McCarthy Asset Management, Inc.

Registered Investment Advisor

February 1, 2007

Monthly Investment Commentary- January 2007

Stock Market Performance for January: The stock market got off to a strong start for the New Year—unadjusted for dividends, the S & P 500 rose 1.4%, the NASDAQ climbed 2.0%, and the Russell 2000 rose 1.5%. REITs rose strongly, foreign stocks rose modestly, while bonds and commodities fell.

MAM Performance: For the month, MAM portfolios under performed the S & P 500, with a composite return of 0.8% (after all fees), versus a rise of 1.5% for the Vanguard Index 500 fund (symbol VFINX) with dividends reinvested.

The five best performing MAM investments for January were Cohen & Steers REIT (rise of 9.2%), Marsico Focus (4.3%), American AMCAP (2.6%), Oakmark Fund/Select (2.3%), and Artisan International Small Cap (2.3%).

The five worst performing MAM investments for January were Allied Capital (down 11.7%), PIMCO Developing Local (bonds) (down 1.0%), PIMCO Commodity (down 0.5%), Hussman Strategic Growth (down 0.4%), and Nuveen High Yield Muni (drop of 0.3%).

Approximately half of the under performance of MAM portfolios relative to the S & P 500 was due to Allied Capital stock, which is discussed below. The remainder was due to the impact of bonds, which fell for the quarter, and international equities which rose less than U.S. stocks due to the rise in the U.S. dollar.

Price Drop in Allied Capital: Allied Capital is the only individual stock that has been purchased in MAM portfolios. I am leery of investing in individual stocks because I prefer the diversification offered by mutual funds and exchanged traded funds. Allied Capital is a unique company that has provided outstanding performance for over 45 years. It is the largest business development company in the U.S., meaning that it makes loans and equity investments in more than 100 private companies. This allows MAM portfolios to diversify into private equity in a cost-effective, liquid manner. Alternatively, private equity investments can be made through hedge funds and limited partnerships. I do not like investing in private equity through such vehicles due to high management fees, tax complexities (K-1 tax reporting) and lack of liquidity.

Allied Capital has been the target of hedge fund manager David Einhorn, who has shorted the stock since 2002. This means that his hedge fund sold Allied Capital stock that it did not own. As a result, Einhorn's hedge fund will profit if the price of Allied Capital stock falls. Recently, Einhorn has been provided ammunition in his attacks on Allied as one of its portfolio companies, Business Loan Express (BLX), has had an ex-employee indicted in making falsified loans that were guaranteed by the Small Business Administration. The employee was fired last fall. BLX currently represented 6.2% of Allied Capitals total assets as of 9/30/06.

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While I do not negate the seriousness of the alleged fraud conducted by BLX's ex-employee, I feel that the 12% drop in the stock price was an over reaction. David Einhorn's continued actions against Allied (in January he filed a lawsuit against Allied) have undoubtedly had a significant impact on the stock price. In due course, I am confident that the price of Allied's stock will recover. In the meantime, Allied's quarterly dividend (which is currently providing nearly a 9% annual yield) will provide a good return. Allied has consistently paid an increasing dividend since 1963. For those of you who would like additional information on the situation, I can email you a recent article from the Motley Fool which discusses Einhorn's actions and asserts that the recent price drop is a buying opportunity.

Economy- Surprising Strength in 4th Quarter: On January 31st, the Commerce Department released its initial Gross Domestic Product (GDP) report for the fourth quarter of 2006, showing that the U.S. economy grew at a 3.5% annual rate. This was above expectations, and was up from the 2.0% rate for the third quarter of 2006. The surprising strength was due to consumer spending offsetting a sharp drop in housing. For all of 2006, the U.S. economy grew at an annual rate of 3.4%, up from 3.2% in 2005, and well above its 20-year average of 3.1%.

As expected, the Federal Reserve announced on January 31st that they voted to leave the federal funds rate at 5.25 percent, where it has been since last June. As a result of recent strong employment and other reports, many analysts have gone from forecasting that the Fed would cut rates possibly three times this year, to thinking that the most likely outcome is that the Fed will leave rates steady for a considerable period. And some are worried that there could be rate hikes in the second half of 2007 if inflation does not slow further. This was the reason for the weakness in bonds this past month.

Congratulations to Billy: This past month Billy Alhorn received the great news that he passed the rigorous exam for becoming a Certified Financial Planner. Among his many duties, Billy is able to sharpen his CFP skills as he works on the Net Worth Analysis for clients.

2006 Tax Reporting: For those of you who are tax clients, I want to remind you there is no need to fill out anything in the Tax Organizer related to your taxable Schwab account(s) managed by MAM. Schwab is sending us a copy of your Form 1099(s). In addition, for your mutual fund sales we have produced a gain/loss report that we will attach to your tax return.

For those of you who are not tax clients, in mid-January we mailed you the 2006 Realized Gains and Losses Report, along with instructions explaining how to reference and attach the report to your tax return. Be sure and provide this to your tax preparer, as having this information really simplifies preparation of your return.

Please call or email me if you have any questions or would like to discuss your portfolio(s).

Sincerely,

Stephen P. McCarthy, CPA, CFP