.

Legislative Logistics

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Progressive policy implementation may be limited to reconciliation and executive orders

Legislation

- **Healthcare:** Universal coverage
- **Environment:** Green New Deal, ban all fracking
- **Education:** Free public college
- **Corporates:** Antitrust reform
- **Infrastructure:** Direct spending on heavy infrastructure
- **Statehood**

60 votes – Major policy changes highly unlikely

Reconciliation

- **Healthcare:** Public option, insurance subsidies
- **Environment:** Tax incentives
- **Education:** Student loan forgiveness
- **Infrastructure:** Tax incentives
- **Tax proposals:** Personal, corporate, and capital gains rates

51 votes – Fiscal policy changes likely moderated

Executive Order

- **Healthcare:** Reverse Affordable Care Act deregulation, drug pricing, decriminalize marijuana
- **Environment:** Ban fracking on federal land, stricter regulations and standards
- **Education:** Regulate for-profit higher ed institutions
- **Corporates:** Limit stock buybacks, stricter merger approval
- **Finance:** Regulate banking activities
- **Trade policy:** Trade deals, tariffs, investigations
- **Immigration**

0 votes – Proposals possible through executive order

Source: Strategas and GSAM. As of March 28, 2021. Votes refer to the number of Senate votes necessary to pass policy. For illustrative purposes only.

Debt Risk

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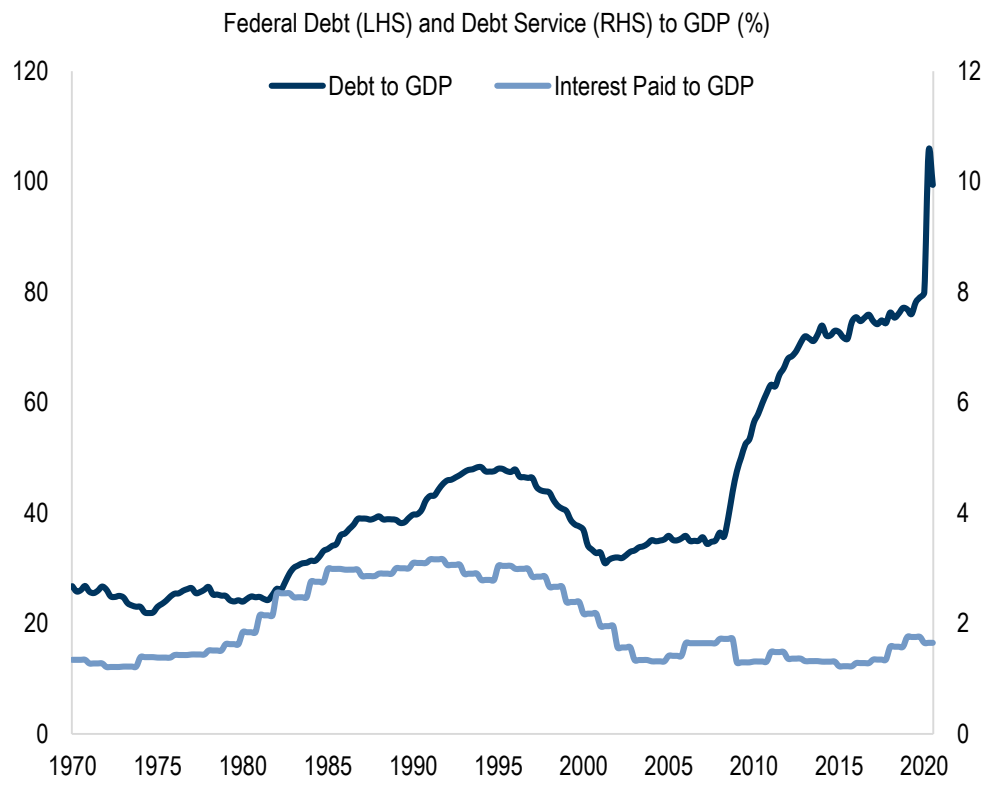
Rising deficits and debt levels may weigh on longer-term growth prospects, though in the near-term low interest rates may make it manageable

- **Debt ceiling:** The two-year suspension of the debt limit expires July 31. Once reinstated, Congress will have several weeks to raise it or, more likely, suspend again.
- **Stock versus flow:** Debt-to-GDP can misalign stock and flow analysis, potentially overstating financial risk. Dividing a stock (US debt) by flow (economic output of a single period) ignores the future value of the output. Measuring the cost of servicing the debt (nominal interest expense) as a share of GDP produces a different picture.
- **How low can it go:** While the level of debt is historically high, interest rates are historically low, which implies roughly average interest expense as a share of GDP.
- **Up, up, and not away:** Interest rates are currently low in part because the bond market judges that they will be low on average in the long run. The increase in interest rates we forecast would raise debt servicing costs over the next decade, but would still leave them within a normal historical range, assuming the deficit stabilizes.
- **Key risks:** One, slowing the rise in debt servicing costs will likely require changes to entitlement spending, which under current law is projected to grow indefinitely as a share of GDP. Two, the long-run neutral rate is uncertain, and a high debt-to-GDP ratio would amplify the fiscal cost of any surprise increase in interest rates.



Source: Federal Reserve, Goldman Sachs Global Investment Research, and GSAM. As of March 28, 2021.

2022 Midterms

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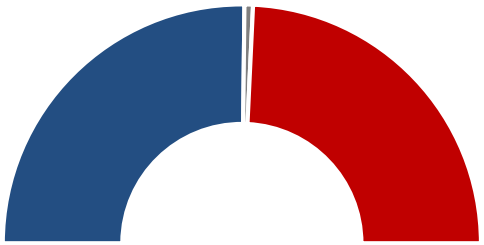
Nothing in politics is permanent, and over the last 105 years the opposition party to the president gains 31 seats on average in the midterm

Current House of Representatives

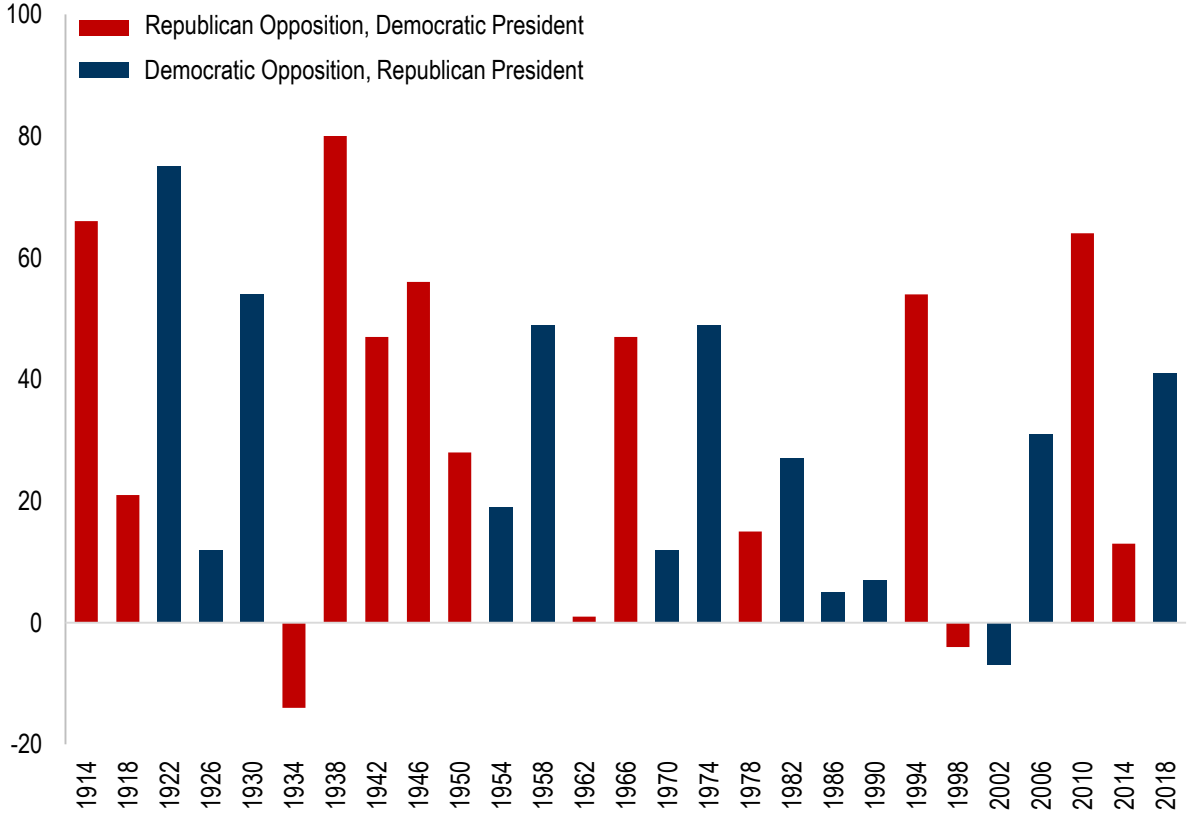


219 Democrats

211 Republicans

5 Vacant

Opposition Party Midterm Gains in the House (Seats)



Source: GSAM. As of March 28, 2021.

Key Takeaways

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- The First 100 days have primarily been focused on COVID-19 relief, the next few years will likely be centered on investing in the recovery
- Policy will likely be moderated by narrow Congressional margins
- As political risk shifts, we see value in a commitment to strategic discipline with an eye for idiosyncratic opportunities

Source: GSAM. As of March 28, 2021. The portfolio risk management process includes an effort to monitor and manage risk, but does not imply low risk.

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