



INDEPENDENT
THINKING

THE NEW STANDARD IN WEALTH MANAGEMENT

EVERCORE
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A Message from the CEO



As advisors to multigenerational families, foundations, and endowments, we are determinedly focused on the long term. This can be challenging at times – and this is one of those times, as the news from the Ukraine is so appalling and the markets are so volatile. But this discipline is also helpful to us, providing us with a lens and context through which to evaluate these developments.

No one knows how these events will play out, of course, but our initial thinking (and I am writing this only a couple of days after the Russian invasion) is that the geopolitical ramifications will be higher than the costs to global GDP, the U.S. economy, and most investors. The market repercussions of major geopolitical upheavals tend to be short-lived, illustrated by the chart accompanying Jeff Maurer's article on page 23.

At present, we do think it likely that events in the Ukraine could impact inflation, as addressed by Brian Pollak in this issue of *Independent Thinking*, as well as global energy prices and defense spending. There will be associated risks and opportunities to assess, particularly in Europe and other developed international markets, where we have been underweight for some time – an approach that has served our clients well. In the interim, we are maintaining our asset allocation, subject to regular and rigorous review.

So, more to come on these shifting geopolitics, in future editions of *Independent Thinking* and in our other client communications. (And please contact us if you didn't get a chance to view the Evercore ISI webinar *What Comes Next in the Russia-Ukraine Crisis* with guest Michael Allen, which was open to Evercore Wealth Management clients; a replay is available.)

Back in the United States, the markets appear resilient, following a correction in February. That's thanks in part to the influence of the remarkable American technology industry, as discussed by John Apruzzese in these pages. Also in this issue is an article by Stephanie Hackett on investment opportunities in illiquid alternatives and, on a related note, a Q&A with SROA Capital, a vertically integrated private equity real estate and technology platform focused on self-storage across the United States. The self-storage success story is well known by now, but we are interested in the consolidation prospects in what is still a remarkably fragmented market.

The big headlines of this year so far have pushed potential tax reform off the front pages. But it is still very much on our minds, as you'll see here in the articles by Justin Miller and Alex Lyden-Horn. The topics are different (family philanthropy and interfamily wealth transfer, respectively), but underpinning each is our continuing awareness that the gift and estate exemption will almost halve by 2026 and may be cut much sooner. Our job is to ensure that our clients are fully informed about these and other transitions in the context of their long-term goals and able to make the right – and never rushed – decisions for their families.

Speaking of focusing on the long term, I am pleased to welcome new faces and voices to Evercore Wealth Management and Evercore Trust Company, and to see others, including our Head of Operations and now newest Partner, Sebastian Granzo, flourish in their roles. One of the joys in managing an entrepreneurial firm, perhaps especially for me and our other partners, is to teach – and learn from – our new colleagues. We are building a strong, diverse, and inclusive team across the United States, reinforcing the best of our culture, and growing to meet new challenges and opportunities.

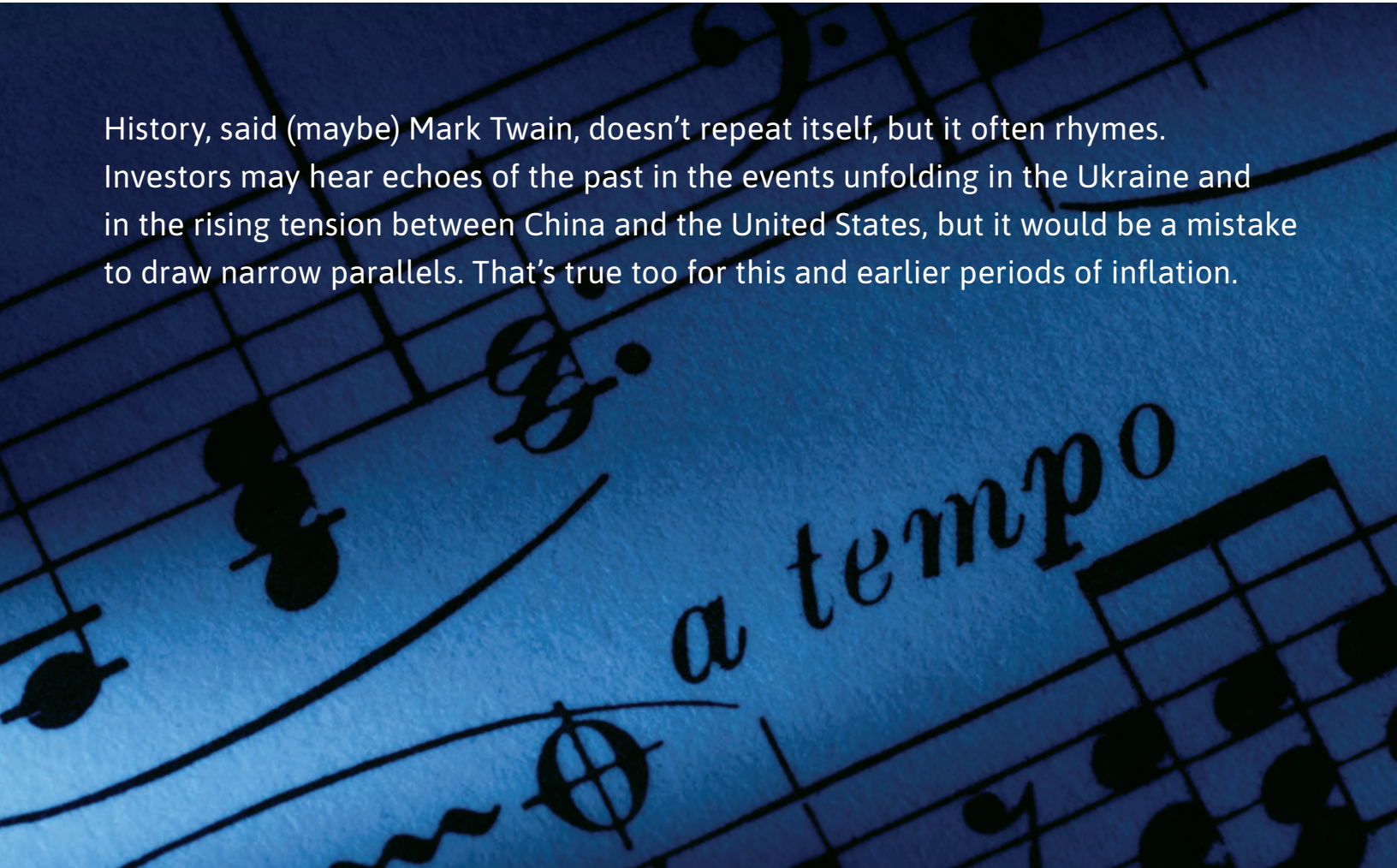
I hope that you and your family are well in this stressful time, and that you find this issue of *Independent Thinking* informative and engaging. We are developing a strong event series for this year, so please look for invitations, both for in-person and virtual gatherings, as appropriate. We look forward to seeing you.



Chris Zander
President & Chief Executive Officer

Echoes of the Past in a New Economy

By Brian Pollak



History, said (maybe) Mark Twain, doesn't repeat itself, but it often rhymes. Investors may hear echoes of the past in the events unfolding in the Ukraine and in the rising tension between China and the United States, but it would be a mistake to draw narrow parallels. That's true too for this and earlier periods of inflation.

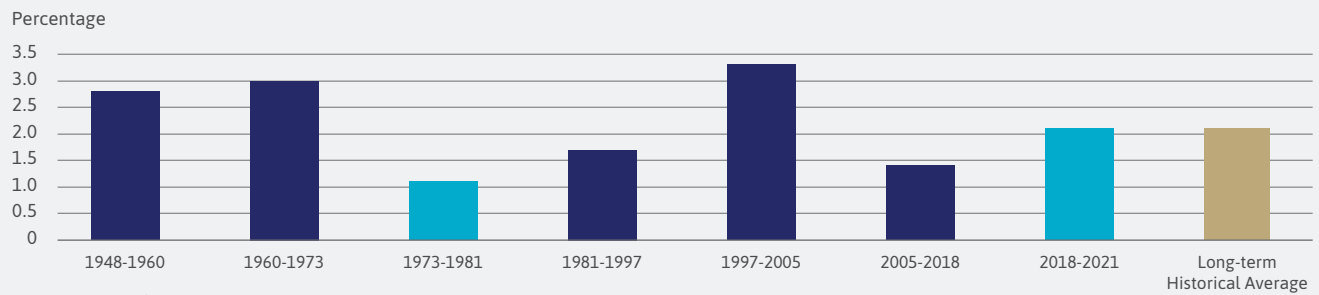
The Consumer Price Index, or CPI, is 7.5%, its highest rate in 40 years, a shocking change after two decades at under two percent. And potentially sustained higher prices for global commodities, notably oil and wheat,

in the wake of the Russian invasion of the Ukraine, won't help. Some observers are understandably anxious that this could signal the start of another period like 1973-1981, when inflation averaged about 9.25% and

real GDP growth was modest, a combination known as stagflation. But today's situation is different on three major counts: productivity, demographics, and the relationships between wages and prices.

Productivity: Not the 1970s

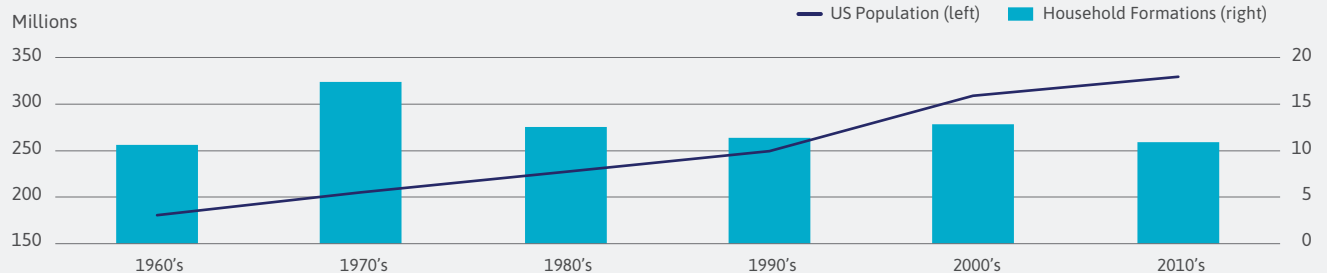
Average Annual Productivity Growth Rates for Selected Periods



Source: Bureau of Labor Statistics

Home is [Still] Where the Parents Are

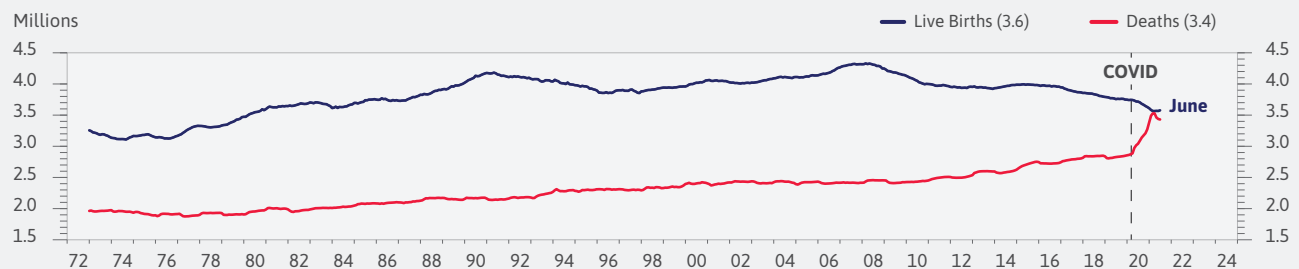
U.S. Population vs. Household Formations



Note: In millions. US population as of the end of the listed decade.
Source: Federal Reserve Economic Data

Converging Birth and Death Rates

U.S. Live Births & Deaths (12-month sum)



Note: WHO declared global COVID-19 pandemic on 3/11/2020.
Source: US National Center for Health Statistics, Vital Statistics of the United States, and National Vital Statistics report

PRODUCTIVITY

The nine years starting in 1973 marked the lowest productivity rates post-WWII, generating just 1.1% labor force productivity growth, or half the rate for the full period, as illustrated in the chart on page 3.

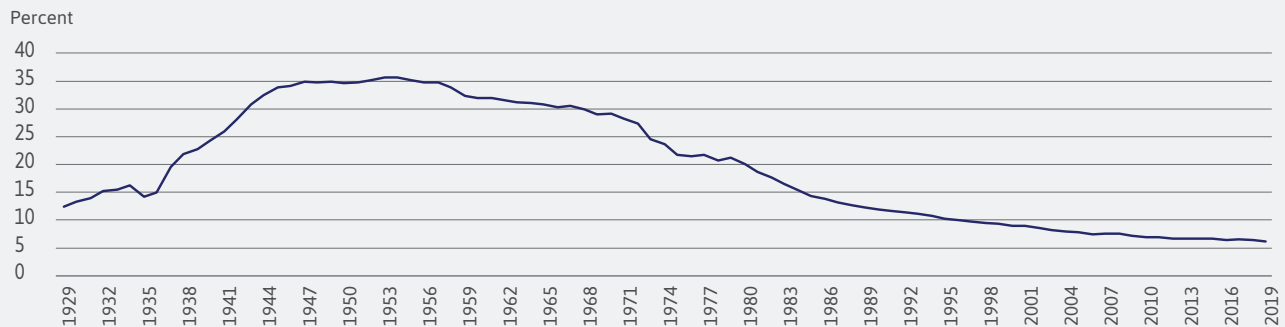
Today, there are reasons to think that the recent uptick in productivity in the

last two years could usher in a period of still higher (above 2%) productivity growth. In addition, capital spending (CapEx) is robust, with expenditures increasingly focused on technological advancements and significant productivity-enhancing technology. We can see this through the growth in robotic installations across all industries, which has been steadily growing in the last decade, and the

percentage of overall CapEx that is focused on new technology. While we may not see a 50s-, 60s- or late 90s-style productivity boom, recent CapEx trends and technological advancements should drive productivity to at least the long-term average of above two percent. Strong productivity growth perhaps makes the best case for why stagflation is less likely moving forward.

The State of the Unions

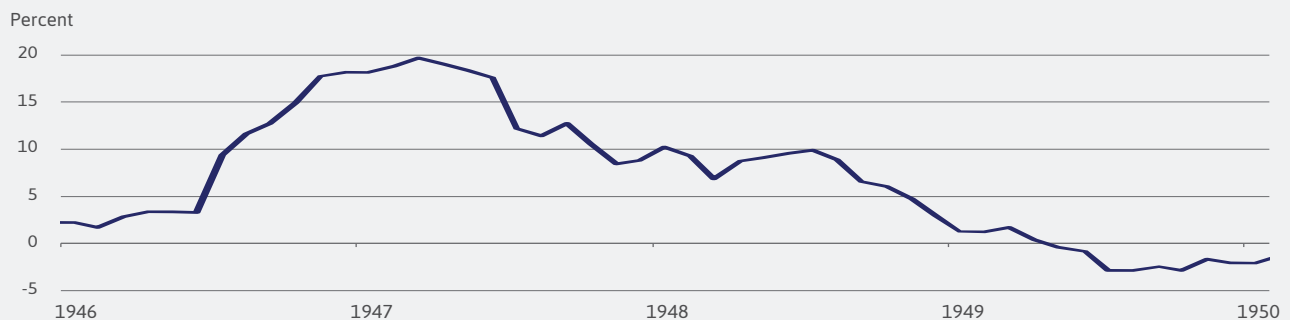
U.S. Private-sector Union Membership Rate (1929-1972)



Note: There is no definitive, fully time-consistent series on union membership as a share of employment. Figures for 1929-1972 were compiled by Troy and Sheflin (1985, Appendix A) from union financial reports; those for 1973 forward are compiled from Current Population Survey (CPS) household data (Hirsch and Macpherson, 2003, updated at <http://www.unionstats.com>). 1973-76 CPS figures adjusted to account for association members, who are included both in the Troy-Sheflin series and in the CPS beginning in 1977. 1973 CPS figure adjusted so that 73/77 CPS ratio equals 73/77 ratio in Troy and Sheflin. Source: Economic Policy Institute

Back to the Future?

Post-World War II Inflation



Note: Consumer price index, monthly, year over year, not seasonally adjusted. Source: Federal Reserve Economic Data

DEMOGRAPHICS

While the Millennial generation is almost as large as that of their Baby Boomer parents, they aren't forming households and having babies at anything like the same rate. Indeed, there were nearly seven million fewer households formed in the decade of the 2010s than in the decade of the 1970s, despite a population base that was nearly 40% smaller. With fewer new households being formed, it is no wonder that the number of births and deaths in 2021 was roughly the same. COVID-19 contributed to the deaths, but the low birth rate did far more to change the equation. (See the chart on page 3.) With birth rates so low, U.S. population growth will depend solely on net immigration, a trend that has also recently been moving in a negative direction.

At the same time, Baby Boomers are retiring at a high rate (the youngest Boomers are now in their late 50s). As retirees generally consume less than those in the labor force, and households with babies generally consume more than those without children, it seems that downward pressure on demand will serve to also dampen inflation for some time to come. It's also worth noting that even though Boomers are retiring, the average age of the labor force continues to increase, another potential argument for long-term high productivity and low inflation.

WAGE-PRICE SPIRAL

In the 1970s, unionization was broad-based in the private sector, representing between 25%-30% of the private sector work force through most of the decade – down from its peak in the 1950s but a powerful force nonetheless, as illustrated on page 4. Many of the unionized private sector labor contracts in the 1970s (as high as 59% in 1970) were subject to

cost-of living adjustments, or COLAs, meaning that many union wages were tied directly to inflation. A manufacturer of the day, having its primary expense (labor) tied directly to inflation, and with little advancement in productivity to offset those higher costs, would have no choice but to increase the price of products to keep margins at least somewhat intact. Higher prices passed through to the consumer would again impact the calculated rate of inflation in the labor contracts, causing further wage increases.

Today, with only 6% of the private sector labor force unionized, and a very small percentage of that group with wages tied to COLAs, a 70s style wage-price spiral is quite unlikely, even if wages continue to rise.

During the 1970s, Baby Boomers were pouring into the labor force, causing an oversupply of labor, which theoretically should have driven the price of labor down. But because of the combination of high unionization rates and high rates of COLAs in collective bargaining agreements, labor costs continued to rise. The abundant supply of workers also made it easy for corporations to hire new workers as needed, and corporations in aggregate did not make significant technology-driven capital investment to reduce their labor costs and improve productivity.

Today, there is a real labor supply problem. In 2021, wages rose 5.7%, with lower-wage workers experiencing a higher wage increase than higher-wage workers. Although they did not quite keep up with the high rate of inflation, further increases are expected in 2022. Can corporate margins keep pace with these wage increases? As John Apruzzese discusses in this issue of *Independent Thinking*, productivity will determine the answer. If wages increase

by 4% and productivity increases by 2%, the unit labor costs will be increasing by 2%, a manageable scenario for most companies and a healthy increase in wages for most employees.

Can corporate margins keep pace with wage increases?

While there are many other factors that could impact the economy and the inflation backdrop, and we are certainly maintaining vigilance in portfolios to protect against worst-case outcomes, we don't think the current period will repeat, or even rhyme with, the 1970s. Perhaps the post-World War II bout of inflation, between 1946 and 1948, is more analogous. Then, as now, there was significant suppressed demand and supply chain disruptions, and then a sudden spike in consumer demand, which caused inflation to surge to 20% in July 1947. Inflation, as illustrated on page 4, then quickly dissipated, and a period of disinflation set in.

We are living in interesting times, with echoes of the past but also important new influences. For now, we are comfortable with our current asset allocation and remain confident in the continued strength of corporate earnings and real GDP growth. We will be watching for potential new risks and opportunities, including in Europe, where we all hope for better days soon.

Brian Pollak is a Partner and Portfolio Manager at Evercore Wealth Management. He can be contacted at brian.pollak@evercore.com.

Powering Up: Technology Continues to Drive the Markets

By John Apruzzese

The four biggest technology companies account for 21% of the S&P's market capitalization.



American technology companies have powered the market gains of the past five years and the astonishing 48% surge in the S&P 500 from pre-pandemic highs. The sector's four biggest constituents (Apple, Microsoft, Amazon, and Alphabet, the parent of Google) now generate average annualized profit margins of 25% and account for 21% of the S&P 500's market capitalization. Their ability to consistently maintain these extraordinarily high margins ranks them among the most successful companies in the 200-year history of limited liability corporations. No other country has anything to rival them.

Now what? The recent market correction could be attributed to a growing recognition among investors that valuations, while not at record levels overall, need to come down in the face of higher inflation and prospectively higher interest rates. Or it could signal that future earnings may come in significantly below the consensus projection of 9% growth rate for this year and 10% for next year.

Either way, revenues are not likely to disappoint, assuming the pandemic ebbs and fairly high nominal economic growth continues. But can the technology giants, and by extension, the S&P 500, continue to generate record-high profit margins in the face of increasing costs? There are good reasons to think so, at least until we see evidence to the contrary.

First, the economy-wide investment in software, computer equipment, and research and development is growing at a rapid pace relative to GDP. As

described on page 5, we believe this growth rate will continue or increase. Companies are searching for ways to replace labor with technology.

Of course, some companies and entire sectors will be able to make this shift more easily than others. We are constantly on the lookout for the technology companies providing the best solutions, and for the companies in other sectors most likely to benefit from implementing that technology. One of the best examples of broad-based productivity enhancement through technology is the transition of most business software applications to the cloud. The major cloud providers, such as Amazon and Microsoft, are able to significantly reduce the cost of running essential business software for non-tech companies, as well as allow new companies with disruptive ideas, like Uber and Netflix, to scale quickly and easily. As remarkable as it seems, given all the technological changes

25%

The average annualized profit margins of Alphabet (Google), Apple, Amazon and Microsoft for 2021

of the past decade, we are still in the early stages of businesses moving to the cloud.

Second, many of the companies implementing technology into their businesses will themselves be able to increase productivity at a fast enough pace to offset current wage price increases. Those facing rapidly increasing labor costs are particularly incentivized to replace labor with software-driven technology if possible, a self-reinforcing virtual circle, at least from a profitability viewpoint.

Third, technology companies are also increasing their own rates of productivity, providing increasingly more powerful products and services at lower prices per unit of utility. Software companies are unlikely to suffer from the current spike in wage inflation. While great software engineers don't come cheap and there is a shortage of programmers in this country, that could soon change if related visa restrictions are eased; otherwise these jobs will move offshore.

Indeed, it could be argued that the profit margins of software companies are understated, because their biggest current expense – paying coders to write new software – represents their biggest investment in the future. Established software companies have very little need to reinvest profits in

traditional capital investments to drive future growth, so they are free to use their profits for dividends or share buybacks.

Most other sectors have healthy margins, notably pharmaceuticals, but not at anything like the tech industry levels – and they require the reinvestment of over half their profits to grow. The productivity of software companies as measured by revenue and earnings per employee remains unrivaled, and that productivity grows as software gets written on top of established programs. In addition, the application of the software a company sells enhances the productivity of the purchaser.

Fourth, we think the large tech companies will manage to maintain

their high profit margins and that the implementation of software by companies in other sectors will reduce the risk of a wage-price spiral. One caveat: The large software companies currently pay very little to no corporate taxes because they are able to move their most valuable assets – the licenses on the programs – to tax havens. Although it's easier said than done, the United States and other major countries would like to see the giant tech companies pay more tax. There is also rising political pressure to rein in these companies through increased regulations and antitrust legislation, which we will be monitoring.

So, there are some good reasons to remain positive about the technology sector in particular and the United

States in general. However, we are mindful that our clients have enjoyed high returns over the past decade from their large-cap technology investments. We continue to hold significant positions in these companies but remain careful to rebalance portfolios as appropriate, taking profits and reinvesting in companies likely to benefit as the economy fully reopens – and technological advancement and adaptation powers on.

John Apruzzese is the Chief Investment Officer at Evercore Wealth Management. He can be contacted at apruzzese@evercore.com.

OUTLOOK RECAP

Chris Zander, CEO of Evercore Wealth Management and Evercore Trust Company, and Chief Investment Officer **John Apruzzese** hosted the *Independent Thinking* webinar, The 2022 Investment Outlook, on January 11, 2022. To view a replay of the broadcast, please visit our website or contact your Evercore advisor.



Chris Zander



John Apruzzese

Investing in a Digital Future

By Michael Kirkbride

Kidney disease forecasting, drywall hanging, pizza delivery and crop management: These are just a few examples of activities being transformed through technology. The digital economy (ecommerce, software, tech hardware and so on) now represents more than 10% of the U.S. economy.

And there's more to come. More than half of corporate capital expenditure, or CapEx, is now being invested in productivity-enhancing investments like cloud technology, artificial intelligence and vision technology, as well as robotics and the like. The \$700 billion projected to be spent globally over the next decade building cutting-edge software for the cloud may herald exponential growth in related data applications, such as autonomous vehicles and automated manufacturing. At the same time, the investment payoff timeline is accelerating. Investments in robotics, for example, now pay off in half the time that they did 10 years ago.

The technology companies are both the beneficiaries and drivers of these trends, as John Apruzzese observes in the article on page 6 of this issue of *Independent Thinking*. Amazon spent more on CapEx in the past two years than it did in the previous 20, and Microsoft is working with thousands of organizations around the world to grow and combine their physical and digital worlds, and to explore collaboration opportunities in the metaverse.

A few other examples of current new economy investments in general, and digital investments in particular, by companies in the Evercore Wealth Management core portfolio holding include:

- **Blackrock's** investments in its Aladdin processing system have increased the productivity of its customers throughout the financial sector;
- **Williams Company** has entered into an agreement with Microsoft to bring sensor technology and artificial intelligence, or AI, to help in the move toward carbon neutrality;
- **McDonald's** has been improving throughput and ameliorating the impact of labor shortages through its investments in digital and process technology;
- **United Health** continues to ramp up investment in data analysis, driving outcome-effectiveness and cost-saving efficiencies throughout the healthcare system;
- **Home Depot** continues to invest in the technology underpinning the transformation of its supply chain, significantly increasing the efficient delivery of orders to end customers through a more efficient and reimagined distribution system;
- **Federal Express** has invested in data technologies that are driving network efficiencies, reducing package touches and providing more accurate delivery time estimates.

As these and other corporations continue to invest in improving their productivity, economy-wide productivity should also increase.

Michael Kirkbride is a Managing Director and Portfolio Manager at Evercore Wealth Management. He can be contacted at michael.kirkbride@evercore.com.

Illiquid Alternatives: Looking for Diversification and Alpha Opportunities

By Stephanie Hackett

Illiquid alternatives is an umbrella term for different types of investment strategies that range from venture capital and private equity, to illiquid credit strategies, to investments in real estate and infrastructure projects. Many of the portfolios that we manage have a 5%-20% allocation to these illiquid assets, as these investments have the potential to generate strong returns relative to traditional asset classes.

An optimal allocation should have exposure to multiple strategies and diversification across vintage years, industry sectors, stages of investment and geography. In addition, illiquid portfolios can be structured so that maturing investment proceeds can be reinvested in similar strategies, allowing the pacing to become self-perpetuating. As with any investment, illiquid alternatives should be evaluated in the context of each qualified investor's risk tolerance, liquidity needs and investment horizon.

Investors should consider adding illiquid assets to their portfolio that have the potential to provide diversification and alpha opportunities:

- **Diversification:** Adding investments that are uncorrelated to stocks and bonds may improve a portfolio's

risk-adjusted return. Opportunistic niche investments generate returns based on risks unrelated to equity markets, such as weather events, drug approvals, litigation outcomes, or cryptocurrencies and blockchain technology. Private real estate offers diversification and a potential hedge against inflation. Real estate spans broad risk-return opportunities from development/construction to core properties, and across a range of property types including office, multifamily housing, retail, industrial and logistics.

- **Generating income in a low-yield world:** As global yields remain at or near historic lows, many investors trade liquidity for nontraditional income with higher yields, such as middle market corporate lending, consumer lending, real estate

lending, and specialty finance. Income-producing real estate, such as triple net lease or self-storage properties (see our Q&A with SROA Capital on page 12), generate attractive cash flow with the potential for capital appreciation. Some investments, such as solar development, can offer attractive uncorrelated yields and may help investors meet their impact goals.

- **Growth:** Private equity growth and venture investments offer exposure to fast-growing companies and new technologies not accessible via public markets. Private equity managers have multiple ways to create value through economic cycles, including strategic and operational measures, acquisitions, and capital structure optimization.

Illiquid alternative strategies can be attractive additions to a portfolio for qualified investors comfortable with a degree of complexity. They are long-term investments that may take a decade or more to return capital. The fee structures are generally higher than for stocks or bonds, and the timing of capital calls and distributions is unpredictable. Illiquid alternative investments also often have more complicated tax filing and require extensions. Investors rightly expect a premium return to compensate for this lack of liquidity, such as the potential to outperform public markets by at least 300-500 basis points, along with portfolio diversification.

Illiquid investments have the potential to provide diversification and alpha opportunities.

Even investors who are older should consider illiquid investments, as they can be a valuable tool in estate planning. For other investors with compressed timelines or other constraints, illiquid alternatives may not be suitable. But for many high net worth investors, foundations and endowments, these investments offer the prospect of enhanced returns and diversification.

Stephanie Hackett is a Partner and Portfolio Manager at Evercore Wealth Management. She can be contacted at stephanie.hackett@evercore.com.



5% - 20%

The allocation to illiquid alternatives in many Evercore Wealth Management portfolios

Q&A

with SROA Capital



Ben Macfarland

Editor's note: Evercore Wealth Management supplements its core investment capabilities with carefully selected outside funds across the range of the firm's asset classes. Here we discuss opportunities in self-storage with Benjamin S. Macfarland III, Chief Executive Officer and Co-Founder of SROA Capital, LLC ("SROA"). SROA is a leading, vertically integrated private equity real estate and technology platform that has an established track record of providing risk-adjusted returns to its capital partners through its focused strategy of investing in self-storage throughout the United States. Evercore Wealth Management recently invested in its most recent fund, SROA Capital Fund VIII. Please note that this article represents the views of SROA and not necessarily the views of Evercore Wealth Management.

Q: Self-storage has been a huge pandemic play for investors, with returns for the asset class outstripping real estate investment trusts and the broader market by a considerable margin. Why do you think that is – and do you worry that it's going to change as the pandemic subsides?

A: The pandemic has generated a surge in storage demand as people were dislocated for periods of time and, in many cases, have changed the way they work and live. Whether

it was college kids forced off campus, young professionals moving back in with their family, professionals clearing out an extra bedroom to create space for a home office, or investment managers moving their businesses and families to Miami, people from all sorts of backgrounds found themselves in a transition.

Storage is not a new concept. It has been around since the 70s and has become a widely accepted commodity. Today, storage is utilized by both businesses and individuals, with roughly one in 10 U.S. households renting a unit. For individuals, storage serves as a short-term solution during a life event or as a long-term extension of the home. Life events creating a need for storage can be positive (relocating for a new job or building a new home) or negative – something we call the "4 D's" – death, divorce, downsizing, and dislocation. Positive life events have a strong positive correlation with the macroeconomy, while negative life events have a strong negative correlation, creating demand during both good times and bad. For small businesses, storage functions as a critical part of the supply chain. A contractor uses storage for equipment and materials, while the owner of an e-commerce business utilizes storage for order fulfillment. During prosperous times, businesses move from the garage to a storage facility, and during bad times, as we saw with COVID-19, businesses downsize from a light industrial warehouse to a storage facility. Storage has become an integral part of the economy as more and more Americans recognize its benefits.

One of storage's most attractive traits from an investment perspective is its ability to generate consistent growing dividends that can be sustained through down cycles. This is a major reason why storage has outperformed other asset classes, and we expect this to continue.

Q: As you say, there are a lot of storage units out there, a lot of different companies. How do people decide which to use?

A: At SROA, we are a consumer-facing business. Every day we interact with consumers who rent space to solve a problem. When you think about storage, I think it's analogous with an emergency room – you only need it when you need it, and you're not going to spend a lot of time shopping around. And so, the location of a facility plays an important role when acquiring customers. In fact, of the roughly 80,000 unique tenants we have at SROA, close to 75% of them live within five miles of their unit.

Now, location is always an important factor, but you need to have other ways to attract new tenants. At SROA, we have built an operational technology platform overseen by an in-house digital marketing team that focuses solely on our marketing and digital web capabilities – things like search engine optimization (organic search) and search engine marketing (pay per click) – to develop targeted customer acquisition strategies for each market and property. We also have a 30-person customer call center that fields over 10,000 calls a month. Having this infrastructure in place is a critical component of our business, and its importance was highlighted more than ever by the onset of COVID-19. Pre-COVID, roughly 65% of our customer leads were generated through digital channels, be it from a Google search or paid advertisement; at peak-COVID levels, this figure jumped to over 90%. And today, this figure has settled down around 84%; we believe it will stay in this range.

Q: Self-storage is a highly fragmented asset class that is recognized for its strong performance during the COVID pandemic. How has the competitive landscape changed within the industry, and how do you see this industry consolidating?

A: Storage was one of the best performing asset classes during the pandemic and the best performing REIT sector during the great financial crisis. During the depths of COVID, our occupancy was flat year over year, rent collections were up, and we maintained our quarterly distributions, something we have never missed since I founded SROA in 2013. Given the strong performance of the asset classes during these periods, we have seen several new entrants into the space, but most are really only focused on acquiring large, brokered portfolios (>\$500mm). This has had little to no effect on our business and, in the end, they have provided us with another exit option by deepening the institutional buyer pool for large portfolios.

A few other reasons we have seen little change to the competitive landscape include the size and fragmentation of the market and our focused roll-up strategy. First on the market, Public Storage is the largest player in the space with a market cap of ~\$65 billion, and they only own 5.8% of the market, which means self-storage is a ~\$1.1 trillion market. The top 100 operators only own ~29% of the market; the remainder is owned by non-institutional (or “mom and pop”) owners. We see this landscape evolving over the next five to ten years as these mom and pop owners approach retirement

age and look to sell their assets. The largest group of these owners is the Baby Boomer generation who lack succession and estate planning. Let’s face it, storage is not a sexy business, and more times than not the second generation would rather sell the business than assume operations. That’s where we come in. Our focus has always been on acquiring regional operators to expand our footprint into new markets and to then send our dedicated in-house acquisitions team into these new markets to acquire smaller independent storage operators. To date, this strategy has served us well, as 81% of our acquisitions have been sourced off market.

Q: What do you think about current market conditions, notably the increasing volatility and the prospect of inflation?

A: Volatility in markets creates opportunities, and we have been a direct beneficiary of the public market volatility created by COVID. The first acquisition in the SROA Capital Fund VIII was a 16-property portfolio in southern New England (Connecticut, Massachusetts, Rhode Island) that came about when a large public REIT was forced to drop the deal when their stock sold off ~30% in April of 2020. This was a portfolio that we had bid on but were ultimately outbid by the REIT. When we heard that the REIT had dropped the deal, we immediately called the seller and were able to negotiate the purchase on a direct basis without it ever going back to market. This portfolio has been the best performer in the fund. We have already acquired two additional properties in New England and are looking to expand our footprint in this region.

As for inflation, we welcome it and view it as a tailwind to our business, but we do not want to see hyperinflation. There are few asset classes better suited for an inflationary environment than storage, as all our tenants are on month-to-month leases, which allows us to raise rents with 30 days’ notice. People who are not familiar with the asset class often view these month-to-month leases as a liability, but our average length of stay is ~14 months, which is longer than multifamily and, more important, provides us with real pricing power to protect against inflation.

For further information on SROA and the other externally managed funds on the Evercore Wealth Management platform, please contact Partner and Portfolio Manager **Stephanie Hackett** at stephanie.hackett@evercore.com.

Preparing the Next Generation for Success

By Justin Miller

In preparing the next generation of young children and grandchildren to be happy and productive members of society, we believe that one of the single best activities to consider is family philanthropy. For parents and grandparents looking to transfer values to future generations and create a lasting legacy, family philanthropy can't be beat.



The benefits of philanthropy are extraordinary and well documented. Giving can boost happiness and satisfaction, increase life expectancy, reduce stress, and ease depression.¹ For children, philanthropy can be especially impactful. By engaging in charitable activities, children experience increased well-being, popularity, and acceptance among peers, which leads to better classroom behavior and higher academic achievement.²

Family philanthropy is about giving together as a family. Collective, communal, and cooperative giving helps solidify family values. Through making gifting decisions as a family, younger family members can develop a wide variety of skills, including communication, negotiation, shared decision-making, leadership, accountability, investing, financial literacy, and responsibility to help others. As an added benefit, family philanthropy teaches the same skills that are necessary to prepare the younger generation to manage and expand the family's wealth in the future.

ESTABLISHING A FAMILY PHILANTHROPY PROGRAM

Family philanthropy is not only accessible to the wealthiest families with private foundations. Even for families without private foundations, a donor-advised fund, or DAF, could serve as a great cost-efficient resource for parents or grandparents to begin family philanthropy programs for younger members of their families. Because

DAFs typically offer user-friendly online platforms without the expense and administrative burdens of a private foundation, they are often the ideal charitable vehicle to help the younger generation become a part of a family philanthropy program.

Collective, communal, and cooperative giving helps solidify family values.

Before engaging in family philanthropy, it's important for the elder generation to first facilitate a family meeting, which should include a meaningful discussion about philanthropy with the entire family – ideally, one where each member of the family proactively participates. Research has shown that conversations between parents and children about charity have an even greater positive impact on children than parents serving as silent role models through their own philanthropic activity.³ With the additional help of a neutral professional facilitator, this family meeting also could benefit from the inclusion of effective communication exercises, as well as the use of tools to help the family members discover their common values and vision.

Children can become part of a family philanthropy program as young as five years old and can begin to play a deeper role with respect to the actual

administration and investments of the family philanthropy program before they're teenagers. Family members may wish to set standards for performance to accompany each grant given as part of the family philanthropy program, and selected charities that attain those standards might be allocated more funds in future years. The children can propose – and advocate for – a grant request, which could include site visits to the proposed grantee and interviews. A family philanthropy program could even require each participant to make some type of personal investment in any organization that will be receiving funds – such as actively volunteering with the organization or making a small personal gift along with the larger donation from the family philanthropy program.

As part of the family philanthropy program, each family member could be given a relatively small amount to donate to charity independently. In addition, a separate larger amount may be set aside for all the family members (for example, siblings or cousins) to give away as a collective unit – so that they will be required to discuss and agree together on the organization receiving the donation. Many organizations encourage children's participation in philanthropic activities and welcome the younger members to visit their facilities and even volunteer – often a terrific way to unite family members as they work together toward a common goal. For more substantial donations, particularly ones in which the family name will be recognized, involving the whole family can help instill a sense of pride in the family legacy. So long as the elder generation does not assert too

¹ Dunn EW, Aknin LB, Norton MI, "Spending money on others promotes happiness," *Science*, Vol. 319, Issue 5870, pp. 1687-1688 (Mar. 21 2008); Harbaugh W, Mayr U, Burghart D, "Neural Responses to Taxation and Voluntary Giving Reveal Motives for Charitable Donations," *Science*, Vol. 316, Issue 5831, pp. 1622-1625 (Jun. 15, 2007).

² Layous K, Nelson SK, Oberle E, Schonert-Reichl KA, Lyubomirsky S, "Kindness counts: prompting prosocial behavior in preadolescents boosts peer acceptance and well-being," *PLoS One*, 7(12): e51380 (Dec. 26, 2012).

³ "Women Give 2013: New Research on Charitable Giving by Girls and Boys," Lilly School of Philanthropy, Indiana University, Women's Philanthropy Institute (Dec. 2013).

Getting Started in Family Philanthropy

When it comes to that first family meeting, a good place to start is by asking each member of the family to address the following very specific who, what, when, where, why and how questions:

- Who do we want to be as a family?
- What are we trying to accomplish?
- When should we start?
- Where do we want to end up?
- Why do we care?
- How are we going to get there?

To maintain a strong family philanthropy program over time, the program should have the following four components:

1. Choose philanthropic projects based on shared family values.
2. Encourage proactive participation from family members and shared decision-making.
3. Define goals, measure and review performance, and evaluate success.
4. Continually learn from experience to improve in the future.

much oversight or control over the program, family philanthropy typically is an extremely positive experience for the younger generation.

Consider the experience of a married couple with three children, ages 11, 13 and 18. They provide \$1,000 annually to each of their children to give away on their own. They also set aside \$5,000 annually for their children to give away together. The couple allows their children to explore their own passions and helps facilitate the group discussion to accommodate the different age ranges of their children and their different communication styles. In the first year, after visiting and volunteering at multiple charitable organizations, the 11-year-old and 13-year-old give their \$1,000 to a local animal shelter, and the 17-year-old decides to give his \$1,000 to a micro-lending organization.

As a collective gift, the three children discuss the family's values and vision with their parents and decide to give the entire \$5,000 to a cancer research organization, in the name of their grandfather who had died in his early 50s from cancer. For the upcoming year, the couple allows their three children to decide how to invest the \$8,000 in annual funds for the family philanthropy program. If the investments do well, they will have more to give away; but if they take too much risk and make bad investment decisions, they will have less to give away. It's a real-life lesson, administered with care.

The right giving approach is different for each family. Ultimately, however, family philanthropy helps younger family members learn both independence (how to be self-sufficient and self-supporting) and interdependence (how to be emotionally, economically,

The right giving approach is different for each family.

ecologically, and morally responsible to other family members). With such an overwhelmingly positive impact, we believe that family philanthropy should be a top consideration for every family beginning a journey toward healthy governance.

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A Formula for Maximizing Gift Exemptions

By Alex Lyden-Horn

In the absence – yet – of new tax legislation, families face continued uncertainty regarding the future of the estate and gift tax systems. Washington could remain in deadlock on this issue, of course, but tax changes could also be back on the agenda soon, along with the possibility that they could be made retroactive to the beginning of the year. As it is, the current inflation-adjusted exemption of \$12.06 million is set to recede to about \$6.5 million in 2026.



Historical Estate Tax Exemption Amounts and Rates Per Person:

2004-2005	\$1,500,000	48-47%
2006-2008	\$2,000,000	46-45%
2009	\$3,500,000	45%
2010-2011	\$5,000,000	35%
2012	\$5,120,000	35%
2013	\$5,250,000	40%
2014	\$5,340,000	40%
2015	\$5,430,000	40%
2016	\$5,450,000	40%
2017	\$5,490,000	40%
2018	\$11,180,000	40%
2019	\$11,400,000	40%
2020	\$11,580,000	40%
2021	\$11,700,000	40%
2022	\$12,060,000	40%

Source: <https://www.irs.gov/businesses/small-businesses-self-employed/estate-tax>.

\$1 million, putting you in no better place than if you had waited. If you used the full current exemption, the amount over \$6 million and less than \$12.06 million would not be subject to any clawback gift tax or estate taxation on your death if the exemption were later reduced.

\$12.06 MILLION

The current estate and gift tax exemption per person

There are also risks. One danger with gifting the entire exemption amount is that it leaves little margin of error should the IRS adjust the value of the gift – any increase in the valuation will be subject to an immediate 40% gift tax.

An IRS adjustment is generally not an issue with easy-to-value assets, such as cash, marketable securities, or U.S. treasuries; there are very clear valuation guidelines for those assets (for example, publicly traded securities are simply valued at the average of opening and closing values on date of gift), which leaves little room for an IRS challenge.

Assets without a readily available market price must comply with the amorphous “willing buyer and willing seller” test. Even with a comprehensive appraisal performed by an experienced appraiser, there is always a risk that the IRS will challenge the valuation, particularly if discounts for lack of marketability or control are being used. Also, if the gift fully utilizes the exemption, then

That’s no reason to rush in, of course. Significant wealth transfer should always be informed by substantive discussions among family members, and with the family’s wealth and fiduciary advisors and other trusted members of their team. As Jeff Maurer writes on page 20, the starting point should be a thorough analysis of whether the donors can maintain their lifestyle after the gift is made. But for families who have done the planning work and are prepared to make gifts, there may be several non-tax benefits to be gained by gifting sooner rather than later (or not at all).

First, gifting now removes future appreciation from the estate. Second, it provides current creditor protection. Third, it may enable the estate to avoid state estate or inheritance taxes on the gifted assets.

As for the tax advantages, there is a considerable incentive to give as much, if not all, of the current exemption amount in this environment. Look at it this way: If you were to make a gift that used \$5 million of the current \$12.06 million exemption, and the exemption were to be reduced to \$6 million, your remaining exemption at that time would be

the IRS has the added incentive of an immediate payday if it is successful in challenging the valuation.

The easiest solution to the problem of revaluation would be to gift only easy-to-value liquid assets. However, transferring closely held businesses, real estate or art often provides the best opportunities for valuations that allow the donor to take advantage of common discount techniques and also allow liquid assets to be earmarked for living expenses.

It is important that the gift instrument clearly articulates your specific intent.

The best way to deal with this dilemma is to use the “defined value” or “formula” gift approach, which allows the taxpayer to maximize usage of the available exemption while providing safeguards against revaluation. Formulas have been commonplace in estate planning documents for as long as there has been an estate tax exemption; for example, to calculate the proper funding of marital and credit shelter trusts. Historically, courts placed strict limitations on the formula approach for gifting that limited its utility. That started changing about 10 years ago, when a series of court cases upheld the use of defined value clauses and laid a framework for their successful use. It’s important to note that, while this approach has become more commonplace, it may still be subject to IRS scrutiny.

There are two primary approaches to formula gifting. The first, more

conservative approach is to direct any excess valuation to a beneficiary that would not trigger gift tax. The safest option would be a charitable beneficiary, as that strategy has been approved by the courts and is supported by the general public policy toward charitable giving. However, if donors don’t have the requisite charitable intent and a specific charity in mind, then this approach may generate less in benefits than simply paying the gift tax. In the absence of a specific charitable intent, another option would be to have the excess pass to a marital trust or an incomplete gift trust. That strategy has not been fully tested by the courts.

The second, more aggressive approach simply ties the transferred percentage of the gifted assets to the dollar value of such interest as finally determined for gift tax purposes. This is considered somewhat aggressive because the IRS chose not to acquiesce to the court decisions approving this structure. Still, it is the most efficient approach, as it does not require use of an alternate for any excess valuation, meaning that the assets go exactly where you want them to go, with no waste.

In either case, it is important that the gift instrument clearly articulates the specific intent and ties the value of the gift directly to the value “as finally determined for gift tax purposes.” An IRS revaluation for gift tax purposes does not automatically trigger an adjustment under the gift documents if that specific language is not included. It is also important that the characterization of the gift as representing a dollar value rather than a percentage of interest be carried through to the description of

There is a strong incentive to make gifts as close to possible to the maximum exemption amount.

the gift in the gift tax return so that there is no ambiguity.

In the current environment of historically high estate and gift tax exemptions combined with the constant threat of dramatic reductions thereto, there is strong incentive to make gifts as close as possible to the current maximum exemption amount. While cash and marketable securities can be gifted in definite dollar amounts, gifts of hard-to-value assets carry the risk that the IRS will seek to revalue those assets, potentially triggering a gift tax liability. In this regard, the “defined value” or “formula” gifting approach offers an interesting mechanism to maximize the use of the current exemption amount while providing a hedge against IRS valuation challenges.

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Now What? Time to Revisit Goals

By Jeff Maurer

Here's a paradox: In the two years in which we have wrestled with a global pandemic and its myriad related issues, the S&P 500 soared, rising 120% from the initial shutdown shock. Now, just as the virus may be downshifting to endemic, the market and world is becoming more volatile.

There are reasons for this contradiction, of course, notably the recent spike in inflation and the prospect of rising interest rates, which are addressed in this issue of *Independent Thinking* – and now a major geopolitical shock in eastern Europe. But over the years, we have learned a thing or two about change. That's why we work to construct flexible wealth plans and resilient portfolios intended to limit drawdowns and to produce reasonable, risk-adjusted returns, in *all* market conditions.

The first and most important step for investors is to acknowledge that these are challenging times and hang in there, come what may. Equity markets generally recover as the world returns to order, illustrated on page 23.

Second, and specifically to investing, let's deal with this change in the full context of our decade of remarkable gains. Thanks to a rare show of partisan

resolve and an accommodating Federal Reserve, the U.S. economy barely missed a beat throughout the pandemic, and investors enjoyed spectacular stock market growth. Those of us who are retired or working remotely and sheltering in our own homes saw our balance sheets improve dramatically. We spent less and saved more, while our assets, including the homes in which we sheltered, soared in value.

As we look ahead and deal with this market correction, along with a period of inflation and rising interest rates, it is important to take the time to reexamine goals and appetites for risk and liquidity. As I talk with our clients, some common themes emerge. Here's an example:

A couple, let's call them the Smiths, had \$20 million in liquid assets when they began working with us in our New York office in 2017, when the

Let's prepare for change after remarkable gains.

S&P 500 was less than 2,500. They were comfortable with some degree of risk but were willing to forfeit some prospect of return to protect their portfolio against substantial market drawdowns – an approach that kept them sanguine during the COVID-19 drawdown, illustrated on page 21. In keeping with their risk tolerance, we continued to actively rebalance their portfolio, trimming equity gains as tax-effectively as possible, while adding to defensive and illiquid asset allocations. They have spent about 5% of their portfolio a year, but the market has more than made up for that, and they now have \$25 million in investable assets even after the S&P 500 has fallen close to the 4,200 level in the current market drawdown.

120%

The cumulative total return growth of the S&P 500 March 23, 2020 to January 3, 2022

As we recently sat down with the Smiths to review their accounts and our investment outlook, we came to the joint realization that they can now afford to explore more options, even taking into account the current volatility. The overall growth in their assets over the past five years has made them confident about their own future, able to withstand and exploit market fluctuations. They are now considering using a portion of their unified gift and estate tax credit and giving a portion of

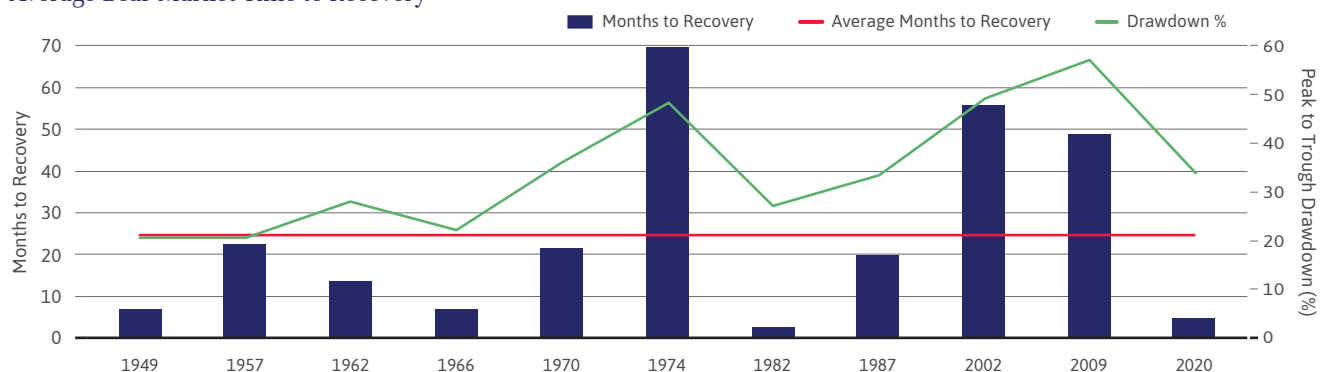
their still very appreciated securities to their children and grandchildren, letting the funds recover and grow for the next generation free of future estate tax. They can hedge their gifting through a Spousal Limited Access Trust, or SLAT, which would enable them to remove the assets from their taxable estate while allowing one spouse to have future access to the trust funds.

It's important to note that the Smiths are able to consider taking on a little

more illiquidity risk because they have over 25% of their portfolio in cash and defensive assets, enough to cover spending and capital calls for five years. Based on our capital market assumptions, we believe investing in illiquid growth opportunities can produce returns that exceed liquid growth equities by 3%-4% annually. The Smiths are also prepared to put some of their cash to work now, adding to quality shareholdings at more advantageous prices.

Hang In There

Average Bear Market Time to Recovery



Note: Recovery measured by time from trough to reaching the prior peak. Number of days includes weekends and holidays. Bear markets are defined as declines of 20% or more. Source: Ed Yardeni Bull & Bear Market Tables, March 22, 2020

Our Current Market Assumptions

Asset Returns*

Current 10-Year Expected Return	Assumptions (5 Years Prior)	Current Pre-Tax	After-Tax	After-Tax Real
Cash	2.4%	2.0%	1.2%	-1.1%
Defensive Assets	2.9%	2.3%	2.3%	0.0%
Credit Strategies	5.0%	3.8%	2.2%	0.0%
Diversified Market Strategies	5.4%	4.0%	2.5%	0.3%
Growth Assets	7.0%	6.1%	4.7%	2.4%
Illiquid Alternatives	11.5%	10.0%	7.2%	4.9%

Source: Evercore Wealth Management

Asset Allocation Summary*

Neutral Policy Allocation	Capital Preservation	Balanced	Capital Appreciation	Cap App 20% Illiquids
Cash	10.5%	9.0%	5.5%	5.5%
Defensive Assets	38.0%	23.0%	10.0%	10.0%
Credit Strategies	9.0%	8.0%	7.0%	7.0%
Diversified Market Strategies	0.0%	0.0%	0.0%	0.0%
Growth Assets	32.5%	50.0%	67.5%	57.5%
Illiquid Alternatives	10.0%	10.0%	10.0%	20.0%

Neutral Policy Returns & Drawdowns	Capital Preservation	Balanced	Capital Appreciation	Cap App 20% Illiquids
Pre-Tax Return	4.4%	5.1%	5.7%	6.1%
After-Tax Return	3.4%	3.9%	4.3%	4.6%
After-Tax Real Return	1.2%	1.6%	2.1%	2.3%
EWM Estimated Maximum Drawdown Estimate	-18%	-25%	-32%	-31%

Source: Evercore Wealth Management

A SLAT allows a married couple to hedge gifting.

Of course, the right plan and the right investment portfolio will be as unique as the family it serves. The Smiths are

considering taking on more risk. For others, sitting tight or taking less risk may be the appropriate solution at present. But I hope that all of us who are living through this extraordinary, paradoxical time will consider a thoughtful review now with trusted advisors.

Jeff Maurer is the Chairman of Evercore Wealth Management and Evercore Trust Company. He can be contacted at maurer@evercore.com.

Equity Declines Following Geopolitical Events Were Mild and Short-lived

Event (Date sell-off began)	Sell-off Duration (Trading Days)	Sell-off Size (%)	1 Month from Bottom
Invasion of Grenada (October 17, 1983)	15	-3.3	2.7
Bombing of Libya (April 22, 1986)	20	-3.7	3.2
First Gulf War (December 14, 1990)	24	-8.2	18.0
Kosovo Bombing (March 22, 1999)	3	-2.7	6.5
9/11 Attacks (September 11, 2001)	9	-11.7	10.7
Iraq War (March 24, 2003)	6	-4.7	8.6
Intervention in Libya (February 21, 2011)	18	-6.8	6.4
Annexation of Crimea (March 7, 2014)	6	-2.7	1.0
Intervention in Syria (September 19, 2014)	20	-8.7	7.2
Taliban Takeover of Kabul (September 7, 2021)	20	-5.7	7.1

Note: Data reflects MSCI All Country World from 1988 to present and MSCI World prior to February 1988. All returns reflect price changes in U.S. dollars. Source: MSCI Inc. and Thomson Reuters Datastream. MSCI data provided "as is" without any express or implied warranties. Cambridge Associates.

*The assumptions on the opposite page include projections or other forward-looking statements regarding future events, targets, intentions or expectations. Due to various risks and uncertainties, actual events or results may differ materially from those reflected or contemplated in such forward-looking statements. There is no guarantee that projected returns or risk assumptions will be realized or that an investment strategy will be successful. No representation, warranty or undertaking is made as to the reasonableness of the assumptions made herein or that all assumptions made herein have been stated. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product made reference to directly or indirectly in this document, will be profitable, equal any corresponding indicated performance level(s), or be suitable for your portfolio. The expected performance results do not reflect the impact that material economic and market factors may have on Evercore Wealth Management's future decision-making. Model performance results cannot completely account for the impact of financial risks associated with actual market conditions. These returns should not be considered as indicative of the skills of the investment adviser. A client's actual return will be reduced by the advisory fees and any other expenses which may be incurred in the management of an investment advisory account.

Estimates for each asset class are based on proprietary Evercore Wealth Management research and both historical return data and on various forward looking forecast from accepted government agencies and private forecasters. 10-year return forecast is based upon a balanced account asset allocation. Returns are based on the these assumptions. After-Tax assumptions: Cash and Credit Strategies taxed at ordinary income rate. Defensive Assets are exempt from taxes. Growth Assets taxed at long-term capital gains rate. Diversified Market Strategies is taxed at a weighted average rate of 25% capital gains and 75% ordinary income. Illiquid Assets is taxed at a weighted average rate of 25% ordinary income and 75% capital gains. After-tax real returns are net of inflation. The maximum drawdown metric refers to the worst-case scenarios for a trading period, usually between a peak and trough for the market, including the following events: +200bps parallel shift in U.S. Treasury curve, +300bps parallel shift in credit spreads (OAS), 40% decline in global equity markets and +300% increase in the VIX Index. Asset class allocations may change. Returns are based on performance of certain well-known and widely recognized indices. There is no representation that such index is an appropriate benchmark for such comparison. In addition, the Advisor's recommendations may differ significantly from the securities that comprise the indices. Please consult your Evercore Wealth Management advisor for additional information.

What Comes Next in the Russia-Ukraine Crisis?

We realize these are unsettling times and that you may be looking for informed perspectives on the events in eastern Europe. We arranged access for Evercore Wealth Management clients to a recent briefing by the Evercore research arm, Evercore ISI, on the repercussions of the Russian invasion of Ukraine, an event that was widely anticipated in the markets but has potentially serious geopolitical ramifications across Europe and around the world.

These briefings are normally confined to institutional clients of the firm, so if you would like to access the replay, please contact us.

Evercore ISI strategists Tobin Marcus and Krishna Guha interviewed guest Michael Allen of Beacon Global Strategies. Topics covered include:

- Scenarios for how the invasion might play out in the initial invasion and beyond, including kinetic attacks, cyberattacks, and more.
- The immediate military and sanctions response by the U.S. and Europe.
- What additional responses we might see over time, including further sanctions and support for Ukrainian insurgency.

- The tail risks in this conflict, including military escalation and collateral damage from sanctions.
- The geopolitical implications for the post-Cold War order, China's strategic ambitions, and more.

Please look for future invitations of this kind.

The United States and China: Repairing the “Most Consequential” Relationship



Evercore Wealth Management Partner and Portfolio Manager Brian Pollak interviewed David Firestein, President & CEO of the George H.W. Bush Foundation, on March 3, 2022, in a contemporary discussion of what the 41st President described

as the most consequential bilateral relationship in the world. Getting Sino-American relations back in sync is a key challenge for both countries, with significant implications for investors everywhere. A replay is available.

Upcoming *Independent Thinking* speaker series event planned include an in-depth exploration of wealth planning considerations and resources for families with member/s with special needs; a discussion

on reinvesting retirement; and focused panels on raising children in an affluent environment and on philanthropy. The firm will also host its annual women speaker event in May, *Women on What's Next*. Please contact your Wealth Advisor for further details on what promises to be an engaging afternoon.

Please look for invitations to these and other *Independent Thinking* events, both online and in person, reflecting the thought leadership of Evercore Wealth Management and Evercore Trust Company, and our experience in serving high net worth families, foundations, and endowments.

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