THE BOSTON FAMILY OFFICE

Investment Update

Third Quarter 2016

Twenty years ago on October 1st, the Boston Family Office opened its doors with the purpose of providing better service to the founding partners' families and clients. Since then, we have grown from five people to sixteen, with two working far from Boston, and from $150 million or so of assets under management to over $1.0 billion. Despite this growth, we remain committed to helping our clients meet their investment goals in a tax-efficient manner by using a more flexible investment framework than many other firms. On this occasion, we would like to thank our clients and others who have supported us along the way.

Much has changed in the ensuing twenty years. Your author was in college back then and remembers swearing to himself he would never waste his time getting an email account after hearing a schoolmate say, "I was in my room all afternoon emailing a friend from home." The next fall email submission of homework was required, and it is fair to say that the medium has actually proven to be a productivity enhancer for me and many others since. In 1996 the entire US Treasury yield curve was between 5% and 7%, Seinfeld was the top show on TV, Dolly the Sheep along with the Unabomber and Mad Cow disease filled the headlines, AOL sent CDs in the mail to advertise their 56k dial-up internet access, our youngest employee was in third grade, an app was an hors d'oeuvre, and the Patriots were on their way to a Super Bowl loss behind Bill Parcells and Drew Bledsoe.

Back to 2016. We spent much of the last investment update discussing the surprise outcome of the Brexit vote at the very end of June. By the time our piece was published, the US stock market had regained all of the ground lost immediately after the vote, and proceeded upwards to new all-time highs shortly thereafter. Bonds also rallied strongly with Treasury yields reaching historic lows. The rest of the summer saw very little price volatility, disturbed only briefly in early September when a sharp rise in Treasury yields caused weakness in stocks. Nonetheless, both markets have settled back to end the quarter closer to where they had been in August, firmly in the positive over the last year.

Equity Markets (Total Returns)	**3Q16**	**1-Year**
Dow Jones Industrials	2.78%	15.46%
S&P 500	3.85%	15.43%
S&P Mid-Cap	4.14%	15.33%
S&P Small-Cap	7.20%	18.12%
MSCI All-Country World	5.19%	11.42%
MSCI Foreign Developed Markets	5.70%	7.62%
MSCI Foreign Emerging Markets	7.71%	13.37%
US Bond Markets (Total Return)	**3Q16**	**1-Year**
Barclays US Gov't/Credit Intermediate	0.44%	5.31%
Barclays US Gov't/Credit Long	2.26%	15.73%
Barclays Municipal Intermediate	-0.30%	5.58%

It has been a strong year so far for most stocks that offer an attractive income return. REITs, utilities, telecoms, and consumer staples have spent most of 2016 well ahead of the broader market, something one would not normally expect in an "up market." Of course any time fears of central bank tightening or longer term bond yields increase, these high-yielding equities have suffered more than the broader market. Significant investor attention is still paid to if, when, and how often the Fed will raise interest rates, but the European Central Bank and Bank of Japan are increasingly sharing the spotlight. Moves by

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foreign central banks in and of themselves should not greatly affect the fundamentals of American companies, although they clearly are indicative of the economic fundamentals in their home markets where American companies may sell their products. Potential upward interest rate moves by the Fed certainly will require a psychological adjustment after all these years at or near zero, but monetary policy would still be extraordinarily accommodative by historic standards even with several interest rate increases over the next year. Having interest rates near zero for so long has likely had consequences that run contrary to their textbook effects, which are that lower interest rates should spur borrowing and investment and ultimately drive price inflation. However, since the Financial Crisis, exceptionally low interest rates have allowed less competitive companies to borrow cheaply and continue competing (which likely has had a deflationary effect on prices) when they might have otherwise gone out of business in a more normal interest rate environment.

The expansion of price-to-earnings ratios driven by ever-lower bond yields has been a significant contributor to stock market performance over the last several years. However with yields near all-time lows, this tailwind has probably run its course and a return to earnings growth (S&P 500 earnings have been flat to negative for six quarters) will probably be needed to drive material upside for stocks. To be fair to the broader market and economy, energy companies' woes have obscured otherwise positive numbers since the price of oil started falling over two years ago, and estimates of 2017 S&P 500 earnings suggest that this quarter or next will be an inflection point.

Looking back at what Ned Weld wrote in our first investment update in January 1997, we are pleased to see that much of what we were thinking then still applies today. We continue to believe that "the long term fundamentals remain constructive for equity investing." While not as enthusiastic about our political environment as we were then, we do still feel that "our major companies are well positioned to compete internationally" and that "the technology revolution continues to provide investment opportunity and productivity enhancements." Finally, he suggested a "cautious outlook" for the coming year. As we enter our twenty-first year, we maintain an optimistic outlook with a dose of caution for the potential potholes that develop from time to time.

The information contained in this report has been taken from trade publications, statistical services and other sources, which we deem reliable. We do not represent that it is accurate or complete, and it should not be relied upon as such. Any opinions expressed herein reflect our judgment at this date and are subject to change.

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