



## CONVERSATION SERIES

CARY STREET  
PARTNERS

Episode 1

**Tom Herrick:** Welcome to the CIO Conversation Series brought to you by Cary Street Partners. I'm Tom Herrick, as Cary Street Partners' Chief Investment Officer I have the privilege of collaborating with some of the best minds in the business. Our very first guest on this podcast certainly fits that bill.

**Steve Pavlick:** Our timing for this conversation is actually pretty good.

**Tom Herrick:** Steve Pavlick, our guest today, is the Head of Washington Policy Research for one of Cary Street's trusted partners, Renaissance Macro Research. Renaissance is an institutional level research firm that we collaborate with on a daily basis, on a number of fronts. Steve is in Maryland near the halls of power, which is what he's an expert in. He's a veteran public policy adviser who brings a wealth of experience in the private sector and government. Most recently, he served as a Senior Legislative Affairs official in the U.S. Treasury Department, and prior to that, he was a staffer on Capitol Hill.

**Steve Pavlick:** One thing I think just to keep in mind too, just where Biden's philosophy might be is there was a Times story that actually focused on Biden sort of venting himself as a modern-day FDR.

**Tom Herrick:** Our conversation covers timely questions that are front of mind right now, current events, and pocketbook issues at a time of change in Washington.

Welcome to the CIO Conversation Series. Steve Pavlick, very excited to have you as our very first guest.

**Steve Pavlick:** Oh, thank you so much, Tom. Happy to be aboard and honored to be the first guest here.

**Tom Herrick:** We're recording this conversation the morning of February 11th. It's clearly a unique time to be in Washington, D.C., both from a legislative policy standpoint, but also the second impeachment proceedings of former President Trump. How does it feel down there in Washington these days?

**Steve Pavlick:** Well, I guess it depends on your time horizon. Over the past years, it's been a lot of activity. And from that perspective, maybe it doesn't necessarily feel all that different. I think we were hoping that maybe things would be a little quieter on this front. With respect to impeachment, I think at this point it looks like the verdict is probably something that everybody knows. We'll still go through the motions before we get there. I guess one thing that I would be curious to see how this plays out moving forward is going to be, have we seen a normalization of the impeachment process? If Republicans were to make gains in the House or Senate in 2022, for instance, would there be a lot of pressure from their constituents to actually pursue impeachment of Biden? Is that sort of the road where we're headed down? I don't know, but I think that's one of the fears that I see.

**Tom Herrick:** Before we dig any deeper into the policy conversation, I do want to describe to our audience the relationship between Renaissance Macro and Cary Street. Renaissance Macro publishes research every day to partner asset management firms, including Cary Street Partners. That incorporates economics, market strategy, sector analysis and of course, our favorite Washington, D.C. policy. This is providing depth to our own in-house work here at Cary Street Partners. How did I do, Steve?

**Steve Pavlick:** I think you nailed it.

**Tom Herrick:** Great. So let's get into it. After a year of pandemic and its impact on the economy, the pocketbook issue that's on the front of everybody's mind is the COVID relief package. President Biden's moniker for that is the American rescue plan. I refer to it as an omnibus COVID relief plan. Steve, maybe we could start with what that mix of spending looks like.

**Steve Pavlick:** Well, sure, so I think the relief plan is one of three issues. I think that the Biden administration is going to pursue legislatively, so you have the relief referring to the stimulus, you have the potential recovery that's going to refer to the two trillion-dollar green infrastructure package, as well as a redistribution which could potentially refer to tax reform. In looking at the relief package right now, there's a one point nine trillion-dollar proposal that largely mirrors what the House Democrats put forward last year in the Heroes Act. I don't think that's surprising because it seemed during the presidential campaign that Biden was pretty aligned with House Democrats in terms of what he was putting forward. So a lot of what we're seeing now is just sort of repackaged version of those ideas. I think it's probably more important to watch what the Senate actually provides, because I think at the end of the day, that's going to be the version that's more likely to resemble what we see the finished product to be. But in terms of what's actually in the package, I think it's clear that there's a lot of support for additional funds for vaccine distribution. There's going to be some additional funding for unemployment insurance benefits. Right now, Democrats are looking at boosting it from the current three-hundred-dollar federal enhancement to four hundred dollars per week. And they'd like to actually extend that beyond March 14th, which is when the current benefits are set to expire. And I think that's the target date they're trying to get this package done by in order to try to extend that potentially through the end of August. Other areas that are probably likely to make it in: additional funding for small businesses, restaurants and schools to reopen. We can talk about, I think, probably the issue of the minimum wage. That seems to be a little contentious in terms of whether or not to raise that to 15 dollars per hour and if so, when, as well as state and local governments. The proposal has three hundred fifty billion dollars. To put that in context, the original March Cares Act included one hundred and fifty billion dollars. It was negotiated back and forth between the two sides whether or not to include additional funding. And I did think it was notable that Senator Manchin's proposal actually included one hundred and sixty billion dollars in December when he was sort of leading the bipartisan efforts. That might be an opportunity for him to potentially come down on that number and lower the overall price tag.

**Tom Herrick:** If this evolves towards sort of the lower end of the betting range for the final bill, are there any Republicans, one or two, likely be in the type of numbers we're talking about that are close to being on board if we're at that lower bound of the range?

**Steve Pavlick:** Well, sure. So I'm skeptical that we're going to see one point nine trillion actually be the final number. I'm personally looking at somewhere closer to one point five trillion. I think ultimately, it's going to be Senator Joe Manchin. What number is he comfortable living with? There was a Politico article that referred to a Biden aide saying that he believed Manchin's number might be one point three trillion. If that were the case, if he were able to come down another 100 billion or two hundred billion dollars, they might be able to win the support of Senator Susan Collins, a Republican from Maine, or potentially Senator Lisa Murkowski, a Republican from Alaska. And I think that would go a long way in terms of just political optics, of having some bipartisan support. In terms of historical context, when the Obama administration proposed their recovery proposal in 2009, it was less than half the size of this one. There were three Republican senators that ended up voting for that. One happened to be Susan Collins of Maine. The other two are no longer senators. So at this point, bipartisanship is probably nice to have, but not necessary. If it's within kind of a two hundred billion or so range, I think you could see Biden try to push for that. But outside that number, I just don't think he can swing it because we have this political seesaw. If he tries to go down too far, he risks alienating support from the progressives and that could complicate the eventual vote count.

**Tom Herrick:** So if the American rescue plan, if this legislation, the COVID relief plan, if this moves by reconciliation, which, you know, you might want to explain what means for our audience, you know, this is one of those the nuances of Washington, D.C. legislation. Does that have consequences for Joe Biden's further legislative priorities? You know, primarily I'm thinking infrastructure because he's always been the infrastructure guy. Do we live on a planet where there's votes for two bills that total four trillion dollars in spending? Does that get endangered by going through a reconciliation process as opposed to a 60 vote majority?

**Steve Pavlick:** Well, I think first, just to clarify what budget reconciliation is for those that may be fortunate enough to live away from D.C. and not have to live and breathe this every day like I do. Typically, Senate requires 60 votes to pass through regular order. That actually cuts off debate and allows a vote to proceed. Now, there's a parliamentary maneuver known as budget reconciliation, which allows votes related to spending and taxes to actually pass with a bare majority of 51 votes. And again, going back to sort of the earlier point about Bernie Sanders, there's a lot of pressure from progressives right now to alter those budget reconciliation rules and potentially expand its scope. So it would potentially have the same effect of removing the 60 vote filibuster so that you could pass many of the priorities through a simple majority. And so I think that's what I'm sort of waiting to get an indication on as we see this relief measure play out, is how far do Democrats actually go in terms of altering the budget reconciliation rules? My sense

is that they'll probably be fairly successful in doing that. I think, to your point, probably an indication that we're looking at partisan votes moving forward and that Democrats would like to use the budget reconciliation process to pursue the two trillion-dollar green infrastructure proposal that Biden is proposing.

I think if they were to abandon Republican support and bipartisanship from this initial relief proposal, and keep in mind that the five previous coronavirus relief bills, all were bipartisan bills. I just think it can be very difficult to get Republicans to move forward with this. And the other thing that I think would keep an eye on, too, is just the price tag. Talking about two trillion dollars, potentially more in terms of green infrastructure spending, I don't know that Republicans would be able to support much more than a trillion. And then we're going to have the question of whether or not to pair this with potential tax increases. And I don't think many Republicans, if any, will be on board for that.

One thing I think just to keep in mind to just where Biden's philosophy might be, is, you know, there was a Times story that actually focused on Biden sort of fancying himself as a modern-day FDR. That he thinks he can actually better position Democrats for electoral success by trying to deliver on big, bold policies as opposed to incremental change. I don't think Biden is going to be somebody who is likely to run regardless in 2024, just given his age. So the fact that he doesn't have to face the electoral consequences of these decisions may again embolden him to sort of go a little bolder and without the Republican support.

**Tom Herrick:** So with that, maybe we can pivot to everybody's favorite subject, taxes. From a legislative perspective first, where do you see the priorities on the tax side? I've seen conversation about SALT, which in, you know, the great tradition of Washington, D.C., is an acronym for state and local taxes. And, you know, the deduction limit being repealed. Do you see that as a likely candidate on the tax side as the first legislative mover?

**Steve Pavlick:** Well, sure. I do think that SALT is a priority. And just for people who aren't familiar with the acronym, SALT actually stands for state and local tax. It does refer to the deduction that permits taxpayers to itemize when filing their taxes to deduct certain taxes paid to state and local governments. The Tax Cut and Jobs Act that the Trump administration and congressional Republicans pass limited that amount to ten thousand dollars per year, and that consists of property taxes as well as state income sales taxes or sales taxes, but not both. So you have a lot of Democrats from states like California, New York, Connecticut, New Jersey, they're all asking for it to be repealed because it's increased their overall rate of taxes that they are paying. And so since Senate Majority Leader Chuck Schumer is actually up for reelection in 2022, this has a sort of a personal interest for him, because I think while he's not in danger probably of losing his seat in the general election contest, he does fear a potential challenge from Representative Alexandria Ocasio-Cortez on the primary. And so I think that's where he feels that he needs to sort of deliver a win here to his constituents to lower their overall tax bill. And whether or not it's included as part of relief measures or whether it's something that might be done towards the end of the year, I think is something to keep an eye on. But that would actually lower taxes for people. I think the other question now to consider is, you know, like Biden campaigned on is whether or not to actually go ahead and move forward with a plan to increase taxes, sort of offset some of the spending that he's been proposing to do. And I think when you talk about this other issue of what the progressive priority of income inequality, I think many on the left feel that they sort of need to deliver on this. And so the areas that they're sort of pointing to are raising the corporate tax rate from twenty one percent to twenty eight percent, increasing the individual rate on those making four hundred thousand dollars or more from thirty seven percent to thirty nine point six percent, and taxing capital gains at the individual rate. I think those are probably the three things that are most likely to be considered. And there's some relief that Senator Joe Manchin, he made some comments that he would support increasing the corporate tax rate to maybe twenty five percent. But if he were to limit maybe the increases on the corporate side, will Democrats sort of look to offset the potential revenue there by going a little further on some of the individual rates? So that's something to keep an eye on. The other thing I think that's important and that's still being debated right now amongst Democrats is this issue of timing. I think moderate Democrats are particularly concerned that voting to increase taxes puts them in a politically vulnerable situation. So there's a lot of back and forth.

**Tom Herrick:** Another area we're keeping an eye on is this country's relationship with the rest of the world. One thing that is in your background is extensive foreign policy experience as it relates to trade specifically. That was a key piece of your work at the Treasury Department. You've done some very interesting work recently on our competitive relationship with China in the sort of the escalating rhetoric and tensions between Taiwan and the mainland. This is one of those potential market tail risks, you know, an unlikely event, but it may occur more often than you would think. And they have big implications. Can you comment on this and

maybe handicap how you see that confrontation evolving in terms of does it actually turn into something hot as opposed to a lot of rhetoric?

**Steve Pavlick:** Sure, well our timing for this conversation is actually pretty good. Fortuitous because President Xi from China actually spoke with President Biden from the U.S. last night, so we had some indication and Taiwan was one of the issues that was raised by Biden, in terms of the readout we got from the U.S. side. On the Chinese side, it was interesting that they provided a very different readout in the sense that they said Taiwan remains a parochial issue for them and that the U.S. should simply put butt out. So I think that reinforces this theme that Taiwan will continue to be a flashpoint. Historically, President Xi Jinping has had this goal of one China policy in sort of reuniting portions, he believes that should be a part of this. So last year, you saw him take Hong Kong because he did not really face any challenge from other countries since they were responding to the coronavirus, I think he feels a little more emboldened by this. And that based on that, my sense is that Taiwan is sort of the next domino and I think Xi is sort of calculating that Biden is probably reluctant to commit U.S. troops push comes to shove. And regardless, it's sort of a way for him to test the new Biden administration early on, sort of see what they can get away with. Both sides, the U.S. and China have really increased their military presence in Taiwan as well as the South China Sea recently. And I think that sort of poses a potential kinetic war that nobody really wants. I think what's different about Taiwan, maybe compared with Hong Kong, is that there's sort of economic and national security reasons for both sides with respect to the semiconductors that are produced there by TSMC. The U.S. comes up with the designs for a lot of semiconductors, as well as producing a lot of the equipment, but in terms of the actual fabrication and production, they outsource a good portion of that. And the most cutting edge semiconductor chips are actually produced there at TSMC, at least a good portion of them. And so you have China's larger aspirations in terms of challenging the US in sort of these critical technologies that depend very much on the production of chips. So I think that's sort of why Taiwan is a little different than maybe other regional conflicts in the past.

**Tom Herrick:** Maybe we could turn to last but certainly not least the digital world. And, you know, there's been a lot of comment from both sides of the political aisle with different perspectives, but they both seem to be dissatisfied with what's commonly referred to as Section 230, which is the Communications Decency Act, which has taken center stage. So what's the summary status of Section 230 reforms? And maybe even just starting with what is section 230? And we can go from there.

**Steve Pavlick:** Section 230 refers to the actual section of the 1996 Communications Decency Act that provides legal immunity from liability for internet services and users for content posted to the internet. I think what that means in practice is that internet companies, everything from social media platforms to online retailers to news sites, etcetera, are generally not liable if users post something illegal. I think supporters of Section 230 sort of credit it for allowing companies like Facebook and Twitter and YouTube to sort of succeed, because it depends so much on the vast amount of user generated content. As you mentioned, there's bipartisan criticism, but I think it's for different reasons. Democrats argue that tech firms do not do enough to stop the spread of misinformation and hate speech, whereas Republicans argue tech firms go too far in actually censoring conservative viewpoints. And so I sense that divide really makes it less likely that we're going to see meaningful legislation actually move this year.

**Tom Herrick:** So before we say goodbye, let's take a step back, you know, and maybe look at Washington from 10,000 feet in a general way. Do you see the possibility of greater bipartisanship over the next four years, as opposed to the last four years? Are you optimistic or pessimistic about that? You know, does the fact that, you know, Joe Biden is a creature of the Senate would seem to lend itself to the understanding that he would be more of a legislative mover? Do you have an opinion on that?

**Steve Pavlick:** I think there was a lot of hope. And certainly Biden sort of positioned himself in the campaign as somebody who was going to be a unifier and somebody who was going to pursue bipartisanship. I think, in terms of actions, matching rhetoric, I don't really see that really occurring right now. You've seen a lot of executive orders right off the bat to sort of undo the Trump administration policies. That was followed by an impeachment trial, which I think personally had Biden maybe offered to stop the trial in the Senate, that might have gone a long way to helping maybe win over some Republican lawmakers to maybe want to work with him. And now we're looking at a potential budget reconciliation used to pass his legislation without Republican votes. So I don't really see that coming. I don't want to just say it's on the Democratic side either. And just in terms of the political side, I don't really see a lot of incentives for Republicans, for the most part, to want to get reelected in states and districts that Trump carried that have much political incentive necessarily to work with Biden. Historically, the political party out of power tends to make a lot of gains in the congressional midterm election. Republicans gained 63 seats during Obama's first midterm election and 54 during

Bill Clinton's first midterm election in the House. They also gained seven seats during Obama's first midterm election in the Senate. So the reason they obtain those, that largely was by not working with him. So I think just the political calculation is probably to do that. So I don't want to sound cynical, I hope I'm wrong, but at least right now I don't really see a lot in terms of the incentives to do that. And then I look at it in sort of the folks in power there on the Democratic side, I see sort of this perfect progressive policy alignment. You have Biden, 78 years old, probably not running again for reelection, looking to try to position Democrats on delivering these bold promises. Not going to be able to do that in terms of bipartisanship. If he wants to be sort of a modern-day FDR, most Republicans aren't going to go along with that. And again, if he's not worried about facing the voters again, I don't really see him incentivized to do that. House Speaker Nancy Pelosi, she's 80 years old. She said this will be her last two years as speaker. So she's not worried about necessarily losing the House that she's not going to be in charge of and maybe more focused on trying to secure her liberal legacy in San Francisco, where she represents her constituents. And then you look at Chuck Schumer, we sort of talked about this before, concerned about a progressive primary potential threat from Representative Alexandria Ocasio-Cortez. So he sort of aligned to go along in a more liberal direction. And then you have Senate Budget Committee Bernie Sanders. I think he's 79 years old. Probably at that age, you start to think more about your legacy at this time, in this position at Budget Committee Chair probably wants to realize a lot of these things that he's been pushing for so long. So I don't want to just sound cynical, I at least want to provide some rationale for maybe how I arrived at that opinion.

**Tom Herrick:** Given the very narrow majorities in the House and the Senate going into the 2022 midterms, which are typically, difficult for the administration in power, the timeline seems like it would be to me tight in terms of the Biden agenda. If we could just wrap it all up in that kind of phrase, it's a 2021 event. Is that a fair estimate?

**Steve Pavlick:** I think you make a really great point there. I think in terms of the timeline, yeah, by the time we get to next spring, early next summer, at that point, the congressional midterm election clock sort of starts to pick up and makes it difficult to pass legislation. And I think historically, you know, Biden has been a creature of the legislature as Pelosi and Schumer. They're very aware of this. I think that's a progressive push to go big, go bold and go early. They sort of recognize that that time horizon and why they're looking to push for these things to occur sooner as opposed to later. There could also be a sort of political calculation there, too, on their part, where I think Democrats want to see this as an opportunity, one, not to miss it, because as the economy picks up the case for additional stimulus sort of declines and to think politically, they want to sort of take credit for the economy improving. Look, we passed stimulus now in a few months everything seems to look better. Republicans were on record for opposing the recovery, so I think that's sort of the political calculation that they see going on. But, you know, they tried that sort of in 2009 with the Obama Recovery Act that he put forward. And again, that was about half this size and that led to the 2010 sort of Tea Party rebellion, and Republicans making a lot of gains there. So it's risky. We'll see how it plays out. You know, a lot's changed just politically and socially since 2010, but that's sort of where I see the dynamics and maybe the impact there on the timeline.

**Tom Herrick:** Thanks for your perspective and insights, as always. It was great speaking with you.

**Steve Pavlick:** Thank you, Tom. Likewise. I appreciate you having me on and enjoyed our conversation. Look forward to doing it again.

**Tom Herrick:** That was Steve Pavlick from Renaissance Macro Research. And that's a wrap on our first edition of Cary Street Partners CIO Conversation Series podcast. For more information and insights, please visit our website at [carystreetpartners.com](http://carystreetpartners.com). I'm Tom Herrick, talk to you next time.

*The opinions expressed in this report are those of Renaissance Macro Research and are not necessarily those of Cary Street Partners or its affiliates. Cary Street Partners is the trade name used by Cary Street Partners LLC, Member FINRA/SIPC; Cary Street Partners Investment Advisory LLC and Cary Street Partners Asset Management LLC, registered investment advisers.*