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EXCHANGE TRADED FUNDS (ETFs)

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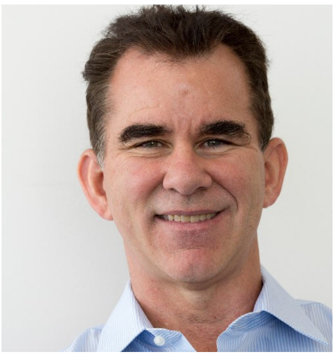

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McCarthy Asset Management, Inc. is an independent, fee-only investment advisory firm that has been helping people invest wisely for over fifteen years. Our mission is to help you better understand and improve your financial situation. We specialize in Retirement Planning, Portfolio management and Tax Planning.

This January marked the 20th birthday of the first and the biggest Exchange Traded Fund, SPDR S&P 500. In this article, Alexey gives a quick primer on what ETFs are and profiles some of the ETFs which you may have in your MAM portfolio(s).

What are ETFs? An Exchange Traded Fund (or ETF for short) is a basket of securities (stocks, bonds, alternative instruments, etc.) similar to a mutual fund, but trades on the exchange like a stock. An ETF allows investor to invest in a sector, an asset class, a region or some corner of the financial market without having to pick individual securities. Nearly $60 billion of exchange traded products are swapped daily on US exchanges, accounting for almost a third of a total trade volume. According to the Investment Company Institute, assets in domestic equity ETFs jumped $146.31 billion, or a 27% increase since December 2011 and global equity ETFs increased $83.41 billion. The total size of the ETF market in 2012 was estimated to be $1.337 trillion, including $243.2 billion in bonds and $656 million in hybrid ETFs.

The adoption of ETFs has increased among financial advisors in recent years. Low cost fund champion Vanguard manages nearly $230 billion in ETFs, while Schwab offers a suite of ETFs that have the lowest operating expense in their respective Lipper categories. A recent development, which is likely to increase the use of ETFs even more, also comes from Schwab. *More than 100 ETFs can now be traded commission free*.

Why use ETFs? ETFs can be used to gain broad exposure to the stock market, to gain access to a specific corner of the market or to augment an existing portfolio. According to Reginald Browne, a senior trader at Knight Capital, whom Forbes Magazine recently profiled as "the Godfather of ETFs", *"ETFs are the future of mutual funds. They just don't know it yet."* The market for ETFs is robust and growing fast, but is dwarfed by $10 trillion of investors' money still sitting in traditional mutual funds.

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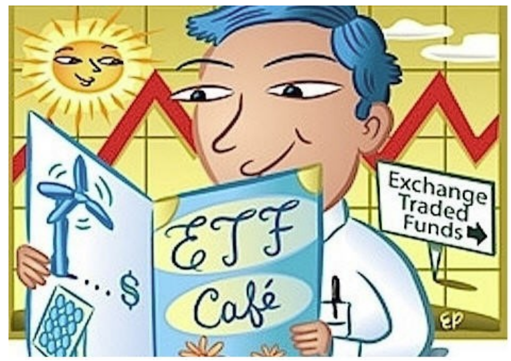
While it is premature to write-off mutual funds, ETFs do combine some of the best features of investing in mutual funds and individual equities:



- **Liquidity:** ETFs are traded throughout the day and change price constantly. The market is "deep" and efficient. Some exchanges even chose to pay market makers to provide liquidity and maintain a competitive quote.

- **Transparency**- Unlike many investment vehicles and investing strategies that only disclose their holdings quarterly, most ETF index funds publish their exact holdings on a daily basis, so an investor always knows what he or she owns.

- **Low Cost**- ETFs trade with no loads or 12(b)(1) fees. Because of the passive nature of the investment, expense ratios (cost of running an ETF) are low, which translates to investors keeping more of their gains.

- **Tax Efficiency**- most ETFs in existence today are not actively managed (i.e. track an index or a category). Thus there is very little buying and selling (turnover) going on inside the fund. That, in turn, contributes to tax efficiency.

- **Diversification**- an ETF investor can obtain a broad exposure to a market or an index with just one trade.

- **Fairness**- ETFs are often considered to be more "fair" to existing shareholders than a mutual fund. For example, if a mutual fund is successful and becomes popular, experiencing large inflows of cash, the fund manager has to put the money to work, buying more shares, thus creating turnover, resulting in more expense for existing shareholders. Conversely, when a fund is facing large redemptions (investors pulling money out), a fund manager has to sell the shares, sometimes burdening remaining shareholders with unwanted capital gains. In an ETF, investors are insulated from the tax consequences of the actions of their fellow shareholders.

Why Not Only Invest in ETFs?: One drawback of ETFs is that most of them are passively managed. The manager of the fund (which can actually be a computer program) has the ETF mimic an index.

Our Services

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.

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 several outside experts, whose services are available at no cost to our clients:

- Long Term Care Planning– Allen Hamm of Superior LTC Planning Services, Inc.

For areas of the market where we feel investing in indexes is appropriate (i.e. stocks paying a rising dividend and Master Limited Partnerships), we use them.

There are areas, though, where we still prefer to use actively managed funds. For instance, many of the ETFs that invest in bonds have a large exposure to U.S. Treasuries, which is the area of the bond market which is most exposed to the potential of rising interest rates. In addition, we use some actively managed funds such as Yacktman and BlackRock Health Science, which over time have substantially outperformed their benchmarks.

ETFs in MAM portfolios: At MAM we have been keeping a close eye on ETFs and added a few to portfolios in areas where we think they can add value. Some of the examples of the ETFs found in our portfolios are:

- VIG– This fund tracks the performance of the index which consists of common stocks of companies that have a record of increasing dividends over time.
- SCHD– The most recent addition to MAM Portfolios, this ETF seeks investment results that tracks, net of expenses, the total return of the Dow Jones U.S. Dividend 100 Index.
- AMJ- This exchange-traded note seeks to replicate, net of expenses, the Alerian MLP Index, which tracks the performance of midstream energy Master Limited Partnerships, giving our clients access to this growing alternative asset class that offers a generous dividend.
- IWM– This ETF seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of the Russell 2000 Index which measures the performance of the small-capitalization sector of the U.S. equity market.

Because we customize portfolios to meet the goals, objectives and risk tolerances of our clients, not every portfolio will have every ETF listed above. We constantly monitor for new additions which we believe will benefit our clients in the long haul. If you would like to learn more about the ETFs or have questions about any of the investment funds in your portfolio, please contact us.