McCarthy Asset Management, Inc.

Personalized Wealth Management

April 2023 Monthly Commentary

May 1, 2023

Inside this issue:

Stock Market & Portfolio Performance

April 2023: For the month, U.S. stocks were mixed with large U.S. stocks rising and small U.S. stocks falling. International stocks had another good month with the continued slide in the U.S. dollar. Bonds rose modestly as the rate on the 10-year Treasury declined slightly.

	Apr 2023	YTD 2023	Description:
Without Dividends:			
S&P 500	1.5%	8.6%	500 Largest Public U.S. Companies
Russell 2000	-1.8%	0.5%	2000 of the smallest U.S. stocks
MSCI EAFE	2.5%	10.3%	international stock index
U.S. Aggr Bond	0.6%	3.8%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	1.0%	5.0%	non-very conservative MAM portfolios
MAM Consrv	0.7%	3.5%	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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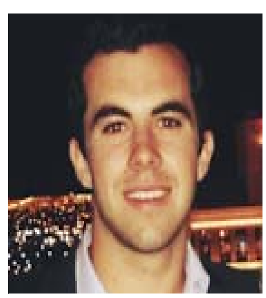

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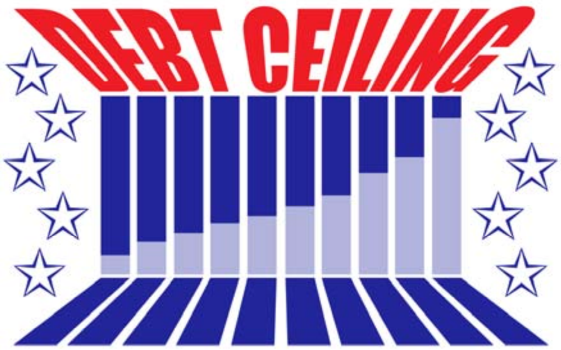
U.S. Debt Ceiling Drama



The United States reached its debt ceiling cap on January 19, 2023. This article discusses what that means and speculates on what Congress is likely to do to rectify the situation.

What it is: The debt ceiling is the cap Congress places on the total amount of debt the United States can accumulate. Raising the debt ceiling itself authorizes no additional spending—it merely allows debt to be issued to pay for spending that's already been passed. Since 1960, Congress has raised the debt ceiling 78 times. But over the past two decades, what was once a routine vote has become one of the most politically contentious issues that Congress faces. Congress last raised the cap to $31.4 trillion in December 2021.

By reaching the current cap on January 19th, the Treasury can no longer borrow additional funds to pay the nation's debts. In response, the Treasury Department began taking "extraordinary measures," a series of administrative steps to ensure the country does not default. These measures are expected to run out sometime this summer. By then, Congress must either increase or suspend the debt ceiling, or risk a potentially catastrophic default.

The Drama: Both parties have already staked out their positions. President Biden and Congressional Democrats have said they will only support a bill with a "clean" debt ceiling increase, with no strings attached. Republicans are demanding that a debt ceiling increase be paid with significant spending cuts to get the federal deficit under control.

The 2011 Scare: The stock and bond markets' concerns stem largely from painful recollections of the 2011 debt ceiling battle. Washington had the same political configuration then as now—a Democrat in the White House, Democrats controlling the Senate, and Republicans controlling the House. The two parties couldn't reach an agreement in the weeks leading up to the default date, rattling the markets. The S&P 500 fell 16% in five weeks, volatility spiked, and Standard & Poor's downgraded the U.S. credit rating for the first time in history. A deal was ultimately reached to avert a crisis, but only at the "11th hour."

This year, there is again no clear path to a solution. But leaders of both parties have been adamant that they won't let the country default. Markets will likely be carefully watching as negotiations pick up this spring.

What is the Actual Deadline? The real deadline of when the U.S. will no longer be able to pay all of its bills is hard to pin down. In part, it depends on the level of tax revenue the government collects. Currently, the nonpartisan Congressional Budget Office estimates for this to happen sometime between this July and September.

It is likely that a majority of House members would prefer to raise the debt ceiling without any uproar, as there is little political upside in plunging the U.S. economy into crisis. The challenge lies in the fact that House Republican leader Kevin McCarthy needs nearly unanimous support among House Republicans to pass the bill without support from Democrats. The slim margin of the Republican majority (222 to 212) means that McCarthy needs the support of the furthest right members of the Republican caucus, who are vociferously against raising the debt ceiling without steep spending cuts.

Discharge Petition: There is an alternative way for this to be resolved. House Democrats could join with moderate Republicans to force a vote on a different debt ceiling approach. The process, known as a "discharge petition," is a cumbersome and time-consuming one, but one that could offer an escape route if talks get bogged down. A simple majority is enough for the discharge petition to work, meaning only six Republicans would need to join the 212 Democrats. It is believed that House members and their staffs are already laying the groundwork for a discharge petition.

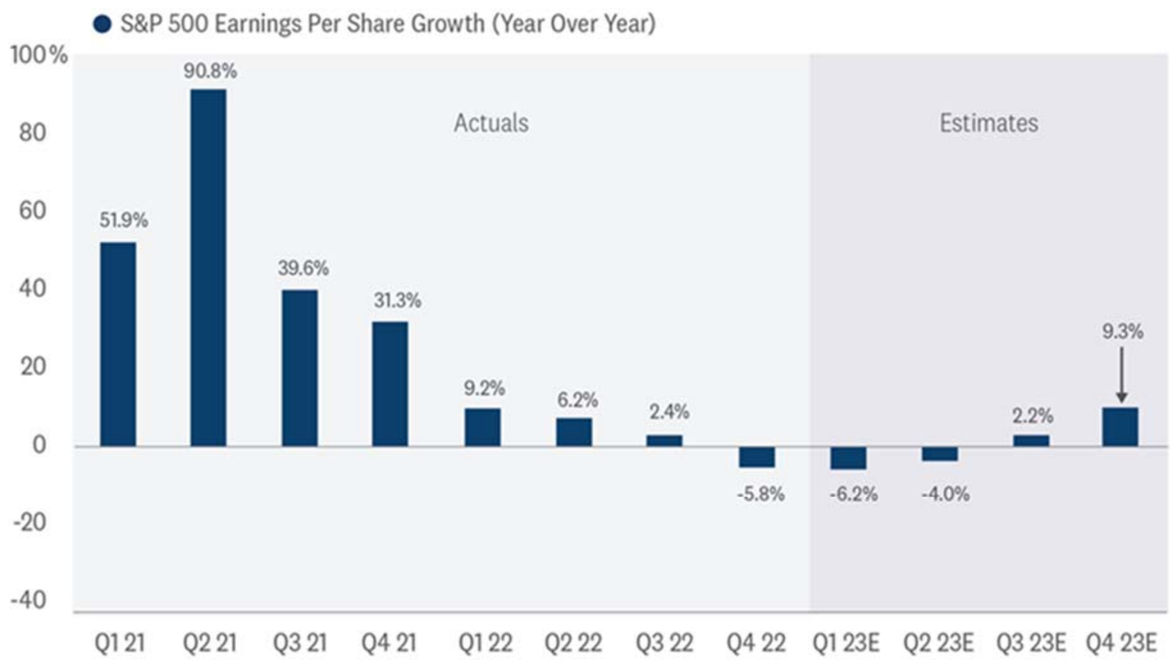
MAM Comments: The stock market historically has not reacted until the default deadline is close at hand. In 2011, the market downturn started about a month before the deadline, and accelerated as the deadline approached. Once again, the path to a resolution is uncertain. A default would be an unprecedented event that would likely have dramatic and unpredictable repercussions in the global financial markets. But it has never happened—Congress has always managed to find a way to reach an agreement. We believe this will once again be the case this time.

An Earnings Recession

After an amazing recovery from the earnings slump triggered by the outbreak of COVID, earnings per share for S&P 500 companies are expected to have fallen for the second consecutive quarter. After falling 5.8% in the fourth quarter of 2022, earnings are expected to drop around 6.2% from the prior year in the first quarter of 2023, according to data from FactSet. This would mark the steepest earnings decline since the second quarter of 2020, when the onset of the Covid-19 pandemic resulted in a 32% profit contraction. The news isn't expected to get much better in the second quarter, with FactSet noting that expectations for Q2 are earnings for the S&P 500 will drop another 4.0% from the prior year. As can be seen in the graph below from LPL Research and FactSet, earnings are expected to return to growth in the third and fourth quarters of this year.

1 **EARNINGS MALAISE TO CONTINUE**

Earnings May Trough In Q1 But Declines Likely To Continue For At Least Another Quarter



Source: LPL Research, FactSet 04/06/23
Estimates may not develop as predicted.

Why are earnings falling? Corporate America continues to face numerous headwinds, including rising interest rates, slow global economic growth, cost pressures from still-elevated (but easing) inflation, and some currency drag from a stronger U.S. dollar last quarter compared with the year-ago quarter.

It's not all bad news, though. Inflation pressures have continued to abate. The labor market has loosened a bit, limiting wage increases. The U.S. dollar has fallen about 10% since October 2022, which helps earnings from U.S.-based multinational companies. And while predictions for an economic recession have been commonplace, the U.S. economy very likely grew in the first quarter.

MAM Comments: Given the decline in earnings for the fourth quarter and the expected decline for the first quarter of this year, it is somewhat surprising that the stock market has performed relatively well for the first four months of 2023. Currently, the S&P 500 is trading at 18.2 times its expected earnings over the next 12 months, down from 21.6 at the start of 2022, but above the 10-year average of 17.5. This elevated level of stock market valuation, combined with the risk of the U.S. slipping into a recession by early next year, leaves us with a cautious outlook for stock prices at this time.

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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

Please let us know if there are any topics you would like to have us cover or any questions answered in a future Monthly Commentary.