

# CURBSTONE FINANCIAL MANAGEMENT CORPORATION

## From the Curb

Letter to Clients

Quarter Ending March 31, 2025

Investor concerns changed dramatically during the first quarter as focus shifted from worries a strong economy might re-ignite inflation to fear about a possible recession that was driven by the uneven implementation of a series of new tariffs on goods coming into the U.S. There were hints about looming trade policy issues in January when President Trump threatened Colombia with a 25% tariff, but these were largely dismissed by market participants as negotiating rhetoric since the administration held back on implementation. Stocks initially rallied to a new all-time high in anticipation of a business-friendly administration that would maintain tax cuts and promote deregulation, but quickly reversed as the extreme nature of the policy shift became apparent.

Market volatility rose sharply as trade policy continued to gain a greater influence on markets over the course of the quarter. It became clear that the policy shift was having a major impact when the consumer confidence report in February showed a significant decline implying that trade uncertainty was beginning to undermine purchasing behavior in the Main Street economy. Those fears were reinforced by a release showing that the Atlanta Fed's GDP forecast for 2025 had turned negative which led to further selling in the equity market.

Volatility gripped markets in March as stock indices witnessed declines following the announcement of automobile tariffs. Selling was more pronounced in the tech heavy NASDAQ which was off -10.4% for the quarter, with the benchmark S&P 500 falling -4.6% and the small cap Russell 2000 down -9.18%. Technology and consumer discretionary were the two worst performing sectors dropping -12.8% and -14.0% respectively. These influential components make up a combined total of more than 40% of the S&P index. The performance of the consumer discretionary sector was driven by declines in Tesla and Amazon along with general concerns about lower consumer spending looking forward. Tech sector results were a function of lofty expectations to start the year and the debut of the Chinese AI program Deep Seek which challenged assumptions about the future economic benefit of AI for major tech firms.

We recognize how unsettling a sharp rise in volatility can be for clients, especially those who are drawing income from their portfolios. Risk management is a cornerstone of how we build portfolios because we know that markets do not rise in a straight line over time and that events beyond our control will inevitably appear from time to time to disrupt the best laid plans. Return potential is one factor that we consider in developing strategy and evaluating investment selections, but volatile periods highlight why there are other factors that we look at in our process. It is also important to diversify client portfolios to provide insulation against more challenging environments and to ensure that cash flow needs continue to be met regardless of how the market is performing at a given point in time. A dynamic asset allocation process and thoughtful selection of bonds to provide a reliable income stream are essential to meeting client objectives.

Bonds offered a measure of consolation to investors with more balanced asset allocations as the Bloomberg Barclays Aggregate Index posted a solid gain up +2.78% for the quarter. Positive fixed income performance was the result of more benign inflation reports, the possibility of a slowing economy and some rotation away from stocks. Not unexpectedly, higher quality investment grade bonds performed better than their higher yielding, lower quality counterparts. Longer maturity bonds

provided better returns than shorter ones again pointing to growing expectations for weakness in the months ahead.

The value in taking a well-diversified approach was also evident in the performance of traditionally defensive sectors (health care, consumer staples and utilities) and foreign stocks. Defensive sectors logged modest gains for the quarter, showing some resilience in the face of heightened economic concerns, while foreign stocks posted strong gains with the MSCI EAFE Index rising +8%. This shift was driven by concerns about U.S. trade policy and investors repositioning portfolios to have less exposure to the more volatile technology sector.

Growing uncertainty over how other nations will respond has introduced variability into analyst expectations for GDP and corporate earnings growth looking through the remainder of the year. Forecasting has become more difficult since we cannot be sure of how long particular tariffs will remain in place. We will be closely monitoring the momentum in new jobless claims, purchasing managers' activity and credit spreads to gauge the impact of the trade policy shift as these factors have been reliable indicators of market risk during prior business cycles. The tone of company analyst calls and management guidance on earnings will be an important barometer for business confidence. Concerns about the pace of economic growth in the months ahead are a flashing yellow light that brings focus to finding ways to improve earnings quality, increase the income stream and reduce risk in portfolios. It is a time when a disciplined selection process can add value as solid long-term opportunities present themselves amid the volatility.

We recognize that this is a time of great uncertainty and that you may have more questions or concerns than under normal market conditions. We, therefore, invite you to call and touch base as often as you desire. We believe an open line of communication is critically important to mutually rewarding relationships and look forward to connecting with you.