From the Curb

Letter to Clients
Quarter Ending December 31, 2019

Investors welcomed the positive resolution of several key macroeconomic unknowns in the fourth quarter, and that improved clarity sent the broader stock market higher. The solid fourth quarter gains helped the S&P 500 index achieve its best annual return since 2013. Bonds, as measured by the performance of the Bloomberg Barclays Intermediate Government Corporate Index, also posted the best returns the index has seen in well over a decade.

By far, the most important event for markets during the fourth quarter was the agreement to a "phase one" trade deal by the U.S. and China. Since early 2018, the U.S.-China trade war, and the tariffs that came with it, pressured the global economy and weighed heavily on investor sentiment. Twice in 2019, first in May and again in August, tariff increases caused a significant spike in market volatility.

Improvement in U.S.-China trade relations wasn't the only positive event in the fourth quarter. The Federal Reserve met market expectations by cutting its benchmark interest rate by another 25 basis points at the meeting on October 30th. That cut brought the total reduction in interest rates in 2019 to 75 basis points, the largest annual reduction in over a decade. Additionally, at the December policy meeting, the members of the Federal Open Market Committee communicated that they do not expect to raise interest rates in the new year. That added clarity for stable interest rates in 2020 also helped power stocks higher in the fourth quarter.

The global and U.S. economies also showed signs of stabilization in the fourth quarter after losing positive momentum for much of 2019. First, in the United States, concerns were growing that sluggish business spending and investment would potentially cause a broader economic slowdown. But the market's preferred measure of business spending and investment, the monthly Durable Goods report, rebounded in the fourth quarter, easing some of those growth concerns. Internationally, measures of Chinese manufacturing activity, which had shown the industry was in contraction for the past several months, turned positive in December, and that implied activity was stabilizing. So, while concerns remain about the direction of the global economy, these signs of progress in the fourth quarter further supported the market's rally.

Ultimately, 2019 turned out to be a banner year for both stock and bond markets. Equity returns in the fourth quarter demonstrated that macroeconomic activity matters and that when presented with greater clarity, investors will favor riskier assets. The positive news on the four key macroeconomic fronts coupled with solid fundamentals supplied just the right amount of optimism to carry the momentum into 2020.

The major U.S. stock indices were all solidly higher in the fourth quarter led by the tech-heavy Nasdaq which handily outperformed due to rising optimism on U.S.-China trade and expectations for a rebound in economic growth. The S&P 500, Dow Jones Industrial Average and Russell 2000 (the small-cap index) all had smaller, yet positive, quarterly returns. The performance of the major indices in the fourth quarter mirrored the full-year performance, as the Nasdaq easily outperformed the other three indices in 2019 as investors sought the secular growth potential of the tech sector amidst macroeconomic uncertainty.

US Equity Indexes	Q4 Return	2019 Return
S&P 500	9.07%	31.49%
DJ Industrial Average	6.67%	25.34%
NASDAQ 100	12.99%	39.46%
S&P MidCap 400	7.06%	26.20%
Russell 2000	9.94%	25.52%

Source: YCharts

Internationally, foreign markets saw positive returns in the fourth quarter thanks mostly to the U.S.-China trade deal, although most foreign markets still underperformed U.S. markets. Foreign developed markets posted solid gains in the fourth quarter but lagged emerging market returns. Emerging markets outperformed both foreign developed markets and the S&P 500 in the fourth quarter thanks to rising expectations for a global economic rebound, combined with some weakness in the U.S. dollar. For the full year 2019, foreign markets registered solid positive returns, with foreign developed markets modestly outperforming emerging markets.

International Equity Indexes	Q4 Return	2019 Return
MSCI EAFE TR USD (Foreign Developed)	8.21%	22.66%
MSCI EM TR USD (Emerging Markets)	11.93%	18.90%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	8.99%	22.13%

Source: YCharts

With respect to fixed income markets, the total return for most bond classes were positive in the fourth quarter. Looking deeper into the fixed income markets, longer-duration bonds underperformed those with shorter durations in the fourth quarter which was a reversal from most of 2019. This is reflective of a market that is responding to the recent Fed rate cuts and beginning to expect a rebound in global economic growth going forward.

US Bond Indexes	Q4 Return	2019 Return
BBgBarc US Agg Bond	0.18%	8.72%
BBgBarc US T-Bill 1-3 Mon	0.44%	2.21%
BBgBarc Int. Gov/Corp	0.37%	6.80%
BBgBarc Municipal	0.74%	7.54%

Source: YCharts & Interactive Data

Curbstone's approach to constructing broadly diversified portfolios, customized to your risk profile, benefited from the strong rally in both bond and stock markets during 2019. This is best demonstrated on the **second page** of your report under the **Performance** section. The portfolio's total return appears on the first line followed by the Capital Formation Assets (stocks) return on the third line and the Income Producing Assets (bonds) return on the seventh line.

While the macroeconomic environment appears to be favorable as we begin 2020, a new year always brings new challenges and uncertainties, especially during an election year. Investor's expectations are high and focused on details of the trade deal, a re-acceleration of global economic growth, stable interest rates and growth of corporate earnings and profits. Tensions with Iran have risen and North Korea remains a wild card. Any escalation of aggression on the geopolitical front, along with unmet investor expectations, will likely result in increased volatility.

The take away from this year is clear: What happened in the markets last year doesn't mean much for what could happen in the markets this year. We've managed through both good and bad markets, and those experiences ensure that we guard against complacency following a year of strong returns. We remain committed to assisting you navigate this ever-changing market environment, with a focused eye on ensuring we continue to make progress on achieving your long-term investment goals.

Your year-end reports are enclosed. Please do not hesitate to contact us with any questions, comments or to schedule a portfolio review. We appreciate the opportunity to serve as your investment advisor.

Wishing you a healthy and happy 2020!

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