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Commentary: January 2018

Most financial services companies reported 4Q2017 earnings in January. This earnings season diverged from the norm as many companies expectedly reported "kitchen-sink" quarters, accelerating expenses and other charges to benefit from 2017's higher tax rate. Excluding these extraordinary items, the quarter reflected stable to improving fundamentals and was broadly in line, leaving a clear runway for banks to maximize operating leverage going forward.

More interesting than the reported numbers were the management discussions detailing their collective outlook regarding the impact of tax reform on their business and customers. The benefits will be material and as we have discussed before, the domestic banking sector is one of the largest beneficiaries as it generally paid the highest tax rate of any S&P industry. Some of the gains will be reinvested and some could be competed away (depending on the nature of the product), but overall we are extremely positive about the effects of tax reform on the financial sector and the economy in general.

Another tailwind to the seemingly improving economy could come from discussions surrounding U.S. infrastructure investment. A $1 trillion infrastructure bill may be difficult to agree upon in the halls of Congress, but the focus on using public/private partnerships and tax credit investments by the administration, and Secretaries Mnuchin and Ross specifically, could be very powerful for many industries. Two of the major reasons for the lack of infrastructure investment is the amount of red tape involved in any project and lack of financing options other than historical government procurement practices. Public/private partnerships are used much more often to finance infrastructure projects in other parts of the developed world, with transportation garnering the largest share of investment.

We think both of these initiatives would be especially beneficial to U.S. ports and their surrounding regional economies. As we have detailed over time, the widening of the Panama Canal in 2016 to allow the transfer of much larger ships has had a material effect on import/export volumes in the Southeast, as many of the state governments have worked with their various port authorities to fund projects to improve ports' depths, efficiency, and scale, resulting in record volumes. The Ports of New York and New Jersey remain the largest container port on the East Coast, but may have a harder time expanding. Georgia Ports Authority Chairman Jimmy Allgood recently stated the following about Savannah, which can be applied to other Southeastern ports: "What sets Savannah apart is its ability to grow capacity, increase cargo and do it in an efficient manner without congestion." We expect the ports will play a growing part of many economies, especially in an era of what could be synchronized global growth, and we continue to position our portfolio to capitalize on this.

With earnings season now over, the investment team is back on the road, constantly meeting with management teams in the sector. As always, we welcome your feedback, comments, and questions.

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