Markets in a Minute:
Will the Inflation Reduction Act Actually Reduce Inflation?

The Inflation Reduction Act, which has been signed by the President and has passed the House, has been heralded as a major legislative victory for the Democratic party. The bill includes a long list of agenda items including lower prescription drug costs, charges for stock buybacks and incentives to combat climate change, all tied with the bow of the politically popular idea of "lower inflation."

But will it really matter for the economy or the markets? Reactions to the new legislation range from "tax costs exponentially outweigh benefits" to the bill will "lower costs, create jobs, and help fight inflation." As is common when it comes to politics, the answer lies somewhere in between: while the bill is unlikely to cause lower inflation (that appears to be happening on its own) it will also not significantly increase taxes.

For companies, the two most impactful parts of the legislation are a new minimum 15% corporate alternative minimum tax and a new 1% tax on share repurchases. Will the bill actually bring down inflation?

- The rapidly rising price levels that the US economy currently faces are driven by factors that are largely outside of the government's control: the aftereffects of covid shutdowns and war in Ukraine. As such, there is only so much that the government can really do.
- Both the government's own Congressional Budget Office and the University of Pennsylvania's Penn Wharton Budget Model suggest that the bill will have a negligible impact on inflation. Both analyses do agree that by year 5, the new provisions would contribute to reducing the deficit.

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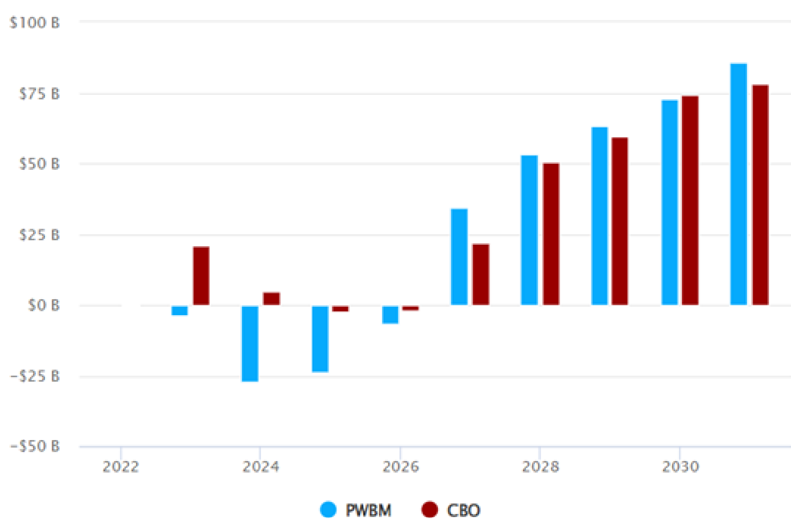
Inflation Reduction Act of 2022, Effect on the Budget

Net deficit reduction (+) or increase (-) from spending and revenues



Sources: Penn Wharton Budget Model, Congressional Budget Office

Is inflation slowing?

- The week of August 8th we had the first official report showing that inflation levels may have peaked. The consumer price index increased by 8.5% compared to the previous year and was flat compared to the prior month.
- This difference between year-over-year change and month-over-month was the source of yet another political debate between Left and Right. So, who was correct? Well, both. While year-over-year increases in prices are what hurts consumer pocketbooks, the leveling off from the previous month provides a clue that overall price increases may be slowing. It is this latter point that sent stocks soaring.

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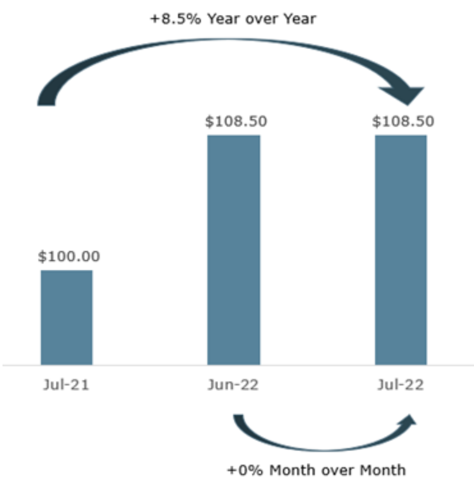
Consumer Price Index

Level of consumer prices and rate of change over different time periods



Sources: U.S. Bureau of Labor Statistics, Kestra Investment Management

Inflation is an enormously difficult beast to tame. The good news is that inflation does indeed appear to be slinking back to its cage thanks to the easing of global supply chain disruptions and the Federal Reserve's tightening of monetary policy. And the stock market has been applauding.

The real legacy of the new legislation will be in providing additional funding for health care and clean energy. Individuals will have their own political opinions on those topics, but they are thankfully outside the scope of these market updates. What we can say is that the Inflation Reduction Act is not likely to lower inflation, just as it is also not likely to hamper corporate profitability. Take that Left and Right.

(see next page for Important Disclosures)

Important Disclosures

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