McCarthy Asset Management, Inc.
Personalized Wealth Management

February 2016 Monthly Commentary

March 1, 2016

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Stock Market & Portfolio Performance

February 2016: U.S. and international stocks posted modest losses for February. As with January, it would have been worse were it not for a late-month surge which allowed stocks to pare their losses. Meanwhile, bonds generated additional gains for the year.

	Feb 2016	YTD 2016	Description:
Without Dividends:			
S&P 500	-0.4%	-5.5%	500 Largest Public U.S. Companies
Russell 2000	-0.1%	-9.0%	2000 of the smallest U.S. stocks
MSCI EAFE	-2.1%	-9.2%	international stock index
U.S. Aggr Bond	0.7%	2.1%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	-0.3%	-4.5%	non-very conservative MAM portfolios
MAM Conserv	-0.1%	-1.9%	portfolios with 50%+ bond allocation

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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Stock Market and Economic Update

The first two months of 2016 have been challenging for investors:

- Concerns over global growth, falling oil prices and the risk of the U.S. economy slipping into a recession have caused global stocks to drop.

- Stock prices hit their 2016 low on February 11th, with the S & P 500 down 10.5% from the end of 2015.

- I sent out a stock market update via email on February 12th stating two key factors I am monitoring: Oil prices and the performance of the U.S. economy.

- Since the February 11th low, oil prices have stabilized and stocks rallied with the S&P 500 recovering nearly 50% of its 2016 losses.

Despite the rebound over the last couple of weeks, I am still not fully confident that this is just a temporary market correction. The biggest unknown is whether the U.S. economy is headed for a recession, which would almost certainly be accompanied by a bear market. While I think recession fears are overblown, I am tracking a number of economic indicators that provide a good reading on the health of the U.S. economy. Generally, recent economic reports continue to be positive:

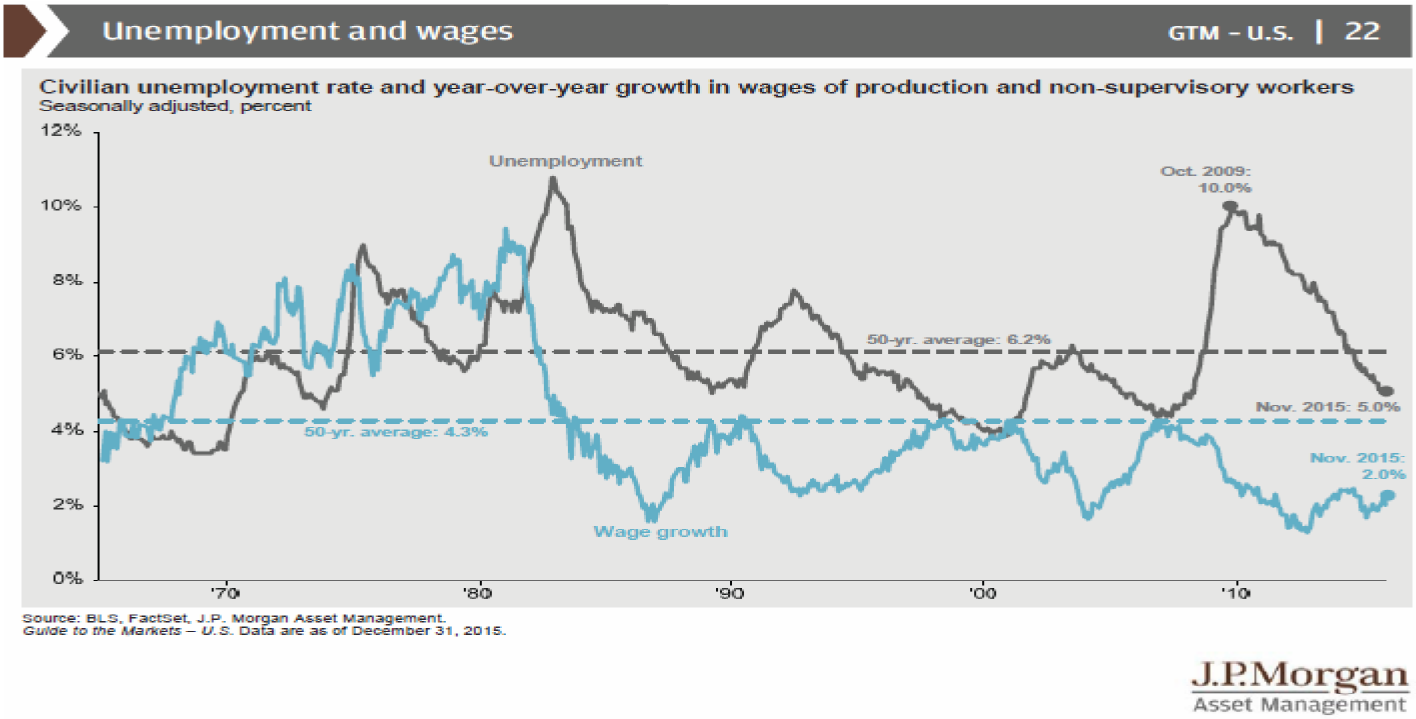
- **GDP Revised Upward:** Last week, 4th Quarter 2015 Gross Domestic Product (GDP) growth was revised to 1.0%, up from a previous estimate of 0.7%. While 1% is still indicative of a sluggish economy, economists currently project 1st quarter 2016 growth to increase to 2.0% or greater.

- **U.S. Consumer Spending Rose in January:** The economy got off to a good start this year as Americans boosted their spending in January at the fastest pace in eight months, and their incomes increased by the largest amount since last June. For the month, consumer spending rose 0.5% compared to December's 0.1% increase. Incomes also grew by 0.5%, up from 0.3% in December. Consumer spending accounts for two-thirds of the United States' economic activity, so the solid showing is likely to bolster expectations that consumers will fuel overall economic growth this quarter.

- **New Orders for Durable Goods:** Last week, the Commerce Department reported that new orders for durable goods—products designed to last at least three years—like dishwashers, cars and aircraft—rose a seasonally adjusted 4.9% in January from a month earlier, their largest monthly gain since last spring.

- **U.S. Employment Growth:** For January, the U.S. economy added 151,000 jobs and the unemployment rate dipped 0.1% to 4.9%. This is the first time the unemployment rate has been below 5% since February 2008. As can be seen on the chart below from J.P. Morgan, the U.S. economy has made tremendous progress on the job front since October of 2009, when unemployment peaked at 10.0%. Just in the last twelve months, the number of unemployed Americans has decreased by 1.1 million. The February jobs report will be released this Friday.

Stock Market and Economic Update- *Con't*



In summary: For the most part, the U.S. economy appears to remain on its slow-growth path. While there are still concerns about risks to global growth, as long as the U.S. economic growth continues, it is likely the current drop in the stock market will prove to be just a temporary correction.

IRA and Roth IRA Tax Strategies at Risk

Last month, President Obama released his fiscal 2017 Budget. Included were proposals that if enacted, would mean the end to several tax-saving strategies wealthy investors have been able to utilize. While it is highly unlikely that Obama's 2017 Budget will pass Congress, the inclusion of these proposals indicate that one or more of them may be adopted at some point in the future. Furthermore, the fact that they have been targeted for elimination suggests they are useful tax-saving techniques. As such, it is good to be aware of them. Here are the strategies at risk:

1. **Elimination of Back Door Roth IRA Contributions:** This is a very beneficial strategy that we utilize for some MAM clients who have earned income and don't have other IRA assets.

    - The big appeal of Roth IRAs is that they can grow tax-free and no tax is due on qualified withdrawals. Roth contributions are made with after-tax dollars and are subject to both annual dollar limits and income caps.

    - A high earner or spouse can currently sidestep the income limits on Roth contributions by making an after-tax contribution to a conventional IRA, and then soon after, converting it tax-free into their Roth (assuming there are no other IRA assets).

IRA and Roth IRA Tax Strategies at Risk– *Con't*

- For additional information about "Backdoor Roth IRA Contributions", here is a link to a white paper we wrote about them:

http://www.mamportfolios.com/files/Backdoor%20Roth%20IRA%20Contributions.pdf

2. **Introduction of Mandatory Distributions from Roth IRAs:** IRA account holders are required to start taking minimum distributions at age 70 ½. Currently, there are no required distributions for Roth IRA accounts as long as the account holder is alive. Furthermore, when the account holder dies, while the heirs will have minimum distribution requirements, they can spread those distributions over their lifespans. Obama's proposal would require people with Roth IRAs to take required minimum distributions starting at age 70 ½.

3. **Elimination of "Stretch" IRAs for Other Than Spouse Beneficiaries:** If you own a traditional 401(k) or IRA, your heirs must pay income tax on the withdrawals they take. But under current tax law, they can stretch out those withdrawals over their own lifespans, prolonging the tax advantages. The 2017 Budget Proposal would eliminate the stretch IRA for beneficiaries other than spouses by requiring non-spousal heirs to liquidate the IRAs and 401(k)s they inherit within five years.

Social Security- Will it Be There for Me?

One reason so many people start Social Security benefits at age 62 is because they are under the misconception that the funding for Social Security is going to run out. According to the 2015 OASDI Trustee Report, the Social Security Trust Fund has over $2.789 trillion dollars in assets. Under current obligations, this will last until 2033. After 2033, the fund can still cover 79% of its obligations, assuming no steps are taken to increase funding.

Between now and 2033, it is likely that Congress will make adjustments to strengthen the fund. The question becomes: Who will pay for the cost of these adjustments? Retirees don't want cuts in benefits or higher taxes on their benefits. Younger workers don't want to wait longer to start collecting benefits, or have more withheld from their paychecks. It's a balancing act to solve the problem. Here are some ideas that have been talked about:

Benefit Reductions:

- **Gradually Increase Full Retirement Age-** Currently, full retirement age, depending on the year you were born, ranges between 66 and 67. One proposal is to gradually increase it to age 69 or 70.

- **Reduce Cost of Living Adjustments (COLA)-** Annual cost of living adjustments are pegged to the Consumer Price Index. Although reducing the adjustment would help stretch the fund, retirees whose main source of income is Social Security would suffer a reduced standard of living.

- **Reduce Benefits for Future Retirees-** Retirees currently collecting benefits would be unaffected. Instead, the payout to those retiring in the future would be reduced.

Social Security- Will it Be There for Me?– Con't

- **Means Testing-** Those retirees with higher incomes would receive lower benefits. Means testing could take just income into account or it could include assets as well.

Revenue Increases:

- **Subject Higher Wages to Social Security Payroll Tax-** Currently, the maximum annual wage/self-employment income subject to Social Security tax is $118,500 (adjusted annually). Once your earned income exceeds this level, there are no additional Social Security withholdings for the remainder of the year.

There are several alternatives for increasing the earnings subject to tax:

1. All earnings could be burdened with Social Security tax with no annual cap and no additional benefits earned for those who pay more.

2. All earnings could be burdened with Social Security tax and those who pay in more get additional benefits.

3. The annual maximum subject to tax could be increased to a new limit, in which benefits are increased for those who pay in more.

- **Raise the Payroll Tax Rate-** Currently, the employee pays in 6.2% of his/her pay to Social Security and the employer matches another 6.2%, up to the annual limit. If this were increased to 7.6%, it is estimated that the Social Security Fund would be funded for the next 75 years. Even a smaller increase to 6.6% solves 28% of the projected Social Security shortfall. The increase could be done gradually over time to allow workers to adjust.

- **Subject Benefits to Higher Taxes-** In retirement, half of Social Security income is taxed for federal purposes if your income exceeds $32,000 (for a married couple). Once your income reaches $44,000 (for a married couple), 85% of Social Security income is taxed. Adjustments here would be to increase the percentage taxed or lower the income threshold where taxation starts.

AMERICAN ACADEMY *of* ACTUARIES

What do you think? The American Academy of Actuaries has an informative exercise called the Social Security Game. Decide which proposals you prefer and then see the impact each has on solving the Social Security funding problem. It can be accessed at

http://socialsecuritygame.actuary.org/#make-your-choice-now

Sincerely,

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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

2015 Tax Returns: I want to remind those tax clients who have not yet provided us with their 2015 tax information to please do so as soon as possible. We have set a deadline of March 20th for receiving your tax packet if you want us to complete your returns on time. Thanks!

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