

## June Monthly Commentary/Q2 2019 Quarterly Letter

July 1, 2019

### Stock Market & Portfolio Performance

**Second Quarter 2019:** U.S. and international stocks had another strong quarter, with large-cap stocks outperforming small-cap stocks. Meanwhile bonds performed well due to the Federal Reserve hinting at a possible reduction in interest rates.

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	2nd Qtr	YTD 2019	Description:
Without Dividends:			
S&P 500	3.9%	17.3%	500 Largest Public U.S. Companies
Russell 2000	1.8%	16.2%	2000 of the smallest U.S. stocks
MSCI EAFE	2.5%	11.8%	international stock index
U.S. Aggr Bond	3.1%	6.1%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	2.5%	11.8%	non-very conservative MAM portfolios
MAM Conserv	2.3%	9.4%	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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## Fed to Cut Interest Rates in 2019?



On June 19<sup>th</sup>, at the conclusion of its most recent two-day meeting, Federal Reserve officials announced they were leaving interest rates unchanged. However, they strongly suggested in a statement that they would cut them in the months ahead if the economic outlook, which has become clouded by uncertainty over trade policy, didn't improve. The last time the Fed reduced rates was in 2008 when the rates were dropped close to 0%. As the economy recovered from the Financial Crisis, the Fed started raising rates in 2015, and has raised them a total of nine times since then to the current level of 2.25% to 2.50%.

**When Might Interest Rates Be Cut?** The next Fed meeting is on July 30-31. For that meeting, investors in interest-rate futures markets have priced in at least a quarter-percentage reduction in the Fed's benchmark short-term rate. Before this meeting, the Fed will have time to evaluate whether U.S.-China trade tensions improve as a result of the late June G-20 meeting between President Trump and Xi Jinping. Furthermore, the Fed will receive important U.S. economic updates by then, including the initial estimate of U.S. Gross Domestic Product for the second quarter of 2019, and the June Jobs Report, which takes on added significance given the weak May Jobs Report. If it appears that trade tensions are easing and the economy is recovering from its recent slowdown, the Fed may decide to not reduce rates.

**Previous Rate Cuts:** While stock market investors may be hoping for lower rates to help prop up the economy, they should be careful what they wish for. The Fed has initiated a sequence of rate cuts four times in the past 25 years. In 2001 and 2007, a recession began within three months. In these cases, the stock market performed poorly after the rate cuts due to the weakening economy. On the other hand, in 1995 and 1998, the Fed lowered rates in time to prevent an economic slowdown from turning into a full-fledged downturn, and officials later reversed some of those cuts. In these two cases, the stock market performed well after the rate cut.

**MAM Comments:** Historically, the Fed has had to adjust its rate path within an economic expansion when global events, the economy, or markets signal rates are too high for the current environment. Therefore, the Fed deciding to enact and then hold just one or two cuts would probably be good news for stocks. On the other hand, the Fed initiating a more significant series of cuts would signal a high likelihood of an impending recession.

## Planning for Long-Term Care

An important consideration in planning for a financially-comfortable retirement is the potential need for long-term care. It is estimated that about half of people turning age 65 will require some type of long-term care in their lifetimes. "Long-term care" refers to a variety of services that help meet both the medical and non-medical needs of people with a chronic illness or disability who cannot care for themselves for long periods. Long-term care costs are not covered by Medicare or regular health insurance.



The Administration for Community Living, which is part of the Department of Health and Human Services, has published a good [primer](#) on long-term care. It includes figures about the likelihood of needing care and how much care the average American might require. According to a report updated in February of 2016, about half (52%) of Americans turning 65 today will require some type of long-term care in their lifetimes. Women will need 2.5 years of care, on average, while males will need an average of 1.5 years. On average, an American turning 65 today will incur \$138,000 in long-term care costs. Families will pay about half of the costs themselves out-of-pocket, with the rest covered by private insurance and public programs.

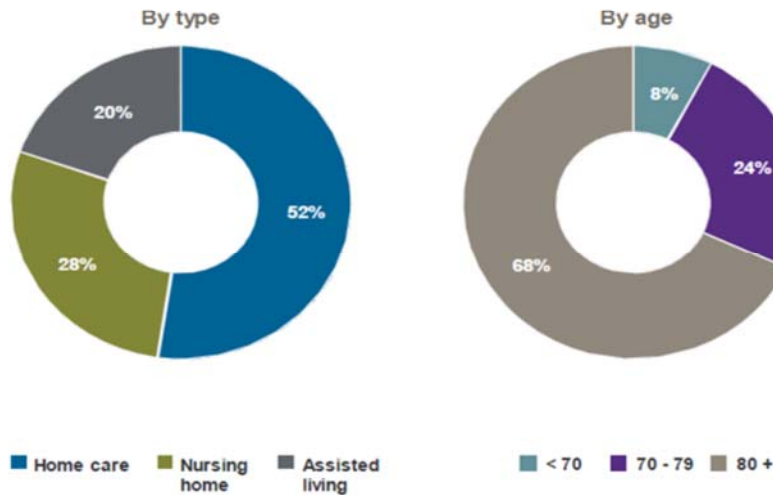
Many older Americans have done little to no planning for their own long-term-care needs. Part of the reason for this may be the misconception that Medicare will cover the cost of long-term care. In a [consumer sentiment survey](#) conducted by Genworth, two-thirds of respondents said they expect government programs to cover all or part of their long-term-care costs. While Medicaid is the largest single payer of long-term-care costs in the United States, it imposes strict income and asset limits on individuals who rely on it.

## Planning for Long-Term Care- Con't

The following charts from J.P. Morgan illustrate the most common type of care being provided (home care) in 2015, and the age when care was first provided (age 80 or later for 68% of those needing care):

### Long-term care considerations | 33

#### New long-term care insurance claims



#### LONG-TERM CARE: NOT JUST NURSING HOMES

Many individuals will need long-term care, which often starts with home care and may progress to assisted living or care in a nursing home.

While the majority had care needs at age 80 or older, nearly one-third experienced a care need before then.

Source (charts): American Long-Term Care Association for Long-Term Care Insurance, 2015 LTC Sourcebook.

Annualized historical inflation for nursing home (private room): 3.8%; assisted living (one-bedroom): 2.6%; home health aide: 2.5%. 5-year CAGR represents the compound annual growth rate based on Genworth Cost of Care Survey. Source for cost of care inflation information: Genworth 2017 Cost of Care Survey, conducted by CareScout®, June 2017. © 2017 Genworth Financial, Inc. All rights reserved. Methodology document for inflation information: [https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/cost-of-care/131168\\_081417.pdf](https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/cost-of-care/131168_081417.pdf)

**J.P.Morgan**  
Asset Management

**Estimating the Cost of Long-Term Care:** [Genworth's annual Cost of Care survey](#) enables you to focus on the community where you are likely to receive care. The data varies about average duration of care, but most of the statistics cover a range of 2.0 to 2.5 years.

Most people would prefer to receive care in their homes. Hiring in-home care may be cheaper than receiving care in a facility. However, it's important to remember that other household expenses, such as housing and food-related costs, would continue with in-home care, whereas they would be included in the cost of care received in a facility.

**Assess Your Available Resources:** The Retirement Analysis that we prepare for clients can help gauge whether you will have sufficient resources to cover long-term care costs. Typically, we run the Retirement Analysis to age 95. If and when long-term care is needed, a good portion of "retirement living expenses" and some portion of healthcare expenses can be allocated toward long-term care costs.

**Long-Term Care Insurance:** Long-term care insurance can be an important way to cover part or all of long-term care costs. These policies aren't cheap, though, and insurance companies have been raising premiums dramatically the last few years. One way to determine who is a good candidate to purchase long-term care insurance is based on the level of investable assets:

- Those with sufficient assets (perhaps \$3 million or more in invested assets) may be able to forego taking out a policy and self-insure the risk.
- People with limited assets shouldn't purchase long-term-care coverage if the premiums are not affordable. If they incur a lengthy need for long-term care, they are likely to deplete their assets and then have Medicaid cover the cost.
- Many people fall somewhere in the middle. They should be able to spend a certain amount of their personal savings on long-term care, but could also benefit from a more limited policy to cover the remainder.

If you decide to buy a policy, doing so while you are still in your early 60's will make it more affordable. In addition, buying while still in good health has become more important as insurers have tightened underwriting standards.

**Traditional or Hybrid Policy?** If you decide to purchase long-term care insurance, should you purchase a traditional (or "stand-alone") long-term care policy or a "hybrid" policy, which combines life insurance with a long-term care benefits rider? In recent years, hybrid policies have become popular with consumers. I have asked Allen Hamm to write an article for a future MAM Monthly Commentary comparing traditional and hybrid policies.

**Services of Allen Hamm of Superior Long-Term Care:** As many of you know, we pay an annual retainer to Allen Hamm of Superior Long-Term Care for Allen to create a Long-Term Care Plan for MAM clients who are interested. The Plan addresses how the client plans to cover long-term care costs from the four possible ways:

- Family members providing the care.
- Self-funding the costs out of assets.
- Government coverage via Medicaid (which entails first depleting your assets).
- Long-term care insurance.

As part of this process, Allen does offer long-term care insurance for those whom it makes sense to purchase insurance to cover part or all of the potential long-term care costs. In addition, if you have the opportunity to purchase long-term care insurance through work, he can evaluate whether that would be your best option. If you have not already done so, please let us know if you would like for us to introduce you to Allen.

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## PIMCO's Annual Secular Forum– Three to Five Year Outlook



PIMCO is one of the world's premier fixed income investment managers. Launched in 1971 in Newport Beach, PIMCO today has offices around the globe with 2,600 professionals. In early May, PIMCO's global team of investment professionals met for the Company's 38<sup>th</sup> annual Secular Forum to discuss economic events that may unfold in the next three to five years. The Forum included input from invited speakers, (including former Fed chair Janet Yellen) as well as its Global Advisory Board (which includes former Fed chair Ben Bernanke). This year the focus was on several key secular drivers that have the potential to significantly disrupt the global economy, financial markets, and investor's portfolios over the next three to five years. Here is a summary of the more important conclusions from the Forum:

1. *Over the next three to five years, they expect lackluster economic growth and persistently low inflation in the developed world ("advanced economies").* With the U.S. unemployment rate near historical lows, they also expect a moderate acceleration of wage gains in the U.S.
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## PIMCO's Annual Secular Forum– Three to Five Year Outlook– Con't

2. *Their most likely scenario (“secular baseline”) includes a relatively shallow recession followed by a sluggish recovery in the advanced economies within the next three to five years. Deep recessions are usually caused by a combination of major economic and/or financial imbalances and aggressive monetary tightening. Although not impossible, none of these significant risks look very likely in the next several years.*
3. *Potential causes of the next recession in the developed world include an escalating trade war, a geopolitical shock, a significant increase in policy and political uncertainty, a spontaneous sharp correction in asset prices, or a sudden downturn in China.*
4. *With inflation likely to remain below target throughout most of the world, they expect the major central banks to keep policy rates relatively low for most of the next three to five years with room to adjust them preemptively when downside growth or inflation risks materialize.*
5. *Geopolitics and trade policy are likely to remain a source of volatility for economies and markets over the next three to five years.*
6. *China’s economic growth is poised to slow over the secular horizon.*
7. *Their economic outlook for emerging markets is relatively positive, although potential shocks to global trade and domestic populism pose risks for the secular outlook.*

**MAM Comments:** Each year, we find the insights from PIMCO’s Secular Forum to be valuable. Prior Forums have coined terms that have become common language among financial professionals including the “New Normal” (conceived by PIMCO in 2009) and the “New Neutral” (coined by PIMCO in 2014) to reflect a low level of interest rates due to the U.S. economy’s lackluster growth combined with low inflation. PIMCO’s current secular outlook for lackluster economic growth, low interest rates and persistently low inflation is consistent with our outlook for relatively modest stock market returns over the next three to five years.

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

*Are you on course for a financially-comfortable retirement? A **Retirement Analysis** can be very helpful in answering that. Please let us know if you would like to have us prepare one for you.*



Discover the difference with a  
Registered Investment Advisor.