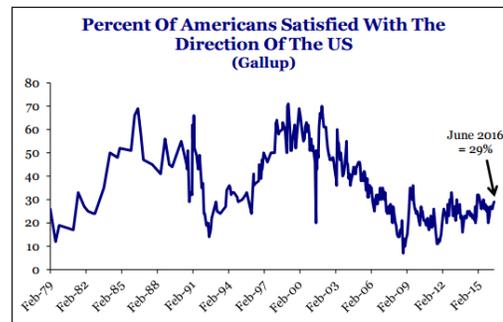




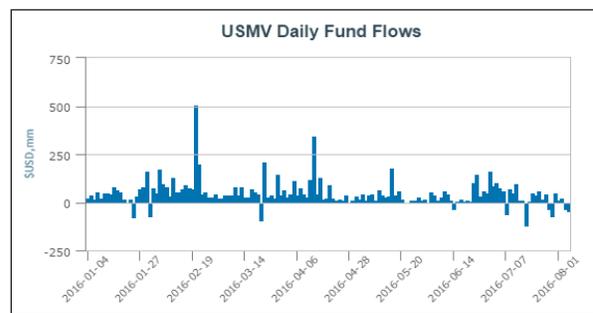
## Summer 2016 Investment Report

We've been blessed in New England this summer with beautiful weather and a US stock market trading at all-time highs. As much as we would like to spend more time outside, this has been a busy summer managing client assets, enhancing our data security and compliance procedures, and (fortunately) transitioning new clients to the firm. Hemenway Trust Company and H&B now proudly work with over 400 families and charitable institutions and assets under management have grown to \$3.8 billion.

The summer started off with a bang as UK citizens voted to leave the EU on June 23rd. The vote initially roiled currency markets, sent equity markets down between 5-15% and pulled government bonds yields to historic lows as investors sought safety. Once it was clear that the vote only started the process of "Brexit" and would take years to implement, risk markets snapped back and now trade above where they did before the vote. Unfortunately, we have not seen bond yields rebound and we worry that much of the increase in equity markets has been a result of interest rates (discounting future earnings at a lower rate), rather than an expectation of higher earnings growth. With subpar growth across most of the developed world, we expect to see more volatility as a result of voter discontent with the political establishment.



In the US, macro data is still mixed. On the positive side, we see jobs continue to grow at +200,000 per month, housing starts hitting levels not seen since 2007 and consumer spending up 4.2% during the Q2. However, despite a strong consumer, GDP only expanded by 1.2% for the quarter, and the Fed's preferred measure of inflation, core personal consumption expenditures (PCE), grew at only 1.6% year over year, less than the Fed's 2% target. The uneven growth in the economy also has led to uneven growth in the equity markets. As investors are forced out of the bond market due to low yields, many have moved into higher dividend stocks that are perceived to be safer – such as REITs, utilities and consumer stocks. In the last three years, there are five new "minimum volatility" ETFs with over \$3 billion in assets under management and many "defensive" stocks are trading at growth stock valuations. We have been a net seller of many of these names and have been rotating to other stocks, some of which are cyclical in nature. These cyclical (more economically sensitive) stocks are perceived to have more



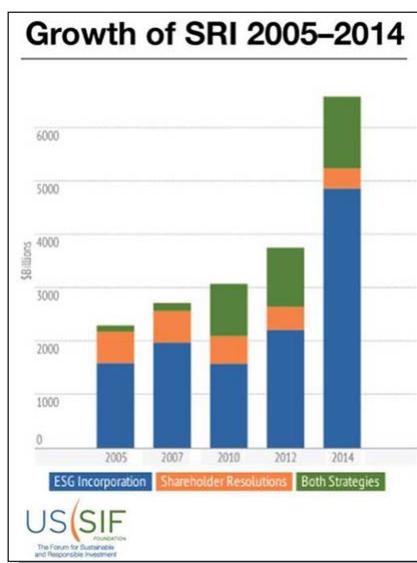
# Summer 2016 Investment Report (continued)

risk, but valuations are more compelling and investors with a longer time horizon should be rewarded. You can read more about on risk in Chris White's white paper "Embracing Market Risk" at [www.hemtrust.com](http://www.hemtrust.com).

## Sustainable investing

Many say that values based investing started in the 1700's with the Quaker prohibition against investing in slavery and wars; however, the goal of investing in people and projects to make the world better has been going on since biblical times. Over the last 50 years, activists and investors have united and taken on many issues, such as labor practices, pollution, nuclear waste and apartheid in South Africa. We've also seen the socially responsible investing (SRI) category broaden to include environmental, social and governance (ESG) issues, with targeted investments called mission-related and program-related investments (MRI and PRI).

While we have a diverse client base and do not impose our social views on our investment strategy, we aim to build a close relationship with each client and to understand their investment goals, and any investments that they are not comfortable owning. Within equities, this could be a more volatile small cap stock, or a company in the packaged food industry. While many social and governance issues can be complex, we see the most interest in issues relating to the environment. Generally, the discussion starts with the energy sector, with some clients wanting a total divestment from the sector to others who are comfortable



with modest exposure to companies that are leaders in safety and who actively work with groups to minimize their impact to the environment. We also have access to extensive non-financial data on social and governance issues such as: product recalls, employee relations, workplace accident data, supply chain data and resource use, executive compensation and diversity. These are not primary factors in our analysis of a company, but they do help create the mosaic on understanding how the company operates and where risks may lie.

While we've touched on some of the ways we align equity portfolios to a client's value, we also can modify bond portfolios and introduce private investments that target a particular issue. We will be

periodically providing updates on these types of investments; please let us know if you have interest.

As always, thank you for entrusting us with your assets and enjoy the rest of the summer.

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