

November 2021 Monthly Commentary

Dec. 1, 2021

Stock Market & Portfolio Performance

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November 2021: Stocks fell for the month, triggered by concerns over the Omicron coronavirus variant that was discovered late in the month. Bonds rose modestly as interest rates fell in response to the Omicron concerns.

	Nov 2021	YTD 2021	Description:
Without Dividends:			
S&P 500	-0.8%	21.6%	500 Largest Public U.S. Companies
Russell 2000	-4.3%	11.3%	2000 of the smallest U.S. stocks
MSCI EAFE	-4.8%	3.6%	international stock index
U.S. Aggr Bond	0.3%	-1.3%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	-1.8%	10.8%	non-very conservative MAM portfolios
MAM Conserv	-1.3%	6.1%	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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After extensive negotiations between progressive and centrist Democrats, on November 19th, the House of Representatives passed the \$2 trillion Build Back Better (BBB) Act. It now goes to the Senate, where lawmakers will use a special budget maneuver known as reconciliation to try to pass the legislation. The bill is expected to face changes as it needs the support of all 50 Democratic senators to pass. Likely changes to the bill include the issues of paid leave and immigration policy.



Among other provisions, the bill calls for creating a universal prekindergarten program, capping child-care costs for many families, negotiating lower prescription drug prices and expanding tax credits for reducing carbon emissions. In addition to expanding tax-enforcement efforts at the Internal Revenue Service, the legislation raises taxes on some corporations and very high-income Americans.

What is Not in The Proposed BBB: While subject to change in the Senate, the House's version of BBB has dropped:

- Increases in the individual income tax rate (except for top earners as indicated below).
- Increases in the capital gains rate.
- Increases in the corporate tax rate.
- Reduction in the estate and gift tax exclusion amount.
- Elimination of 1031 exchanges for high-income taxpayers.

What is in the Proposed BBB: Among the many provisions, the more significant ones include:

- For taxable years beginning in 2022, creating a new 5% tax on individual taxpayers with income in excess of \$10 million (\$5 million for married taxpayers filing separate) and \$200,000 for estates and trust. An additional 3% surcharge will also apply when a taxpayer's Adjusted Gross Income (AGI) reaches \$25 million (\$12.5 million for married filing separate) and \$500,000 for estates and trust.
- Increasing the state and local tax (SALT) itemized deduction from \$10,000 to \$80,000, retroactive to the beginning of 2021.
- Expanding the 3.8% net investment tax (NIIT) to include net income derived in a trade or business (Schedule C businesses, S corporation shareholders, partnerships, etc.) for taxpayers whose AGI is over \$400,000 for single filers, \$500,000 for married taxpayers filing jointly and \$250,000 for married taxpayers filing separate.
- Effectively eliminating Roth IRA conversions after December 31, 2021.
- For sales made after September 13, 2021, decreasing the 75% and 100% gain exclusion from qualified small business stock (QSBS) down to a 50% exclusion for taxpayers whose AGI is in excess of \$400,000.
- Restoring the solar credit for individual taxpayers back to 30% starting in 2022, up from 26% for 2021.
- Expanding new plug-in vehicle credits. However, these expansions are expected to also contain numerous limitations, including AGI limitations and manufacturer's suggested retail price (MSRP) limitations.

Possible Changes in the Senate's Version: There will likely be revisions made to BBB as the Senate takes up the measure this month.

- Some Senate Democrats have raised concerns that raising the SALT deduction is offering tax cuts for high-income households.
- Senator Joe Manchin has stated that the \$2 trillion size of the bill is too large and may insist on it being reduced. It is speculated that he might seek to remove the legislation pertaining to four weeks of paid leave.

MAM Comments: Year-end tax planning is particularly challenging this year given that we probably won't know until well into December if the BBB Act will pass, and if it does, what the final bill will look like. Specifically, raising the SALT limitation has implications on prepaying state income and property taxes by December 31, 2021. Additionally, 2021 could end up being the final year to do a Roth IRA conversion.

Infrastructure Bill



On November 15th, President Biden signed the \$1.2 trillion infrastructure bill into law. The bill, which had bipartisan support, will provide \$550 billion of new federal investments in America's infrastructure over five years. The spending will be used for improving everything from bridges and roads to the nation's broadband, water and energy systems. Experts say the money is sorely needed to ensure safe travel, as well as the efficient transport of goods across the country. Furthermore, economists generally agree that federal spending on infrastructure helps the country become more efficient because it affords workers greater mobility and improves the transportation of goods.

Proponents of the legislation claim it pays for itself through a multitude of measures and without raising taxes. But the Congressional Budget Office brushed aside several of those pay-for provisions, ultimately finding the package would add \$256 billion to the deficit over 10 years. Nonetheless, we feel this is government spending that needs to be done.

There are no significant tax changes for individuals or corporations in the infrastructure bill.

Inflation at a 31-Year High

Inflation in the U.S. hit a three-decade high in October, delivering widespread and sizable price increases to households on everything, from groceries to cars. This 31-year inflation high is due to persistent supply shortages and strong consumer demand. The Labor Department said the consumer-price index, which measures what consumers pay for goods and services, rose by 6.2% last month from a year ago. That was the fastest 12-month pace since 1990, and the fifth straight month of inflation above 5%.



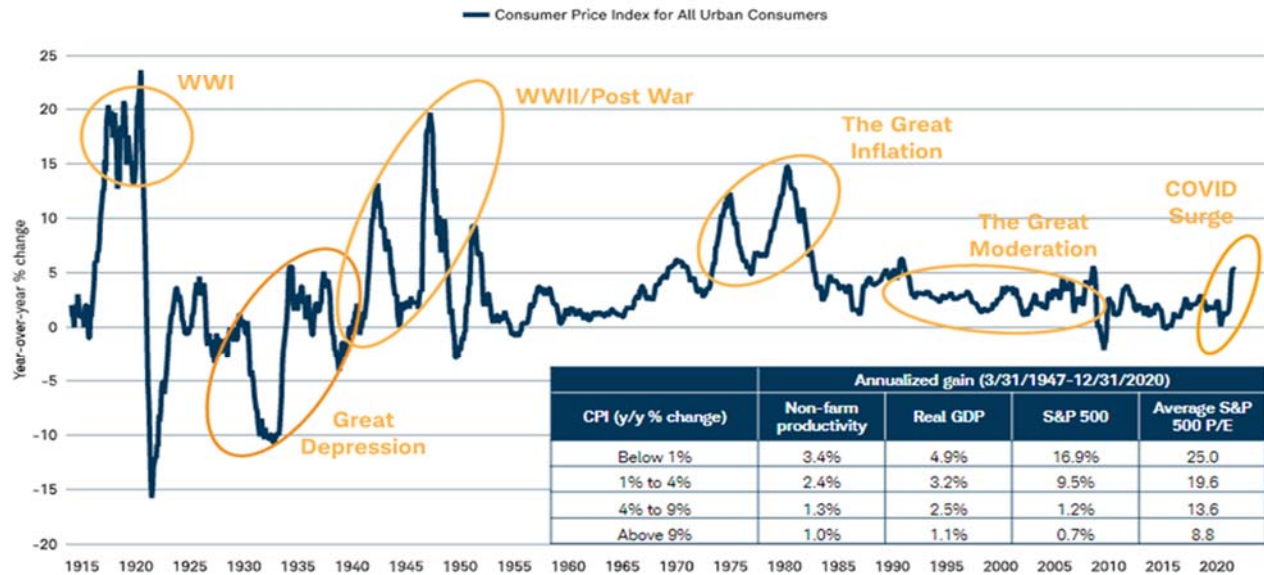
Federal Reserve officials looking to unwind easy-money policies that it imposed early in the pandemic are watching inflation measures to gauge whether the recent jump in prices will be temporary or longer lasting. One such factor is consumer expectations of future inflation, which can prove self-fulfilling, as households are more likely to demand higher wages and accept higher prices in anticipation of further price increases.

The information-packed chart below, from Charles Schwab & Co., shows how U.S. inflation has ranged since 1915. It labels the low-inflation environment from the late 1980s through 2019 “The Great Moderation” and the recent spike in inflation the “COVID Surge”. Also displayed is how the S&P 500 performed during various levels of inflation. As you can see, there is a direct correlation between higher inflation and lower stock market returns:

Quarterly Chartbook | Q4 2021

A long-term view of U.S. inflation

Periods of high inflation were due to unique events that are unlikely to repeat themselves in the modern era of monetary policy and characteristics of the U.S. economy. A pick-up in near-term inflation, due to extraordinary policy stimulus and rebound from the COVID-19 crisis is expected to be somewhat transitory. Higher inflation has correlated with weaker market and economic gains.



Source: Charles Schwab, MacroBond, Ned Davis Research using monthly data available as of 9/30/2021. U.S. CPI Urban Consumers YoY NSA (CPI YoY Index). Past performance is no guarantee of future results.

We don't expect that inflation will return to high levels reached in the 1970s and 1980s. Nonetheless, if the inflation rate were to remain above 3% to 4% for a prolonged period of time, there could be negative economic implications if the Fed takes more aggressive action. What is triggering inflation also has an impact on what actions the Fed will take to fight it. A Fed interest rate hike helps to control inflation by slowing demand when an economy is overheating. But it can't help ships unload containers more quickly or help address order backlogs.

Federal Reserve Actions: As anticipated, in November the Fed started to scale back its \$120 billion monthly purchases of Treasury and mortgage securities. Currently, they anticipate ending its monthly purchasing of these securities by next June. Furthermore, the Fed may start raising short-term interest rates (i.e., the federal funds rate) by mid-2022. This would be six months earlier than previously expected. Because interest rates are likely to rise in 2022, for those of you who would benefit from refinancing their mortgage, I recommend you do so 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 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) **CA Property Tax payments** are due December 10, 2021.
- 2) **Roth IRA Conversions:** Please contact us ASAP if you would like to discuss. The deadline for 2021 conversions is December 31, 2021.



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