McCarthy Asset Management, Inc.
Personalized Wealth Management

September 2024 Monthly Commentary

Oct. 1, 2024

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Stock Market & Portfolio Performance

3rd Qtr 2024: Despite heighten volatility, stocks posted strong gains for the quarter. Bonds also preformed very well due to a sharp drop in the yield on the 10-year Treasury bond.

	3rd Qtr	YTD 2024	Description:
Without Dividends:			
S&P 500	5.5%	20.8%	500 Largest Public U.S. Companies
Russell 2000	8.9%	10.0%	2000 of the smallest U.S. stocks
MSCI EAFE	6.7%	10.4%	international stock index
U.S. Aggr Bond	5.3%	4.6%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	5.0%	13.1%	non-very conservative MAM portfolios
MAM Consrv	4.5%	10.0%	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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Fed Cuts Rates by Half Percentage Point

On September 18th, the Federal Reserve voted for a 50-basis-point (bps) cut in the target federal funds rate, to a range of 4.75%-5.00%. The long-anticipated pivot follows an all-out fight against inflation that the central bank launched in March 2022.

This move was in line with general market expectations heading into the meeting. It's also an aggressive first step in what is expected to be a series of rate reductions. Based on the Fed's dot plot of rate projections, the Fed currently expects an additional 50 bps of cuts before the end of 2024. The rate could then decrease another 100 bps in 2025, with the potential for 50 bps of easing in 2026. If all these rate cuts were to occur, by 2026, the federal funds rate would fall to 2.75%-3.00%.

In its current outlook, the Fed believes a near-term recession is unlikely and expects inflation to continue falling toward its 2% target. The half-a-point decrease in rates improves the odds of a "soft landing' and may reduce the odds of a recession. A "soft landing" is the term for an economy with falling inflation, low unemployment and solid economic growth. Despite the recent uptick in the unemployment rate, Fed Chairman Powell was careful to note with the September 18th rate cut that the job market is "actually in solid condition. And our intention with our policy move today is to keep it there."

MAM Comments: While we were glad to see the Fed cut rates by 50 bps, there is a risk the rate cut could actually hurt the economy. This is because it could be a signal to consumers that the Fed is concerned a recession is coming. It's better if the purpose of the rate cut is because inflation is falling rather than the Fed being concerned that unemployment is rising. In this case, we have both falling inflation and rising unemployment.

What may also be important will be whether this will be a "fast easing cycle," defined as when rates are cut at least five times per year, or a "slow easing cycle," defined as less than five rate cuts per year. Historically, the stock market has performed better in slow easing cycles. This should be intuitive. Markets underperform in fast easing cycles because, in those instances, it is likely the Fed is combatting a recession or a financial crisis. At least so far, the Fed's current plans for further rate cuts point toward a slow easing cycle.

Time to Invest in Small Caps?

U.S. small-cap stocks, typically defined as those with a market capitalization of less than $2 billion, have historically offered higher returns than large caps over the long term. This phenomenon, known as the small-cap premium, is based on the idea that smaller companies are riskier, less efficient, and more prone to failure than larger ones, and therefore require a higher expected return to attract investor capital.

This long-term outperformance has been tracked by Jeremy Siegle. In his book "Stocks for the Long Run," from 1926 through 2021, small cap stocks outperformed large caps 11.99% to 10.35%. However, for at least the last ten years, this small cap premium has vanished, as large-cap companies have outperformed by a wide margin.

With inflation falling and the Federal Reserve having shifted to cutting interest rates, the headwinds that have beset small-cap stocks for the past few years may be starting to fade. Small-cap stocks are more sensitive to borrowing costs and economic conditions than large-cap companies, since they tend to have higher levels of debt than their larger peers and rely more on external financing to fund their operations. In addition, small-caps are often more domestically focused than large-caps and struggle when American consumers are pinched by inflation or a slowing economy.

Since August 1st, 2014, through August 1st, 2024, the Russell 2000 index of small stocks has returned 8.9% annually compared with returns of 15.0% on the S&P 500. So far this year, small-cap stocks continue to be outshined by their larger brethren. For the year through September 30th, the Russell 2000 small-cap index was up 10.0%, while the large-cap S&P 500 returned 20.8%.

Time to Invest in Small Caps?– Con't

Valuations favor small caps. As of September 16th, the forward 12-month price-to-earnings ratio for the S&P 500 Small Cap 600 (symbol "SML") was 16.7, compared to 23.4 for the S&P 500. This is despite analysts expecting better growth for small companies. Stocks on the small-cap index are expected to see a 20% rise in earnings in 2025 versus around 15% for the large-cap benchmark, according to FactSet data.

MAM Comments: We have been underweighting the small-cap allocation in portfolios for years. We don't expect to make any changes to this until we become more confident that small caps are once again shining. While falling interest rates should provide a boost to their performance, we are concerned that they will continue to underperform if the U.S. economy enters a recession next year. Historically, the best relative performance for small-caps has been as the U.S. economy recovers from a recession. We expect to be patient before increasing the small-cap stock exposure in portfolios.

Medicare Open Enrollment

The annual enrollment period ("Open Enrollment") for 2025 Medicare coverage will run from October 15, 2024, to December 7, 2024. During this time, you can make changes to various aspects of your coverage, such as switching from Original Medicare to Medicare Advantage, or vice versa.

As most of you know, we have retained the services of Eileen Hamm to help our clients with issues related to Medicare. Because we pay Eileen's firm a fee, this service is available at no charge to MAM clients. Quite a few clients have already utilized Eileen's services, either when they first became eligible for Medicare, or for those already enrolled, during the annual Open Enrollment. For those of you who have worked with Eileen in the past, she will be in contact to see if you would like to have her review your coverage.

Here is what Eileen can help you with during Open Enrollment:

- Reviewing your Medicare supplemental coverage to see if it has met your needs during the past year and evaluating other options as appropriate.
- Reviewing and making recommendations for any changes to your Part D prescription drug plan.

Per Eileen, "If you are on a Medigap-type supplemental plan and are happy with it, no change should be needed. However, the Part D prescription plans can change from one year to the next. Your insurer should mail you a notice about any changes, so pay close attention to the letter. Your premium may be going up next year, or the cost of your medications could increase, or some medications may no longer be covered under your plan. Even if you are currently happy with your Part D plan, it makes sense to evaluate your coverage every fall."

If you would like to have Eileen help you for the first time, let us know and we will send an introductory email. Alternatively, you can email her directly at eileen@superiorltc.com. Because Open Enrollment is Eileen's busy season, if you would like her to advise you, please reach out to her as soon as possible.

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 are able to utilize the income tax services provided through either the firm Stephen P. McCarthy, CPA or from the CPA firm of Lauren Be. 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 you would like us to show you how to access the information that is available on your MAM portal.