McCarthy Asset Management, Inc.

Personalized Wealth Management

January 2022 Monthly Commentary

Feb. 1, 2022

Inside this issue:

Stock Market & Portfolio Performance

January 2022: U.S. stocks got off to a rough start for the year with the news the Federal Reserve will be raising short-term rates and initiating quantitative tightening sooner than previously expected. Bonds also performed poorly as the rate on the 10-year treasury rose sharply.

	Jan 2022	FY 2021	Description:
Without Dividends:			
S&P 500	-5.2%	26.9%	500 Largest Public U.S. Companies
Russell 2000	-9.7%	13.7%	2000 of the smallest U.S. stocks
MSCI EAFE	-4.9%	8.8%	international stock index
U.S. Aggr Bond	-2.2%	-1.5%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	-4.6%	16.2%	non-very conservative MAM portfolios
MAM Consrv	-3.5%	8.6%	portfolios with 45%+ 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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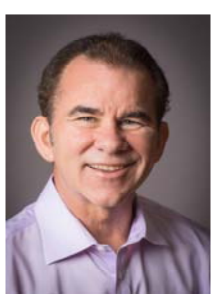

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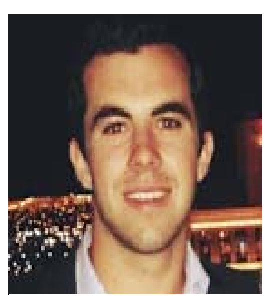

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A Stock Market Correction?

It's been a rough start to the year for the stock market with the S&P 500 falling 5.2% for the month of January. While stock prices may continue to fall in the short-run, we don't think we have entered a new bear market. This downturn was triggered by a shift in Federal Reserve monetary policy to fight inflation. While it is difficult to predict how long this market correction will last, we are encouraged that the economy is likely to continue to grow at a healthy pace, and that by historical standards, interest rates are expected to remain low for some time.

The Federal Reserve: The drop in stock prices started on January 5th when the minutes of the Federal Reserve's previous policy meeting were released. The minutes revealed central bankers were considering a shift toward quantitative tightening. This would entail the Fed gradually withdrawing liquidity from markets by shrinking the Fed's balance sheet of Treasuries and other securities. As recently as Thanksgiving, the Fed was not expected to implement quantitative tightening this year. Furthermore, it was not expected to start boosting the federal funds rate until mid-2022, with rate increases occurring two or three times by year-end. Now the Fed is expected to start raising rates in March with a total of four increases expected this year.

This move by the Fed to initiate quantitative tightening so soon would be a departure from the Fed's approach in the previous cycle. After the 2007-2009 financial crisis, the Fed waited two years after its first short-term interest rate hike to start allowing its balance sheet to shrink. However, there is greater urgency this time because the economy and job market are strong, and inflation has, at least temporarily, reached elevated levels.

It's important for investors to realize that short-term stock market corrections are a common occurrence. Furthermore, despite the Fed switching gears, monetary policy will continue to remain fairly accommodative. GDP growth is still expected to remain relatively strong for both 2022 and 2023, and inflation is expected to be more moderate by the end of this year. Therefore, we expect this stock market correction will likely be temporary.

What Do Rising Interest Rates Mean for Stock Investors?

Last month, U.S. Treasury bond yields climbed back to their pre-pandemic levels. Meanwhile, the S&P had its worst performance since the onset of the pandemic. If interest rates continue to climb, what is the likely impact on the stock market?

Effect of Interest Rate Increases on Stock Prices: Over the past 20 years, interest rates and stock prices have generally moved in the same direction. From the 1970s into the 1990s, though, when interest rates went up, stocks generally fell. Why the difference in performance? The primary factor here was whether the 10-year Treasury yield was above or below 5% at the time that rates were rising:

- When rates were below 5%, stock prices and bond yields tended to move in sync with each other. This was typically of the 1960s and the years since 2000.

- When rates were above 5%, stock prices and bond yields tended to move in opposite directions. This occurred during high inflation environment of the 1970-1990s.

Why do equities perform well when rates are climbing, but from a level below 5%? The reason is because stock prices move in tandem with the outlook for economic growth. Specifically, strong economic growth leads to strong corporate earnings growth. Periods of low but climbing rates indicate a strong economy. But when rates are above 5% and climbing, the Fed is taking action to cool the economy. The risk is these efforts can trigger a recession, which then lead to a down-turn in corporate earnings and stock prices.

Where are we today? At a current level of 1.8%, U.S. 10-year Treasury yields are well below 5%. As such, stocks should still perform ok. The unlikely risk, though, is runaway global inflation. If inflation does not stabilize in 2022, the subsequent increase in yields could turn negative for stocks and for the economic outlook.

What Do Rising Interest Rates Mean for Stock Investors– Con't

Which Stocks Perform Best with Rising Interest Rates and Higher Inflation? Historically, stocks have helped protect well-diversified portfolios from the ravages of inflation. But not all stocks have fared well in times of rising prices. History shows that stocks of companies in the technology sector and other growth stocks have tended to struggle when interest rates and inflation are rising. Conversely, value stocks and European stocks (which tend to be more value oriented), have performed relatively well in these environments. This would favor companies in industries such as finance and energy.

Risk to Growth and Technology Stocks: Why do growth and tech companies underperform in rising interest rate environments? This is because many investors value stocks based on the present value of the companies' future earnings. When interest rates rise, the future value is suppressed. It becomes less appealing to make high-priced bets on companies that may not be profitable for years. This could be particularly relevant in today's inflationary environment because growth stocks have been among the best performers in the S&P 500 over the past 10 years.

Interestingly, growth stocks often sputter when the economy has appeared to be at its strongest. For 2021, the leading economic indicators recorded their biggest year-over-year improvement since the late 1970s.

MAM Portfolios: A particular emphasis in MAM portfolios is on companies that pay an increasing dividend over time. Historically, these stocks outperform in a rising inflation environment. Furthermore, MAM portfolios are diversified among both growth and value stocks. But this is not a static allocation. If it appears that value and international equities are starting to outperform growth stocks, we may shift more of the portfolio allocation from growth to value and international stocks.

Why Your RMD Will Likely Decrease in 2022

The IRS recently released new life expectancy tables, which went into effect on January 1st, 2022. The updated tables reflect an increase in average life expectancy of almost two years. Included below is a portion of the Uniform Lifetime Table, which compares the pre-2022 table to the post-2021 table.

Pre-2022		Post-2021	
Age of IRA owner or retirement plan participant	Life expectancy (in years)	Age of IRA owner or retirement plan participant	Life expectancy (in years)
72	25.6	72	27.4
73	24.7	73	26.5
74	23.8	74	25.5
75	22.9	75	24.6
76	22.0	76	23.7
77	21.2	77	22.9
78	20.3	78	22.0
79	19.5	79	21.1
80	18.7	80	20.2

***Source: IRS Publication 590-B (https://www.irs.gov/pub/irs-pdf/p590b.pdf)**

Although these changes may not seem significant, these new tables will result in reduced RMDs for almost all individuals taking them. As life expectancies continue to increase, it is likely that we will continue to see the IRS update its life expectancy tables in the coming years.

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

ADV Part II: You were provided a copy of our ADV Part II when you became a MAM client. As a Registered Investment Advisor, we file this document with the Securities and Exchange Commission. Along with other items, it contains information regarding our fees and our educational backgrounds. Each year, the SEC requires us to offer clients the opportunity to receive a copy of our most recent ADV Part II. **Please let us know if you would like to receive a copy.**

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