

## November 2019 Monthly Commentary

Dec. 2, 2019

### Stock Market & Portfolio Performance

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**November 2019:** U.S. stocks had another good month, with small-cap stocks outperforming large-cap stocks. International stocks rose modestly while bonds slipped slightly.

	Nov 2019	YTD 2019	Description:
Without Dividends:			
S&P 500	3.4%	25.3%	500 Largest Public U.S. Companies
Russell 2000	4.0%	20.5%	2000 of the smallest U.S. stocks
MSCI EAFE	1.0%	14.8%	international stock index
U.S. Aggr Bond	-0.5%	8.8%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	2.4%	16.1%	non-very conservative MAM portfolios
MAM Conserv	1.8%	12.6%	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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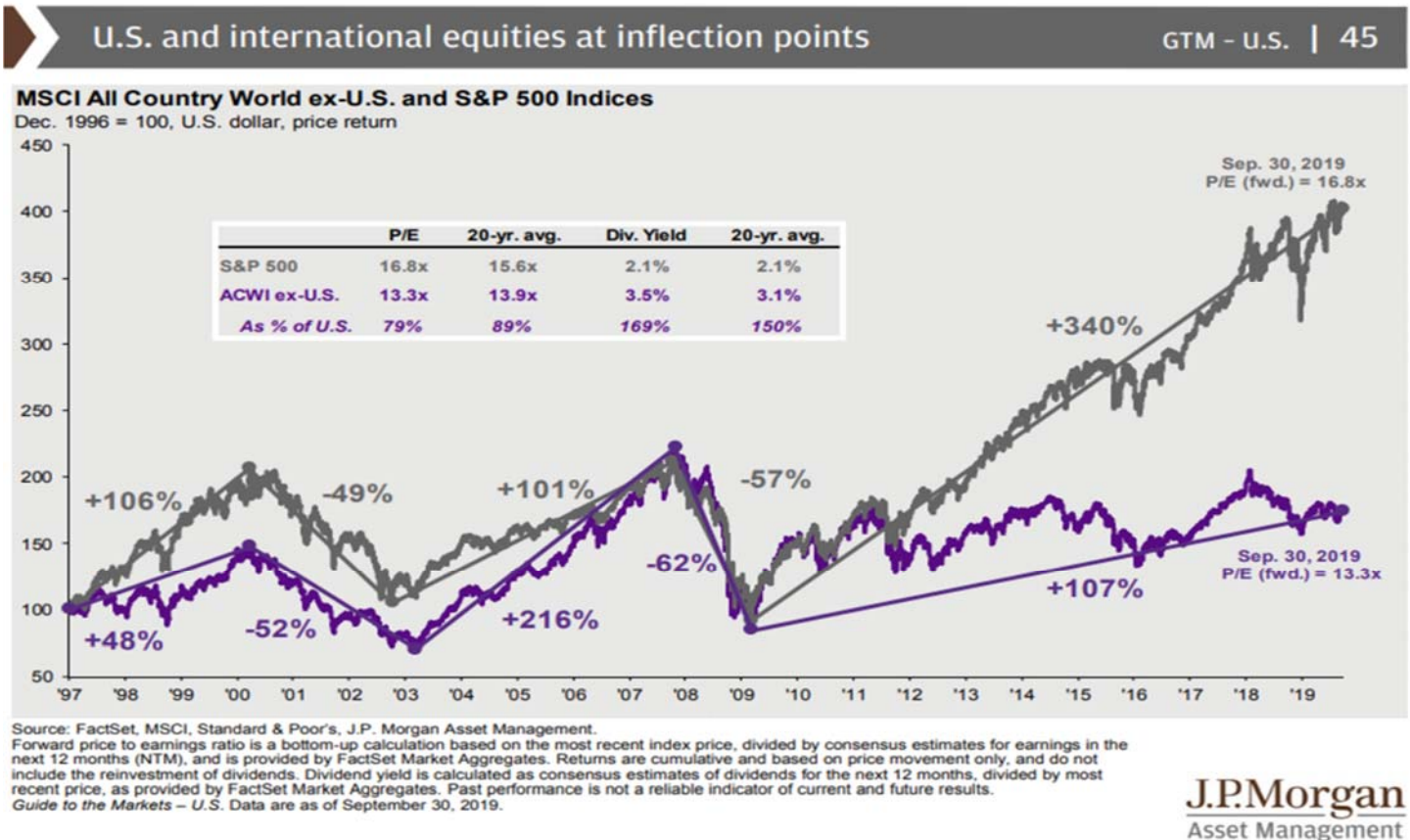
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## International Equities – Ready to Start Outperforming?

The rationale for including international equities in a portfolio is to increase diversification. Historically, a portfolio that includes an international stock allocation has less volatility, but comparable performance, to a U.S.-only stock portfolio. For the last ten years, though, this diversification has come with a price. Since the end of the financial crisis in 2009, international equities have significantly underperformed the S&P 500. As can be seen in the J.P. Morgan chart below, from March of 2009 through September 30, 2019, the S&P 500 returned 340%, while the MSCI All Country World ex-U.S. index returned only 107%.



Historically, there have always been cycles of international stocks underperforming followed by a period of outperforming. This is now the longest stretch of underperformance in over 40 years. At some point, international stocks will once again start outperforming U.S. stocks. The question is when? Here are some considerations:

- 1) **Performance of the U.S. Dollar:** A major reason why non-US stocks have lagged for the last few years has been a sharp rise in the U.S. dollar relative to the Euro and other international currencies. At some point, this rise is likely to end and start reversing.
- 2) **Relative Valuations:** International stocks are reasonably valued relative to U.S. stocks. As of 9/30/19, the forward price-earnings ratio for the MSCI All Country World ex-U.S. ("international index") was 13.3 times (compared to a 20-year average of 13.9 times) while the S&P 500 traded at 16.8 times (compared to a 20-year average of 15.6 times). So relative to their 20-year averages, international equities are undervalued and U.S. equities overvalued.
- 3) **Higher Dividend Yield:** As of 9/30/19, the index of international equities traded with a 3.5% dividend yield, relative to the S&P 500's 2.1% dividend yield.

## International Equities– Ready to Start Outperforming?- Con't



4) Emerging Markets: Emerging market equities are likely to outperform developed market equities (including U.S. equities) over the next ten to twenty years. This is because the emergence of a global middle class will drive economic growth in many of these emerging market countries as income levels steadily increase and the number of people living in poverty continues to fall. For instance, the percentage of the total population occupied by the middle class in India is projected to increase from 14% in 2018 to 79% in 2030, and for China from 34% to 72% during this timeframe.

**BCA Research's Outlook:** On November 15, 2019, BCA Research upgraded its view on international equities to favorable. In particular, they said:

- “Having underperformed for more than ten years, non-US stocks are set to gain the upper hand over their US peers.
- A reacceleration in global growth, a weaker US dollar, and favorable valuations should all support non-US stocks next year.
- Meanwhile, one of the greater drivers of US equity outperformance—the stellar returns of tech stocks—is likely to dissipate.
- Investors should overweight global equities relative to bonds, but start increasing their allocations to non-US stocks at the expense of US stocks.”

**MAM View:** MAM portfolios currently hold a relatively modest foreign and emerging market equity allocation of between 10% and 15%. We look forward to increasing this non-US stock allocation once we are confident that foreign stocks are once again outperforming US stocks. The earliest we would make this move would be sometime in 2020.

## Diminishing Financial Decision-Making Ability Comes with Aging By Lauree Murphy

Research has shown that financial decision-making abilities decline with age. A study completed in 2011 by Dr. Michael Finke and coauthors, Old Age and the Decline in Financial Literacy, reported financial literacy scores decline about 2% each year after age 60. The same study found confidence in financial decision-making abilities does not decline with age. Therefore, it makes sense that as we age, we are more susceptible to financial fraud or bad decision making. The elderly are easy prey for callers claiming to be from Social Security, the IRS, or numerous other schemes that exist. However, fraud is not the only problem. Other issues can include forgetting to pay bills or make tax payments, overspending, and purchasing financial products that are not appropriate for their circumstances.



This raises two questions. How do we protect our aging self from falling victim to schemes? How do we keep older loved ones out of trouble?

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# Diminishing Financial Decision-Making Ability Comes with Aging

## By Lauree Murpy- Con't

### **Starting the Conversation:**

Money is a taboo subject in many families. If your parents have kept financial matters private, it might be difficult to get them to open up. As a rule of thumb, if you are 40 years old or your parents are 70, it's time to communicate. Start by observing and gathering information. Talk with siblings and other family members as well. Get their observations. Pick a time of day to initiate the conversation. If your parents are more cognitive first thing in the morning, make the conversation early in the day. Holiday gatherings when family members are all together might be a good time to broach the subject. Use a story (see mine below), to get the conversation going. Let the message be that you care and are available to help. Don't be accusatory or aggressive. Find out where help is needed now or may be needed in the future. Make a plan for individual responsibilities. If money runs out in the future, what action will be taken? Will parents move in with someone? Will children chip in and provide support?

### **Points you can discuss with relatives and actions you can take now to set yourself up for the future:**

- Identify who you want to help you, when the time comes. Talk to that person and see if they are willing to step in. Give them a picture of where things stand.
- Consider a Durable Power of Attorney. It allows someone to act on your behalf as soon as the document is executed. This way you can give a trusted friend or child access to accounts while you are still competent and guide them on managing those accounts. If the person selected doesn't fit the bill, you have the ability to appoint someone else, as long as you are still mentally competent.
- Tell loved ones where your will, trust, and other important documents are located. For most MAM clients, we maintain a copy of the estate planning documents on their MAM portal.
- Make a list of financial professionals: lawyer, accountant, financial advisor, insurance agent. Include phone numbers and email addresses.
- Make a list of account numbers for saving accounts, investment accounts, credit cards, and utilities.
- Many utilities including PG&E, as well as other creditors, allow a third party to be notified if a bill goes past due. Activate this service. It will help alert loved ones before things get out of hand.
- Write a letter to your future self as a reminder of why you took these actions.

### **A Personal Story:**

One relative of mine in her 80's ran up credit card debts of \$40,000. Living on Social Security, she would never have the money to pay it back. Threatening letters and collection calls hounded her. Finally, she informed her immediate family. She was embarrassed. We thought she was sharp mentally. Her memory was good. She knew what was going on in the world. We were caught by surprise. After the mess was straightened out, her daughter started paying her bills. That way the family could monitor what was going on. Incidents like this are not uncommon. What we should have done differently was to get involved earlier. Even if you think everything is fine, it may not be. It may take some cajoling, but it's important to get a sense of where things stand and head off any problems.

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## Tax Planning— Solar Credits & Donor Advised Funds



With tax season fast approaching, tax planning comes to mind. This article discusses two ways that you can reduce your income tax bills.

**Solar Energy Credits:** There has been a multi-year boom in the installation of solar panels. The motivation for a homeowner to do so includes both a reduction in energy bills and greenhouse gas emissions. Furthermore, the federal government has provided generous tax credits to offset part of the cost of the purchase and installation of solar panels. Federal solar energy credits for both individual taxpayers and businesses are currently 30%, but are reduced to 26% in 2020, 22% in 2021, and 0% after that unless Congress passes an extender bill.

The credit available to individual taxpayers for solar energy property installed on their personal use property, such as a principal residence or vacation home, is the residential energy efficient property (REEP) credit. The credit available to business taxpayers is the nonresidential energy property credit. One of the key differences between the REEP credit and the nonresidential energy credit has to do with timing. All expenditures associated with the purchase and installation of personal use solar property are deemed paid when the project is completed. For example, if a taxpayer pays \$40,000 in 2019 to install solar panels on their home, but the project is not completed until 2020, then the taxpayer claims a 26% credit on their 2020 income tax return.

Note that no tax credit is available for the leasing of solar panels. Taxpayers must purchase the solar panels to claim the credit (no matter what the salesperson says!).

**Donor Advised Funds:** I have been a proponent of donor advised funds as a great planning tool for those who expect to make future charitable gifts. Here's a [link to an article](#) I wrote about donor advised funds in our November 2015 Monthly Commentary. A donor advised fund allows you to receive a tax deduction equal to the fair market value of a highly appreciated security you gift, while being able to delay the decision of which charity or charities to donate the proceeds to. No capital gain taxes are paid on the appreciation of the contributed security. The three biggest providers of these accounts are Fidelity Charitable, Schwab Charitable and Vanguard Charitable.

Personally, I have been very pleased with the use of the Schwab Charitable Donor Advised Fund account that Joanie and I set up in 2014. While there is no cost to establish a donor account, Schwab, and I believe both Fidelity and Vanguard, charge 0.60% annually on the assets held in their accounts. With Schwab, the minimum to establish an account is \$5,000, the minimum for additional contributions is \$500, and the minimum for distributions to a charity is \$50.

The 2018 Act provides an additional benefit for some taxpayers. Because the Tax Act limits the deduction for state income tax and property taxes to \$10,000, and raised the standard deduction, fewer taxpayers are now itemizing their personal deductions. Use of a donor advised fund provides the opportunity to “bunch” years of charitable contributions into one year to itemize that year, while maintaining the benefit of distributing the contributions over future 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

- 1) **Property Tax payments** are due December 10, 2019.
- 2) **Roth IRA Conversions:** Please contact us ASAP if you would like to discuss. The deadline for 2019 conversions is December 31, 2019.



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