

Quarterly

NEWSLETTER



JANUARY 2019

INVESTMENT INSIGHT

GREGORY A. CARLSON, CFP®, CEO AND FOUNDER

As we all observed and experienced, the close of 2018 brought an unsettling time in the equity markets. Markets historically don't respond favorably to uncertainty, be it financial, political or social, and recent volatility appears to be tied to a host of uncertainties. Many individual investors react to uncertainty based on emotion, even though we've seen throughout the history of the market how important it is that investors don't allow emotion to influence decisions. Throughout recent market volatility, we have stayed disciplined in employing our consistent investment strategy at CCM.

Adhering to a consistent strategy means that our team knows what to do in all types of market conditions. When faced with a time like this marked by volatility, we rebalance—which helps us to buy low and reduce risk. We harvest losses when appropriate—which reduces current and future tax liability. We set aside money for future cash flow and expenditures—which assures we won't sell any asset class at an inopportune time. To reiterate our December message, our constant focus is to be your partner in attainment of your long-term financial goals. While volatility is unpleasant for all of us, we know that it is part of the ride we are on as investors. It is core to the tenets of risk and reward, and managed appropriately it is a very key component for long-term success.

When individual investors approach building an investment portfolio, or for that matter choose any component piece of a portfolio, the process for many people usually starts with these two following primary considerations:

1. **Is this a good investment choice considering all the alternatives?** This question can be asked about an individual stock or bond, a sector or asset class, equities or bonds in general, or a whole host of investment choices and investment vehicles.
2. **Is this the right time to invest?** This question arises as one may be thinking about if the economy is strong or weak, if there is going to be a recession, or if markets seem to be overpriced or underpriced. At a more detailed level, they may be wondering about an individual company that has an exciting

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CARLSON
CAPITAL MANAGEMENT

Integrated Wealth Management Since 1987

new product to launch that could significantly increase profits. Or what about a new competitor coming into the marketplace that will challenge a company's profitability?

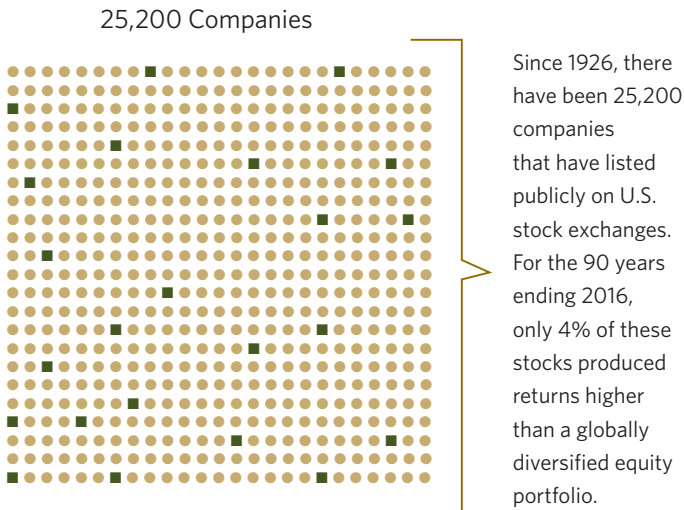
We know these are important questions and how we build and manage our clients' portfolios need to address both; what are good investments and what is the right time (or wrong time) to invest? For this update we are going to focus primarily on a dimension of the first question, but know that we have considered both questions (and more) when we manage your investments and create your financial plan.

As a member of our Investment Committee at CCM, I am part of a group tasked to query, challenge, and oversee our team as we determine how to build what we believe to be our best possible investment portfolios. A core principle on which we operate is that decisions are evidence-based. In this regard, our investment team recently shared a study on diversification, published by Hendrick Bessembinder, Professor of Finance at Arizona State University. For this quarter's *Investment Insight*, I wanted to highlight this work as I think the study makes some very interesting and important observations that are relevant to CCM clients.

The Evidence to the Value of Diversification

In essence, the study entitled "Do stocks outperform Treasury Bills?" identifies, and the related chart below illustrates, that since 1926 approximately 25,200 companies have been listed and publicly traded on the exchanges of the U.S. stock market and that these 25,000 + companies generated approximately 35 trillion dollars of wealth (from 1926-2016).¹ Related to that wealth generation, the following data from the study are of important note:

- 51% of the companies created negative value
- 73% of the companies returned less than short term government bonds have returned
- 96% of the companies returned less than the return of a diversified portfolio



This is the type of evidence that supports the backbone of CCM's investment philosophy and amplifies three very important points:

1. Investors are constantly bombarded by prognosticators and influencers who are pitching something that purports to be superior to the alternative. In the financial world, the loudest voices are often those who have a vested interest in a product sale; are suggesting one should follow them (e.g. active managers) because they have a "crystal ball" that is more clear than others; or they may be part of an organization providing financial insights as a means to sell newspapers or other content. Putting aside the "noise" that can distract investors, the evidence is conclusive—it is very, very difficult to choose individual securities or investment vehicles that beat a diversified portfolio's return. Especially in times of volatility there can be an emotional desire to "do something" even when it is not supported by evidence and is certainly not in one's best interest.
2. Your portfolio is invested in more than 13,000 companies across the globe. This is traditionally highlighted as it relates to reducing risk, but equally important is that a globally diversified portfolio assures that you will capture the long-term excess return of stocks over safer fixed income investments. It is a fool's game to think that anyone can consistently or predictably choose the 4% of stocks that will outperform a diversified portfolio. CCM's investment approach ensures you are not subject to that type of risk. We position your portfolio to efficiently capture the returns that have consistently provided favorable results over the long term.
3. Owning a diversified equity portfolio does not totally protect one from market declines, as evidenced once again by performance in 2018 (in fact, on average, equity returns have produced negative returns in about one of every three years). Equity diversification, along with a fixed income (bond) allocation within a portfolio, further reduces the likelihood of negative returns. This approach, managed well—and as part of a carefully designed overall financial plan—will produce the strongest likelihood for success.

At CCM, we understand the discomfort that comes when the markets are performing erratically. It is important to us that even when we experience this kind of unrest, that our clients are still afforded peace of mind. This is what inspires us to continue to highlight quarterly insights and updates that relate to the underpinnings of our investment approach and how they tie to your portfolio. This has been a priority at our firm since our founding.

CCM's Investment Committee and investment team are tasked with always challenging our investment philosophy, strategy, and execution with a singular focus—working to improve your results and investing experience. Along with our other team members in the disciplines of tax, estate, retirement, risk management and philanthropy, we are committed to being your trusted partner, working with you to help your wealth reach its full potential.

¹ Bessembinder, H. (Accepted/In press). Do stocks outperform Treasury bills? *Journal of Financial Economics*. <https://doi.org/10.1016/j.jfineco.2018.06.004>

AT A GLANCE

FOURTH QUARTER AND YEAR-END RETURNS



	Q4 2018	1-YEAR RETURNS	5-YEAR RETURNS	ANNUALIZED 10-YEAR RETURNS
S&P 500 Index	- 13.52	- 4.38	+ 8.49	+ 13.12
US Large Value	- 11.72	- 8.27	+ 5.95	+ 11.18
US Small Cap	- 20.20	- 11.01	+ 4.41	+ 11.97
US Small Value	- 18.67	- 12.86	+ 3.61	+ 10.40
International Large Cap	- 12.54	- 13.79	+ 0.53	+ 6.32
International Large Value	- 11.70	- 14.78	- 0.61	+ 5.50
International Small Cap	- 16.05	- 17.89	+ 3.06	+ 10.51
International Small Value	- 14.62	- 18.17	+ 2.39	+ 10.14
Emerging Markets	- 7.47	- 14.58	+ 1.65	+ 8.02
US Short-Term Bonds	+ 1.46	+ 1.38	+ 1.32	+ 2.09
US Intermediate-Term Bonds	+ 1.64	+ 0.01	+ 2.52	+ 3.48

Data represents past performance. Past performance is no guarantee of future results. Chart is for illustrative purposes only. Returns are based on data from the S&P 500, Russell Investments for US indices, MSCI for international and Barclays for bonds for the time period of October 1, 2018 through December 31, 2018.

Indexes used for the table and sector references are listed on page 8.

- U.S. equities were negative in the fourth quarter, driving one year returns into negative territory.
- Small companies and growth companies underperformed large companies and value companies in the fourth quarter.
- Utilities (+0.75%), Consumer Staples (-4.23%) and Health Care (-6.04%) were the best performing sectors.
- Energy (-21.81%), Technology (-17.61%) and Consumer Discretionary (-15.54%) were the worst performing sectors.
- International and emerging market stocks were also negative, but outperformed U.S. equities.
- Fixed income returns were positive for the quarter and benefited from higher interest payments.

CCM COLLEAGUE PROMOTIONS ANNOUNCED

We are pleased to announce that Adam Hoffmann, CFP®, AIF® has been promoted to Chief Investment Officer and Matt Morehead, J.D., CEBS, has been promoted to Senior Integrated Wealth Advisor.



ADAM HOFFMANN, CFP®, AIF®
Chief Investment Officer

Adam Hoffmann has more than twelve years of experience at CCM and has served in progressively responsible roles at the firm. “Adam’s incisive acumen in portfolio management and investment research have been invaluable assets to the firm and to our clients. I’m pleased to announce his promotion to CIO,” said President, Justin Stets. Adam chairs the CCM Investment Committee and is a member of both the Management Team and Director Team at the firm.

Adam holds the Certified Financial Planner™ designation and has served as a subject matter expert for the CFP Board. He has also earned the Accredited Investment Fiduciary professional designation awarded by the Center for Fiduciary Studies. The AIF designation affirms the highest in fiduciary standards of care for CCM clients.



MATT MOREHEAD, J.D., CEBS
Senior Integrated Wealth Advisor

Matt Morehead joined CCM in 2015 with more than ten years of experience in financial services and now for the past thirteen years has served clients and their families by advising on all aspects of wealth management. “Helping clients do great things with their wealth over time, as defined by them, and witnessing their resulting fulfillment, is extremely gratifying to me,” stated Morehead.

Matt works primarily with clients in the Rochester area where he is actively engaged in the community serving on the board of directors of the Rochester Area Chamber of Commerce and for the pediatric transplant house, Cy’s Place, in addition to participating as an active member of Rotary International.

AN UPDATE FROM THE TAX TEAM: *Key Tax Figure Updates for 2019*

KEVIN KOSKI, CPA, PRINCIPAL TAX ADVISOR

As the new year begins it brings many important tax-related limits, rates, and deduction updates to be noted. Included below are some of the key items for CCM clients to be aware of. Be sure to contact any member of our Tax Team with questions on how these changes may impact your integrated wealth management planning for 2019 or future years.

RETIREMENT ACCOUNT CONTRIBUTION LIMITS

	2019	2018
401k/403b/457 Elective Deferral	\$19,000	\$18,500
401k/403b/457 Catch-Up Age 50+	\$6,000	\$6,000
Traditional or Roth IRA	\$6,000	\$5,500
Traditional or Roth IRA Catch-Up Age 50+	\$1,000	\$1,000
SIMPLE IRA	\$13,000	\$12,500
SIMPLE IRA Catch-Up Age 50+	\$3,000	\$3,000
SEP-IRA/Profit Sharing	\$56,000	\$55,000
SEP-IRA/Profit Sharing Catch-Up Age 50+	\$6,000	\$6,000

HEALTH SAVINGS ACCOUNT CONTRIBUTION LIMITS

	2019	2018
Single Only Coverage	\$3,500	\$3,450
Family Coverage	\$7,000	\$6,900
Catch-Up Contribution Age 55+	\$1,000	\$1,000

STANDARD MILEAGE RATES

	2019	2018
Business	\$0.58	\$0.545
Charity	\$0.14	\$0.14
Medical	\$0.20	\$0.18

ESTATE AND GIFT TAX EXCLUSIONS

	2019	2018
Federal Estate Tax Exclusion	\$11,400,000	\$11,180,000
Federal Annual Gift Tax Exclusion	\$15,000	\$15,000
Minnesota Estate Tax Exclusion	\$2,700,000	\$2,400,000

INCOME TAX RATES — SINGLE AND MARRIED FILING JOINTLY

Tax Bracket	2019 ENDING TAXABLE INCOME		2018 ENDING TAXABLE INCOME	
	Single	Married Filing Jointly	Single	Married Filing Jointly
10%	\$9,700	\$19,400	\$9,525	\$19,050
12%	\$39,475	\$78,950	\$38,700	\$77,400
22%	\$84,200	\$168,400	\$82,500	\$165,000
24%	\$160,725	\$321,450	\$157,500	\$315,000
32%	\$204,100	\$408,200	\$200,000	\$400,000
35%	\$510,300	\$612,350	\$500,000	\$600,000
37%	No Limit	No Limit	No Limit	No Limit

STANDARD DEDUCTION AMOUNT

	2019	2018
Married Filing Joint	\$24,400	\$24,000
Single	\$12,200	\$12,000
Head of Household	\$18,350	\$18,000
Additional for Age 65+	\$1,300	\$1,300

Tax updates featured in previous newsletters can be found at carlsoncap.com/articles

A MESSAGE FROM CCM'S CHIEF COMPLIANCE OFFICER

As part of Carlson Capital Management's active disaster recovery plan, each year we remind clients of how we will reach you, or how you can reach us, should there be an event causing significant business disruption at the firm. Following physical safety and data protection, our priority is to be able to effectively communicate with you. Please note the following methods that would be deployed if needed:

- CCM has a long-standing contract with an organization that is equipped to immediately notify all CCM clients via your primary phone number (or voice mail) should an emergency arise. If the system is activated, you would receive a message instructing you on how to reach us.
- The home page of our website would also be updated to contain pertinent contact information.

With four separate physical office locations, assets custodied with third parties such as Charles Schwab, TIAA and Vanguard, and all of our electronic data housed at a secure off-site data center, we believe that CCM is well protected from incidents. None-the-less please know that we actively review and update our disaster recovery plan in order to help mitigate any potential risks.

JUSTIN D. STETS, AIF®, *President and Chief Compliance Officer*

CARLSON CAPITAL
MANAGEMENT FILM SERIES

Enriching Lives

We just released the third film in our new *Enriching Lives* series and we're excited to share it with you. In 2016, our firm became one of only a few wealth management firms in the country to be employee-owned. This short clip, "Employee Owned" features our colleagues talking about what we think it means for clients to work with a wealth management firm that is owned by its employees.

"To have that ownership really says a lot about who we are. We have intent and care around colleagues, as we do around clients, to ensure that this culture is continuing for a long time to come."

– JASON KLEY, CFP®, AIF®, MBA

Senior Integrated Wealth Advisor & Director of Financial Planning

The *Enriching Lives* film series focuses on the core aspiration of the Vision Statement of CCM. While the series helps those who don't know us at CCM to be introduced to our firm and our team, we think that clients may also appreciate the insights shared in the films. You may also "meet" someone new or connect a face with the name and voice of someone who works behind-the-scenes with your advisory team.

In addition, as CCM has grown over the years, expanding our circle of care to help the friends and family members you have introduced to us, we invite you to share the films with anyone you think may be interested. We'll be pleased to meet them.



VIEW THIS FILM AT carlsoncap.com/video



WELCOME NEW COLLEAGUES

As growth at the firm continues to serve clients with more breadth and depth, we're happy to introduce eight new colleagues who have recently joined our team at CCM: BEN, BONNIE, HALEY, JSAN, KAT, RACHEL, SUE and VAL.

We encourage you to review full biographies at carlsoncap.com/team where you can also connect directly with any colleague of the firm.



Ben Carlson
Paraplanner
Bloomington Office
St. Olaf College



Bonnie Anderson Rons
Client Servicing Representative
CCM Tax & Trust Administration
Hastings Office
South Dakota State University
and the University of St. Thomas



Haley Jochum
Client Servicing Representative
Rochester Office
Minnesota State University – Mankato



Jsan Homsombath
Investment Operations & Trading Specialist
Bloomington Office
University of North Dakota



Kat Noble Moore
CRM Database Administrator
Bloomington Office
Drake University



Rachel Chacko
Paraplanner
Rochester Office
Grinnell College and the
University of Colorado – Boulder



Sue Desrosier, CFEI
Retirement Plan Services
Client Relationship & Education Manager
Bloomington Office
Hamline University



Val Thomas, CTFA
Senior Integrated Wealth Advisor
Hastings Office
University of Northwestern – St. Paul

COMPANY NEWS & COMMUNICATIONS



On Monday, November 5, CCM clients and friends of the firm gathered at the University of St. Thomas for *Financial Insight, Wealth Intention and Life Inspiration*—a special evening with a discussion focused on insights from Scott Bosworth of Dimensional Fund Advisors, and a keynote presentation delivered by renowned inspirational speaker John O’Leary. We were delighted to see so many of you there and thoroughly enjoyed your company! Pictured above are Scott Bosworth and John O’Leary with Shane, Therese and Steve Kitman.

The CCM Team congratulates JASON KLEY, CFP®, AIF®, MBA, Senior Integrated Wealth Advisor and Director of Financial Planning, as he completes his year serving as President and transitions to the role of Chair of the Board of the Financial Planning Association of Minnesota. FPA MN’s primary aim is to benefit the public by helping to ensure that financial planning is delivered through proficient, ethical financial planners. fpamn.org



HOLIDAY GIFT 2018



One of the highlights for us at CCM this time of year is seeing responses to our Holiday Card arrive in the mail or through the website. In keeping with our tradition of a CCM Holiday Gift of

giving, clients are invited to submit a nomination of an organization where you are engaged as a volunteer or that you support. CCM will be presenting \$1,000 each to ten organizations drawn randomly from those nominated.

Responses sent in by postcard or entered online by January 15, 2019, will be included in the drawing: carlsoncap.com/holidays2018

Indexes used for the table on page 3 are as follows: S&P 500 TR USD; Russell 1000 Value TR USD; Russell 2000 TR USD; Russell 2000 Value TR USD; MSCI EAFE NR USD; MSCI Value NR USD; MSCI EAFE Small Cap NR USD; MSCI Small Value NR USD; MSCI EM NR USD; Barclays US Govt/Credit 1-5 Yr TR USD; Barclays US Agg Bond TR USD.

Indexes used for sector references on page 3 are as follows: S&P 500 Sec/Cons Disc TR USD; S&P 500 Sec/Cons Staples TR USD; S&P 500 Sec/Energy TR USD; S&P 500 Sec/Financials TR USD; S&P 500 Sec/Health Care TR USD; S&P 500 Sec/Industrials TR USD; S&P 500 Sec/Information Technology TR USD; S&P 500 Sec/Materials TR USD; S&P 500 Sec/Commun Services TR USD; S&P 500 Sec/Utilities TR USD.

IMPORTANT DISCLOSURE INFORMATION: *Please remember that past performance may not be indicative of future results. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product (including the investments and/or investment strategies recommended or undertaken by Carlson Capital Management, LLC (“CCM”), or any non-investment related content, made reference to directly or indirectly in this newsletter will be profitable, equal any corresponding indicated historical performance level(s), be suitable for your portfolio or individual situation, or prove successful. Due to various factors, including changing market conditions and/or applicable laws, the content may no longer be reflective of current opinions or positions. Moreover, you should not assume that any discussion or information contained in this newsletter serves as the receipt of, or as a substitute for, personalized investment advice from CCM. Please remember to contact CCM, in writing, if there are any changes in your personal/financial situation or investment objectives for the purpose of reviewing/evaluating/revising our previous recommendations and/or services, or if you would like to impose, add, or to modify any reasonable restrictions to our investment advisory services. CCM is neither a law firm nor a certified public accounting firm and no portion of the newsletter content should be construed as legal or accounting advice. A copy of CCM’s current written disclosure Brochure discussing our advisory services and fees is available upon request.*

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