McCarthy Asset Management, Inc.

Registered Investment Advisor

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Monthly Investment Commentary- July 2012

Stock Market Performance for July: With the exception of small cap stocks, July was a pretty good month for stocks. Unadjusted for dividends, the S & P 500 rose 1.3%, NASDAQ climbed 0.2%, the Russell 2000 (a small company index) dropped 1.4%, and the international equity index MSCI EAFE rose 1.1%. Bonds, as represented by the Barclays U.S. Aggregate Index, rose 1.5% for the month.

MAM July Performance: MAM portfolios slightly under performed the S & P 500 for the month. Excluding the "very conservative" portfolios (which rose 1.2%), MAM portfolios rose 0.9% (after all fees), versus a rise of 1.4% for the Vanguard Index 500 fund (symbol VFINX) with dividends reinvested.

Year-To-Date Performance: For the first seven months of 2012, unadjusted for dividends, the S & P 500 rose 9.7%, the NASDAQ climbed 12.8%, the Russell 2000 rose 6.2%, and the international equity index MSCI EAFE inched up 1.8%. Bonds, as represented by the Barclays U.S. Aggregate Index, rose 3.8% for the year-to-date. Excluding the "very conservative" portfolios (which rose 5.3%), MAM portfolios rose 6.1% (after all fees), versus a rise of 10.9% for the Vanguard Index 500 fund (symbol VFINX) with dividends reinvested.

MAM Blog To Be Introduced

The latest project that Alexey Bulankov has been working on is the creation of a MAM Blog. We are introducing a MAM Blog (planned for later his month) in an effort to bring you even more timely and relevant communications. We will update it with entries such as:

- **Articles on Financial Planning** to give you actionable ideas to prepare for a secure retirement and for reaching your goals.
- **Answers to most frequently asked questions** which we hear from clients.
- **Spotlight on mutual funds and mutual fund managers** used in MAM portfolios to better acquaint you with the investments we select and our thought process.

Economic and Employment Growth Remains Weak

The U.S. economy slowed further in the second quarter as consumer spending weakened and businesses grew more cautious about hiring and investing. Last Friday the Commerce Department reported that growth in gross domestic product (GDP), the broadest measure of goods and services produced by the U.S. economy, slowed to 1.5% for the second quarter, down from the first quarter's 2% annual rate and the fourth quarter of 2011's 4.1% rate.

The biggest obstacle to a more robust recovery is a dearth of consumer spending, which accounts for two-thirds of demand in the economy. Spending rose 1.5% in the second quarter, lower than

2.4% in the first, reflecting weaker demand for cars and big-ticket items. A big reason for this is the stagnant labor market. Employers added fewer jobs in the second quarter than they have in any quarter since the labor market began recovering in 2010.

The 2nd quarter GDP report did have some good news. Construction of houses continued to boost growth, though not as much as in the first quarter. Despite Europe's problems and slowing economies elsewhere in the world, exports rose 5.3%. Cutbacks by federal, local and state governments continued to drag on the economy.

Slowest Economic Recovery Since World War II: Last Friday the Commerce Department also reported revised data that indicated the nation's economy has grown only 6.7% since the recession officially ended in mid-2009. This means that the worst U.S. recession since World War II also has the worst three-year recovery in the postwar period. The reason why the recovery has been so weak is that Americans have been deleveraging by paying down debt and rebuilding savings. This can be seen in the most recent GDP report which shows that the personal savings rate—savings as percentage of disposable personal income—rose to 4%. While this is good on an individual level (and I commend MAM clients that have participated in this deleveraging), it is not good for the economy because it depresses consumer spending.

The good news is that U.S. consumers are far along in this deleveraging process. Furthermore, according to a report issued today by Marketfield Asset Management, consumer spending may see a boost from the ongoing boom in refinance activity. I receive daily insightful economic updates from Marketfield. One of the many economic items they track is the MBA Refinance Index, which is updated weekly. Since early May, the Index has been in boom territory (4000+). This week's reading saw the index reach 5428, the highest level since April 2009. Marketfield concluded "…this would appear to be a genuine and sustained boom in refinancing, with homeowners locking in significantly lower mortgage rates (the 30-year GSE rate is currently 3.60%). This has important ramifications for general consumer spending later in 2012 since it suggest that additional funds currently being used for mortgage payments will become available for other discretionary expenditures as refinancing activity turns into issued loans."

Federal Reserve To Take No New Action For Now: Today the Federal Reserve completed its two-day policy meeting. Here are the results of the meeting:

- The Fed said the economy is losing strength and repeated a pledge to take further steps to stimulate growth if the job market doesn't show sustained improvement.

- The Fed said that strains in the global market pose a significant risk to the U.S. economy, the housing market is improving but remains depressed and inflation remains tame.

- For now, the Fed will not take further action to stimulate the economy.

- Policymakers also repeated their plan to hold short-term interest rates at record-low levels at least until 2014 (which is good news for the "very conservative" MAM portfolios which on a risk-adjusted basis (the risk of loss of principal exists), remain a compelling alternative to CDs, money market and savings accounts)).

No Additional Portfolio Adjustments Planned At This Time: Given the slowdown in the U.S. economy, I am pleased with downside protection provided by the current positioning of MAM portfolios. While the stock market has performed fairly well so far this year, I believe that built into the current level of stock prices is the expectation that the economy is experiencing a temporary "rough patch" and that growth in the U.S. economy and employment will improve as the year progresses. If this resumption in growth does not occur, stock prices could suffer. Furthermore, the European sovereign debt crisis won't be solved any time soon and I have concerns about the "Fiscal Cliff" (see next section).

Fiscal Cliff

As I discussed at length in the First Quarter 2012 MAM Letter ("Concern About 2012 Tax & Fiscal Policy Changes"), pending 2013 tax increases and spending cuts pose a serious risk to the U.S. economy. The scheduled tax increases and spending cuts are already in the law and would need to be changed to mitigate the economic impact (estimated to be a huge decrease of $500 billion or 3.5% of GDP). As I indicated in the letter, Congress probably won't address the projected tax increases or automatic spending cuts until after the November elections, giving it less than two months before the New Year for complex lame-duck negotiations.

Attached to this July Monthly Commentary is a succinct two-page summary of the "Fiscal Cliff".

Expanded Services Available From Allen Hamm (including Medicare Consultation)

We're always looking for ways to add more value to our relationship with you. We're excited to announce the availability of some new services pertaining to the issue of long-term care. As you know, since we are not specialists in this area, we have retained the services of Allen Hamm and his firm Superior Long-Term Care. Allen is the author of the book "**How to Plan For Long-Term Care**". We have complementary copies of his book in our office for any of you who would like a copy. Here is a list of Allen's services that are available to MAM clients free of charge (please let us know if you would like to have Allen assist you with any of these):

1. **Creation of a personalized Long-Term Care Plan**: See the "Long Term Care Planning" link on the left side of the MAM home page (www.mamportfolios.com) for a webinar explaining what the Plan entails.

2. **Policy Audit**: For LTC insurance you already own, Allen can conduct a "Policy Audit" of your coverage, including a comprehensive analysis of the details of the policy, identifying any "red flags" in the fine print. He'll also give his opinion of the appropriateness of the levels of coverage for your situation and an explanation of the insurance company's track record for paying claims.

3. **Assistance With LTC Claims**: A new service now available is to utilize Allen's 23 years of experience in having Allen assist you in filing any claims.

4. **Medicare Consultation**: One final service that is also new is that Allen is available to assist our clients who are approaching the age of Medicare eligibility. With this service, Allen will help you understand how Medicare works, when and how to apply, and whether or not you should own a Medicare Supplement (sometimes called Medigap) insurance policy, and if so, which Plan.

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

Sincerely,

Stephen P McCarthy, CPA, CFP®