

## April 2016 Monthly Commentary

May 2, 2016

### Stock Market & Portfolio Performance

**April 2016:** Large-cap U.S. stocks and bonds posted modest gains for the month, while small-cap U.S. and international stocks posted more significant returns.

**Inside this issue:**

		<u>Apr 2016</u>	<u>YTD 2016</u>	<u>Description:</u>	
<b>Market &amp; Portfolio Performance</b>	<b>1</b>	Without Dividends:			
		S&P 500	0.2%	1.0%	500 Largest Public U.S. Companies
<b>Stock Market Update</b>	<b>2-3</b>	Russell 2000	1.5%	-0.4%	2000 of the smallest U.S. stocks
		MSCI EAFE	2.5%	-1.4%	international stock index
		U.S. Aggr Bond	0.4%	3.4%	index of U.S. bonds
<b>New Rules Affect Retirement Savings Advice— Requirement to be a Fiduciary</b>	<b>3</b>	With Dividends, after all fees:			
		MAM portfolios	1.0%	1.7%	non-very conservative MAM portfolios
<b>Life Insurance: When Do I Need It? How Much Do I Need? (by Lauree Murphy)</b>	<b>4-5</b>	MAM Conserv	1.0%	2.6%	portfolios with 50%+ bond allocation
<b>Our Services</b>	<b>6</b>				

*The returns showed above are unaudited. Past performance is not indicative of future results. Returns for McCarthy Asset Management Portfolios (“MAM Portfolios”) are net of management fees and transaction costs, and reflect the reinvestment of dividends. Results represent a composite of clients using a similar investment strategy, individual results will vary.*

*Returns for the indices are provided solely as a general indication of current market conditions. MAM Portfolios are not invested in a style substantially similar to any index. Indices do not reflect the deduction of management fees or transaction costs or the reinvestment of dividends. Performance for the indices would be lower if these costs were reflected.*

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After a very poor start to the year, the stock market rebounded and has now performed decently for the first four months of 2016. Concerns about the U.S. economy and/or global economies slipping into a recession have receded. Corporate earnings continue to be disappointing, but that is expected to change starting with the second quarter of 2016.

**GDP Growth:** On April 28<sup>th</sup>, the U.S. Commerce Department reported that the U.S. economy grew at a seasonally adjusted rate of 0.5% for the first quarter, continuing the uneven growth that has been a hallmark of the nearly seven-year economic expansion. This first quarter growth was the slowest in two years. Economists expect growth to modestly accelerate for the second quarter and continue for the remainder of the year.

**Corporate Earnings:** The 1<sup>st</sup> quarter of 2016 will be the fifth conservative quarter for earnings for the S&P 500 companies to decline relative to the prior year's quarter. This has been referred to as an "earnings recession." There are two primary reasons for the decline in earnings:

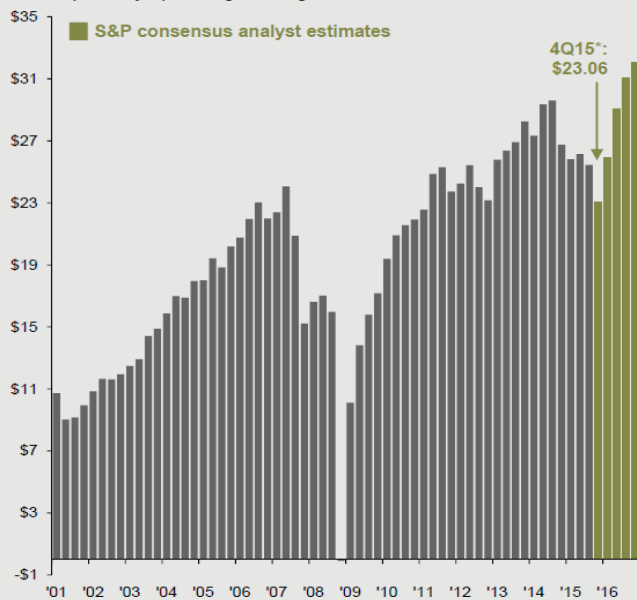
- **A sharp rise in the U.S. dollar:** As can be seen in the upper right on the chart below from J.P. Morgan, the U.S. dollar rose sharply in 2015. This has had a very negative effect on multi-national U.S. firms. Hopefully, the significant rise in the U.S. dollar is coming to an end. For the first quarter, the dollar suffered its worst quarterly performance since 2010, falling 4.2% as the Fed signaled it is likely to take a slower approach to raising short-term interest rates. For more information regarding my outlook for the U.S. dollar, please see our March 2016 Monthly Commentary for the article "Will the U.S. Dollar Continue to Rise?"
- **Dramatic drop in Energy Prices:** Oil prices have plummeted since the summer of 2015. As a result, companies in the energy sector have posted large losses due to the write-down in the value of their assets (see the lower right of the J.P. Morgan chart below). It appears that the price of oil bottomed in January of 2016 at \$26 a barrel. Since then, prices have risen over 70% closing recently at approximately \$45 a barrel.

## Corporate profits

GTM - U.S. | 7

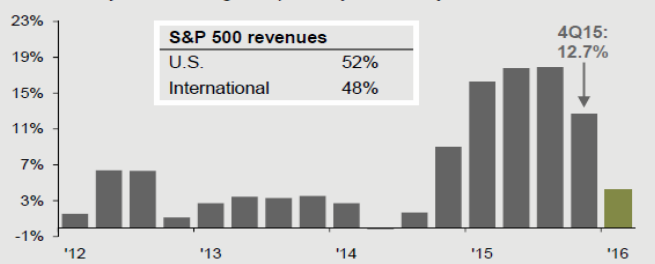
Equities

**S&P 500 earnings per share**  
Index quarterly operating earnings



**U.S. dollar**

Year-over-year % change\*\*, quarterly, USD major currencies index

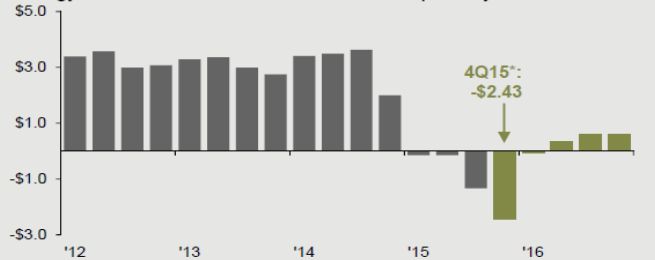


**S&P 500 revenues**

U.S.	52%
International	48%

**Energy sector earnings**

Energy sector contribution to S&P 500 EPS, quarterly



Source: Compustat, FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Top right) Federal Reserve, S&P 500 individual company 10k filings, S&P Index Alert.  
EPS levels are based on operating earnings per share. \*Earnings estimates are Standard & Poor's preliminary consensus analyst expectations. Past performance is not indicative of future returns. Currencies in the Trade Weighted U.S. Dollar Major Currencies Index are: British pound, euro, Swedish kroner, Australian dollar, Canadian dollar, Japanese yen and Swiss franc. 1Q16 dollar is a J.P. Morgan Asset Management estimate. \*\*Year-over-year change is calculated using the quarterly average for each period.  
Guide to the Markets - U.S. Data are as of March 31, 2016.

## Stock Market and Economic Update- Con't

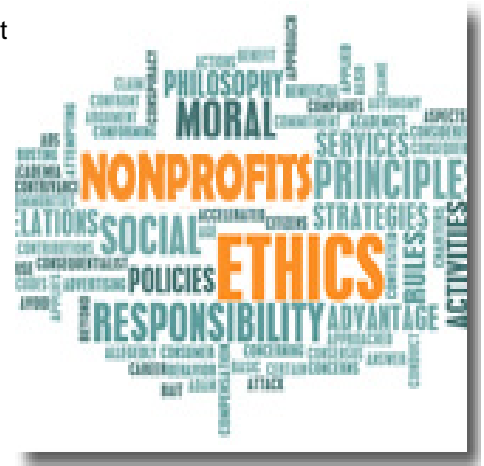
As can be seen from the left half of the chart above, analysts expect earnings for the S&P 500 companies to bounce back sharply, starting in the second quarter of 2016. This is simply due to the reduced impact of a rising U.S. dollar and falling energy prices. Of course, estimates can be revised downward if the U.S. dollar starts rising again or if energy prices fall to new lows.

**Stock Market Outlook:** I have been pleasantly surprised at the good performance of the stock market since early 2016. Assuming that the monthly employment reports continue to be positive, better economic growth returns in the current quarter, and corporate earnings snap back, I am cautiously optimistic in my stock market outlook. Nonetheless, now in its seventh year, this is an old bull market. Furthermore, I am concerned about the market impact of this year's Presidential race, which is likely to be quite contentious. It is possible that with the next portfolio repositioning (i.e. this summer), we may add a little more downside protection to portfolios.

## New Rules Affect Retirement Savings Advice— Requirement to be a Fiduciary

On April 6, 2016, the Department of Labor (DOL) adopted its "Conflict of Interest Rule on Retirement Investment Advice", a landmark rule that requires all professionals who give advice about 401(k) plans, IRAs, and other retirement plans to act in their clients best interests. This new rule, which has been six years in the making, goes into effect in April 2017.

Basically, the new rule requires anyone paid for retirement investment advice to act as a fiduciary. Currently, only professionals who are registered as "investment advisers" with the Securities and Exchange Commission (i.e. MAM, Inc.) or their state securities regulators, are held to the fiduciary standard in all dealings with clients. They charge a fee, generally as a percentage of assets they manage for the client. By law, a fiduciary must be impartial, seek diligently to avoid conflicts of interest, disclose any remaining conflicts, and always serve the best interests of clients.



Brokers, registered representatives, and insurance agents who sell investments, on the other hand, register with the Financial Industry Regulatory Authority (FINRA). Up until this new rule becomes effective, the investments they offer only have to be "suitable", a less rigorous standard that critics say has encouraged some advisers to charge excessive fees or favor investments that offer hidden commissions. One impact that I hope will result from this new rule will be for investors to no longer be asked to roll over their IRAs and 401(k)'s into a variable annuity, which I have always felt was an inappropriate investment vehicle for an IRA account.

Many investors are surprised to find out that most brokers are under no obligation to do what is best for clients. Repeated surveys have found that investors incorrectly believe that anyone offering investment advice must put a client's interests first. Instead, as long as they sell products that can pass muster as suitable, they are generally free to push offerings that earn them the highest fees, even if cheaper alternatives would be better for the investor.

Because this new "fiduciary" rule is being imposed by the Department of Labor, unfortunately, it will only apply to retirement accounts. Stockbrokers, registered representatives and insurance agents will still not be required to act in their clients' best interests for non-retirement accounts. Nor do the new regulations prevent these salespeople from calling themselves "financial advisers", even though they aren't registered as investment advisers with either the SEC or state security regulators. Nonetheless, this new DOL rule is a very important step to help protect investors' retirement accounts.

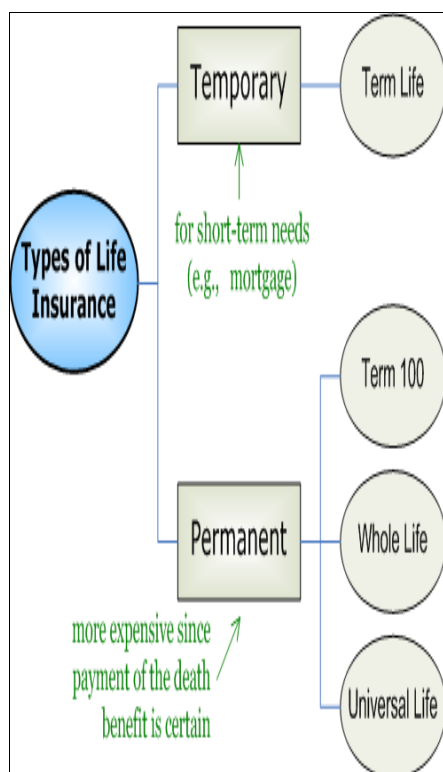
## Life Insurance: When Do I Need It? How Much Do I Need? (by Lauree Murphy)

The main purpose of life insurance is to replace income. If someone has a premature death and has a family to support, life insurance can bridge the gap. A non-working spouse may need insurance as well, particularly if they are taking care of family at home.

Typical events that trigger the need for life insurance include: getting married, taking on a mortgage, and having children. Once you have life insurance, a change in circumstances may trigger the need to increase the amount of coverage or add an additional policy. The attached article "Life Insurance for Your Stage of Life" talks about how you might handle life insurance as you go through life.



There are two main types of life insurance, term and whole life:



- **Term life insurance** is the type of life insurance we typically recommend, as it is pure insurance and is the most cost-effective option. It fits most situations where you are looking to provide for your family if you die young. With a term policy, you buy insurance for a specific term (15, 20, or 30 years for instance) and specific death benefit (\$500,000, \$1 million, \$2 million, etc.). If you die before the end of the term, the death benefit is paid to the policy beneficiary. The insurance has no cash value. If you outlive the term or cancel the policy, there is no payout. The amount you pay annually for premiums is fixed over the term. The younger you buy life insurance, the less expensive it is. Your health figures into the premium as well. Usually there will be a medical exam when you purchase life insurance.
- **Whole life insurance** policies combine death benefits with investing. The premiums are much higher because you are paying not only for insurance, but you are accumulating a cash benefit as well. Whole life insurance is permanent insurance, it doesn't have a term. It has a guaranteed death benefit, and the cash benefit grows over time. One situation where a whole life policy can be useful is to pay for estate taxes. For someone dying in 2016, estate taxes are only assessed if the estate is worth more than \$5.45 million for an individual or \$10.9 million for a couple. Other uses for whole life insurance include providing for a disabled child after you die, leaving a gift at death, or equaling out an inheritance where one beneficiary inherits a large asset like real estate or a business. Note that because the commission for selling a term insurance policy tends to be low, a life insurance agent may be motivated to sell a client a whole life policy, which pays a much higher commission to the selling agent.

If you have life insurance coverage through work, you might think you are set. Insurance offered as an employee benefit is usually pegged to your salary. A death benefit of 1x or 2x your salary is common. Unfortunately, replacing two years of salary is probably not going to leave your family financially secure. Many employer policies allow you to purchase additional insurance and have it deducted through payroll. Often this can be done without a health exam. Employers' policies tend to use group rates. This is helpful if you have a health issue, but if your health is good, you can usually get better rates outside the workplace. Life insurance bought through your employer may not be portable. The problem is if you change jobs, you may have to find new life insurance. Buying the same coverage might be more difficult if your health circumstances have changed. Being older could cost you more as well.

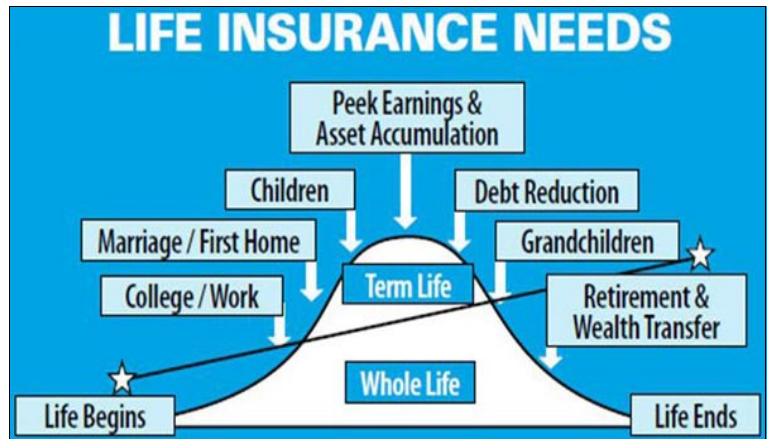
# Life Insurance: When Do I Need It? How Much Do I Need? (by Lauree Murphy)- Con't

**How much do you need?** Consider how much it would cost to pay off your debts including your mortgage, send your children to college, provide essential living expenses and fund other goals you have. Net these costs against the survivor's wages, savings, and existing life insurance policies.

Too much life insurance is better than too little. Statistically, women live longer than men, therefore rates are lower for women. Smokers pay a higher rate. Other health issues will bump up your premiums. Usually, once you retire and no longer have any dependents, you no longer have a need for life insurance. There are always exceptions. Special circumstances occur where you may need some insurance beyond your working years.

Some companies sell life insurance for children. Children don't have a responsibility to provide for anyone. If you want to save for your children, use another vehicle, not life insurance.

While we can help you estimate your need for life insurance, McCarthy Asset Management does not sell life insurance policies.



Sincerely,

*Stephen P McCarthy, CPA, CFP®*

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## Our Services

McCarthy Asset Management, Inc. (MAM) is an independent, privately owned Registered Investment Advisor firm. We provide clients with the peace of mind that comes from knowing professionals are managing their financial affairs. The services we offer include:

### Investment Management Services:

- MAM creates and manages customized investment portfolios based on each client's investment objectives, timeframe and risk tolerance.

### Financial Planning Services:

- The Net Worth Analysis (NWA) tracks the accumulation of Invested Assets for pre-retirees and the retention of Invested Assets for retirees. Updated annually.
- "Retirement Analysis" a comprehensive analysis of your retirement goals, which produces easy-to-read, interactive working plan, stored in the cloud. Updated as needed for life events.
- Social Security Planning is an analysis of the best strategy for when and how to start claiming Social Security benefits.

Tax Services: Clients have the option of utilizing the income tax services provided through the firm Stephen P. McCarthy, CPA. These services are offered at an hourly rate and may include:

- Tax Return Preparation
- Income Tax Projections
- Tax Minimization Ideas
- Tax Authority Representation

**Other Services:** MAM has retained outside experts, whose services are available at no cost to our clients:

- Long Term Care Planning– Allen Hamm of Superior LTC Planning Services, Inc.
- Medicare Advisory Program (MAP) - Eileen Hamm

## Reminders/Updates

Please let us know if there are any topics you would like to have us cover or any questions answered in a future Monthly Commentary.



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Registered Investment Advisor.