McCarthy Asset Management, Inc.
Personalized Wealth Management

August 2024 Monthly Commentary

Sept. 3, 2024

Stock Market & Portfolio Performance

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August, 2024: Despite heighten volatility, with the exception of small-cap stocks, U.S. stocks ended up with gains for the month. Foreign stocks also rose while bonds appreciated modestly as the 10-year Treasury bond fell below 4.0 %.

	August 2024	YTD 2024	Description:
Without Dividends:			
S&P 500	2.3%	18.4%	500 Largest Public U.S. Companies
Russell 2000	-1.6%	9.4%	2000 of the smallest U.S. stocks
MSCI EAFE	3.0%	9.7%	international stock index
U.S. Aggr Bond	1.5%	3.2%	index of U.S. bonds
With Dividends, after all fees:			
MAM portfolios	1.7%	11.7%	non-very conservative MAM portfolios
MAM Consrv	1.4%	8.9%	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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Return of Stock Market Volatility

Return of Stock Market Volatility: Until last month, the stock market had been rising for the last year-and-a-half while displaying very little volatility. In fact, until last month, the sharpest decline this year was a drop of 5.5% in the S&P 500. That changed in early August when stock prices fell partly due to a concerning employment report. On August 7th, the S&P 500 fell to 5200, which was an 8.2% drop from the year's high reached on July 16th. Within the next week, though, the S&P 500 recovered most of that drop.

This latest bout of market volatility could be unsettling, especially after such a calm 2023 and first seven months of 2024 for stocks. However, market volatility of this magnitude is quite common. According to a recent report from LPL Financial, "On average, the S&P 500 experiences three drawdowns of between 5% and 10% each year...Corrections of 10-20% are also quite common, having occurred once per year on average...Elevated volatility and stock market drawdowns can be unnerving, but the market tends to reward those who stay invested, are patient, and do not panic."

"Sahm Rule" and the July Employment Report: The U.S. economy added 114,000 jobs in July, according to the latest report from the Bureau of Labor Statistics. That was well below the increase of 175,000 jobs that economists had predicted for the month. What spooked the stock market was that the unemployment rate increased to 4.3%, up from 4.1% in June. Economists had forecast the rate would remain steady at 4.1%.

In our July Monthly Commentary, we wrote about the "Sahm rule," a rule of thumb popularized by former Federal Reserve and White House economist Claudia Sahm. Looking at data from 1970 to 2018, she determined that recessions began when the unemployment rate over three months rose a half-percentage point or more above the lowest three-month average from the previous year. The Sahm Rule has successfully flagged every recession since the 1950s.

Based on the July unemployment data, the rule was technically not triggered. The increase in the unemployment rate was 0.493 percentage points. But that is close enough. Interestingly, Sahm wrote in her newsletter last month that a recession is not imminent. She said her own rule "is likely overstating the labor market's weakening due to unusual shifts in labor supply caused by the pandemic and immigration." In particular, the Sahm Rule may fail for this cycle because the rising unemployment rate has been largely caused by rising labor supply rather than falling labor demand.

Historically, labor markets slow down only after economic activity slows. But Gross Domestic Product (GDP) growth has remained strong. Nonetheless, once the unemployment rate starts moving upward, it's likely to continue rising. Rising unemployment is part of a vicious process of economic contraction. Employees losing their jobs lead to less spending, which causes firms to cut back, and unemployment to increase further. We will be closely monitoring the Employment reports for the next few months to see if the unemployment rate continues to rise.

U.S. Economy: According to an updated estimate, GDP rose at an annualized rate of 3.0% in the second quarter, dramatically higher than what was estimated and far better than the lackluster 1.4% figure logged for the first quarter. While growth is expected to slow for the remainder of 2024, July's retail sales soared past Wall Street's expectations in a sign that U.S. consumers remain quite resilient. Retail sales rose 1% in July, above estimates for a 0.4% rise.

Another Mild Inflation Report: Inflation fell below 3% in July for the first time since 2021, extending a run of cooler readings, and increasing the likelihood for the Federal Reserve to cut interest rates at its September meeting. For July, the consumer-price index rose 2.9% from a year earlier the Labor Department reported. Core inflation, which excludes volatile food and energy items, was 3.2%, also a three-year low.

First Fed Rate Cut Expected in September: A sustained and broad inflation slowdown provides the Fed with greater latitude to focus on shoring up any potential weakness in the labor market by cutting interest rates. The debate at the Fed's September meeting will likely center on whether to cut rates by a traditional quarter-point or by a larger half-point. The August payroll report, which is due on September 6th, may help the Fed with that decision. The Fed may also provide some clue as to whether officials expect to lower rates further at its last two meetings of the year, in November and December.

Return of Stock Market Volatility— Con't

Solid Corporate Earnings Growth but Stretched Valuations: Earnings for companies in the S&P 500 are on pace to record a jump of 10.9% from a year earlier. This would represent the biggest quarterly increase in over two years. As mentioned in our July Monthly Commentary, equity valuations are stretched. At a price-to-earnings ratio (P/E) of around 21, based on the consensus EPS estimate for the S&P over the next 12 months, stock prices are expensive, and a lot of good news is already priced in. The average P/E ratio of the S&P 500 over the past 25 years is 17.

MAM Comments: The near 10% drop in the S&P 500 index early last month could be a wakeup call for investors that stock market volatility has returned, and a stock market correction could be coming. For us to determine whether stocks prices are at risk for a more sustained downturn will depend upon the state of the U.S. economy. A continued rise in the unemployment rate could be a bad omen that a recession is approaching. On the other hand, aggressive Fed interest rates cuts could help keep the economy on a path of modest, but steady, growth.

Bonds Are Back

Bonds are once again acting as they should. The chart below displays the 10-year performance of the iShares Core U.S. Aggregate Bond ETF (symbol AGG). The returns for this ETF are a good indicator of the performance of the overall bond market. The chart shows the sharp drop in bond prices in 2022 when the Bloomberg U.S. Aggregate bond index fell 13.0%. This drop was triggered by a series of rapid interest rate hikes by the Federal Reserve to fight rising inflation. That's a huge loss for the bond market. Since 1976, the next worst year was a 3% drop in 1994. Historically, the bond market performs well after a down year. 2023 was no exception with the U.S. Aggregate Bond index returning 5.7% for the year.

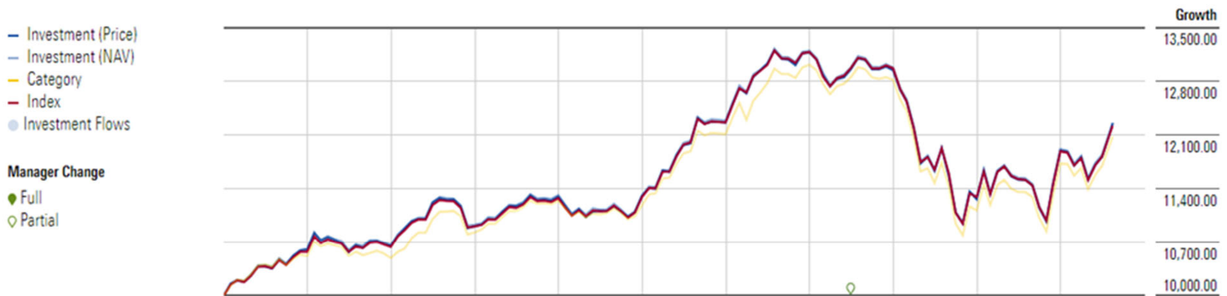
iShares Core U.S. Aggregate Bond ETF AGG ★★★ Gold

QUOTE ANALYSIS PERFORMANCE SUSTAINABILITY RISK PRICE PORTFOLIO PEOPLE STRATEGY PARENT

Show Full Analysis

Performance Returns Distributions

Growth of 10,000



Total Return %	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD
Investment (Price)	6.00	0.48	2.41	3.55	0.10	8.46	7.48	-1.77	-13.02	5.65	3.04

Bonds Are Back– Con't

For the following reasons, we feel that bonds are once again an appealing investment:

1) **Yields are Up:** After rising sharply in 2022, bonds yields are now close to the highest they have been in years. This is important because starting yields historically have a strong correlation to future returns. Currently, high-quality bonds, such as Treasuries and investment grade corporate bonds, are yielding 4% to 5%.

2) **Potential Appreciation:** With the Fed expected to start cutting short-term interest rates later this month, bond prices may experience some appreciation.

3) **Inflation Continues to Fall:** As discussed in the article above, the Consumer Price Index has been declining, and is now at a 3-year low. Falling inflation should lead to rising bond prices.

4) **Bonds Provide Downside Protection When Stock Prices Decline:** While 2022 was an exception, bonds have a strong historical track record of delivering for investors when equities struggle. Since 1974, U.S. stocks have had 10 negative calendar-year returns, in nine of those years, bonds were positive, with the only exception being 2022. This proved to be the case again during the early August stock market correction when interest rates fell, and bond prices rose.

In Summary: As we wrote one year ago, we feel that bonds are once again an appealing investment offering attractive yields. With the Federal Reserve expected to start cutting interest rates later this month, there is a potential for bond prices to experience some appreciation. Finally, at some point the U.S. economy will slide into a recession. If that were to occur, stock prices will likely fall with bonds providing downside protection to portfolios.

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

- Estimated Tax Payments: Third quarter 2024 estimated payments are due on September 16th.

Discover the difference with a Registered Investment Advisor.