Third Quarter 2016

As we enter the Fourth Quarter of 2016 a few thoughts on the year so far, a discussion of the impact of the Presidential Election and some thoughts on future quarters.

Third Quarter 2016 Results

First, the third quarter ended with unusual complacency. In other words, a period of time, where major market indexes trade within a narrow range. Does this mean a new dynamic has entered the market? We think not and expect to see a return of volatility in the coming months. As we have written about in past letters, the market reacts in real time today as news, both positive and negative, enter the realm of knowledge. We don't see this changing in coming months.

Third quarter GDP looks to have risen by 2.1% per the Atlanta Fed's GDPNow forecast, which is not much better than the second quarter of 2016, 1.4% number. We continue in this low GDP growth and low inflation environment. As you look across the various economic reports, a majority support this projection for the third quarter of 2016. The markets were moved on a slightly negative jobs report on one day, while being supported by a positive report for manufacturing or oil the next day.

At the end of the quarter all major market indexes across the globe were positive except for the Global Real Estate Index. The best performing asset class this quarter was Emerging Markets, followed by International Developed Markets. Bond returns reflected actual cash yields from interest payments as rates across all maturities increased from June 30, 2016. Rates are still lower than September of 2015.

We include charts and graphs to further illustrate the performance results of major market indexes for the quarter and for longer periods of time. Please keep in mind that none of your portfolios look exactly like any index and we include these for information.

Impact of Presidential Election on Markets

The upcoming Presidential election is on the mind of everyone. We have received a number of phone calls and have had several discussions in recent meetings with some of you about what the potential impact of this election may have on the financial markets and your portfolios in general.

We have witnessed the candidates in two debates so far, and while the winner or loser is not part of our commentary, you must pay attention to what happens in the markets afterward. After the first debate, the snap polls conducted immediately following the debate, Hillary Clinton came out on top (CNN). For that matter, most professional pundits saw it the same way.

During the first debate, Dow Jones futures, which, among other things, is a gauge that gives us an idea how stocks will open the next day, rose by about 100 points (MarketWatch). The positive reaction extended into the next day, telling us that the professional investment community was pleased with Clinton's performance. The markets reacted in a positive manner after the second debate with all major indexes ending the day higher with almost no movement in interest rates.

As an observer who is interested in viewing the election only through the objective prism of the market (admittedly a very narrow prism), the professional investment community sees continuity in a Clinton win, even if some in the community are more likely to subscribe to the economic and tax ideas of a Republican.

It's that continuity that appeals to the desire for certainty. As we have mentioned many times in the past, short-term traders fear heightened uncertainty. It's the vagueness of some of Trump's ideas, coupled with his rhetoric, that fuels uncertainty. A Trump win in November could lead to a higher level of volatility for the short term.

In our charts and graphs section you will see a piece on Presidential Elections and the stock market created by Dimensional Fund Advisors for our use. As you can see all Presidents have both positive and negative results in the market regardless of the political party. The next President will be no different.

Let us also emphasize, short-term market volatility shouldn't determine how you and we vote in November. The nation faces much more pressing issues. We do, however, want to monitor important events that may create some ripples in the financial waters, even if those ripples are brief in nature. We anticipate seeing more of these ripples as we get closer to Election Day.

That leads to our next point. You've heard us reiterate time and time again: Markets go through choppy periods over the short term, but a disciplined approach is the straightest line to your financial goals. The last graph reflects the growth of the S&P 500 since 1926. The chart of performance indicates short term losses but long term the market value increases reflecting the growth in economic activity.

Your financial plan and therefore your investment strategy is based on your goals and short term movements in market, while creating worry, should not impact the success of your plan. As we have noted in prior letters trying to time the highs and lows in stocks is extremely difficult to do with any long-term success.

Future Predictions

As baseball great Yogi Berra was fond of saying, “It's tough to make predictions, especially about the future.” As with all predictions, this one is based on past events and the reading of indicators that may signal some change in the economy and earnings growth for US companies. At the end of the day, regardless of the politics, capitalism will make you money over time. It’s not that we can’t see some volatility if problems persist, but U.S. fundamentals, which have helped support shares during periods of recent volatility, remain intact.

The employment reports on Friday, October 7, 2016 indicated strong hourly wage growth that is positive in the long run for consumer spending which represents about two thirds of the economy. The economy added 167,000 private sector jobs in September, which was higher than the 144,000 in August. The unemployment rate remains at 5%. Overall, we continue to see a growing number of people working in the private sector.

The Federal Reserve has pushed the potential of another rate increase to the fourth quarter, so we will once again see the volatility return associated with this decision.

Earnings will take the forefront for the next few weeks. We have had five consecutive quarters of declining earnings and the result is the market in general is now fully valued based on historical data and all known information. If this market is to move forward, earnings growth must come to the front and reflect meaningful increases.

We hope you’ve found this review to be educational and helpful. Our goal is to provide an overview of recent and current events. Your own individual financial plan is what’s most important to you not the day to day movements in markets. If you have any questions, please contact us. We look forward to seeing many of you in the coming months.

Quintin and Ginny
October 11, 2016

Market Summary

Index Returns Ending September 30, 2016

3Q 2016	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
	STOCKS				BONDS	
	4.40%	6.29%	9.03%	-0.23%	0.46%	0.10%

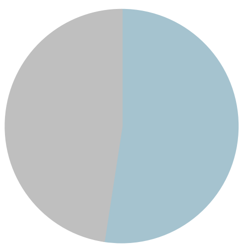
Since Jan. 2001	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
Avg. Quarterly Return	1.8%	1.4%	3.0%	2.8%	1.3%	1.2%
Best Quarter	16.8% **Q2 2009**	25.9% **Q2 2009**	34.7% **Q2 2009**	32.3% **Q3 2009**	4.6% **Q3 2001**	5.5% **Q4 2008**
Worst Quarter	-22.8% **Q4 2008**	-21.2% **Q4 2008**	-27.6% **Q4 2008**	-36.1% **Q4 2008**	-2.4% **Q2 2004**	-3.2% **Q2 2015**

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond ex US Market (Citigroup WGBI ex USA 1−30 Years [Hedged to USD]). The S&P data are provided by Standard & Poor's Index Services Group. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. Bloomberg Barclays data provided by Bloomberg.

Stock Market Period Returns

Ending September 30, 2016

World Market Capitalization—US



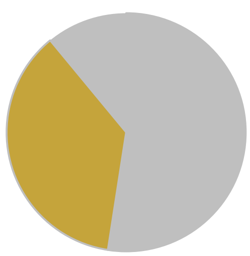
52%
US Market
$22.6 trillion

Period Returns (%)

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Marketwide	8.18	14.96	10.44	16.36	7.37
Large Cap	7.84	15.43	11.16	16.37	7.24
Large Cap Value	10.00	16.20	9.70	16.15	5.85
Large Cap Growth	6.00	13.76	11.83	16.60	8.85
Small Cap	11.46	15.47	6.71	15.82	7.07
Small Cap Value	15.49	18.81	6.77	15.45	5.78
Small Cap Growth	7.48	12.12	6.58	16.15	8.29

** Annualized*

World Market Capitalization—International Developed



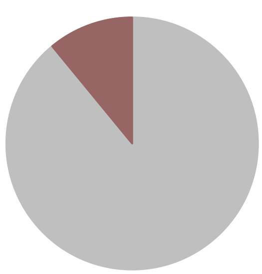
37%
International Developed Markets
$15.8 trillion

Period Returns (%)

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	3.12	7.16	0.33	6.89	1.88
Small Cap	7.26	13.50	4.15	9.72	4.11
Value	2.64	4.87	-1.69	5.64	0.66
Growth	3.61	9.42	2.30	8.08	3.04

** Annualized*

World Market Capitalization—Emerging Markets



11%
Emerging Markets
$4.7 trillion

Period Returns (%)

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	16.02	16.78	-0.56	3.03	3.95
Small Cap	9.08	12.65	1.29	4.72	5.97
Value	16.18	14.50	-3.00	0.79	3.77
Growth	15.84	18.92	1.81	5.19	4.03

** Annualized*

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Fixed Income

Third Quarter 2016 Index Returns

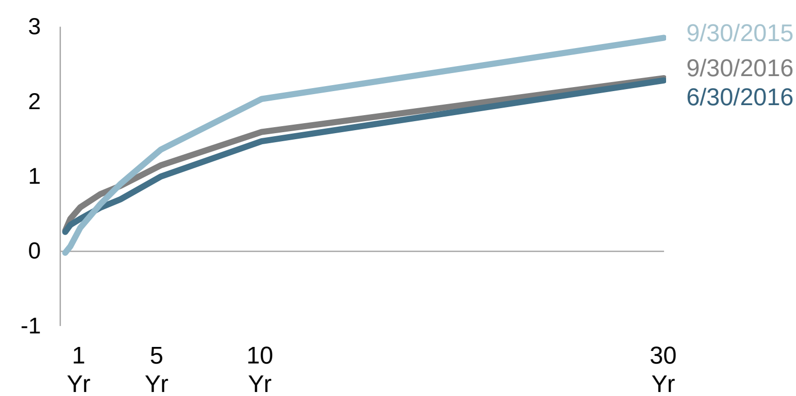
Interest rates across the US fixed income markets generally increased during the third quarter. The yield on the 5-year Treasury note rose 13 basis points (bps) to end at 1.14%. The yield on the 10-year Treasury note increased 11 bps to 1.60%. The 30-year Treasury bond increased 2 bps to finish with a yield of 2.32%.

The yield on the 1-year Treasury bill rose 14 bps to 0.59%, and the 2-year Treasury note yield increased 19 bps to 0.77%. The yield on the 3-month Treasury bill increased 3 bps to 0.29%, while the 6-month Treasury bill increased 9 bps to 0.45%.

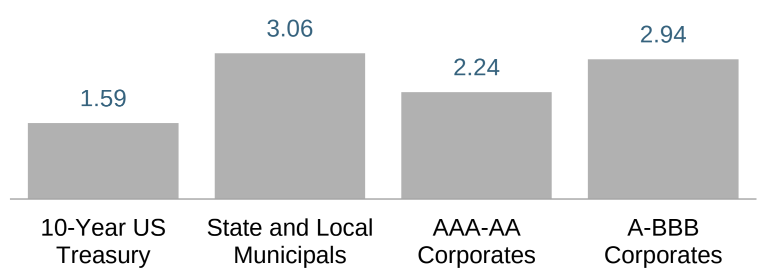
Short-term corporate bonds gained 0.32%. Intermediate-term corporates rose 0.89%, while long-term corporate bonds gained 2.56%.[1]

Short-term municipal bonds returned -0.21%, while intermediate-term municipal bonds were unchanged. Revenue bonds slightly outperformed general obligation bonds.[2]

US Treasury Yield Curve (%)



Bond Yields across Issuers (%)



Period Returns (%)

* Annualized

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
BofA Merrill Lynch 1-Year US Treasury Note Index	0.71	0.54	0.35	0.33	1.53
BofA Merrill Lynch Three-Month US Treasury Bill Index	0.24	0.27	0.12	0.10	0.92
Citigroup WGBI 1-5 Years (hedged to USD)	1.98	1.89	1.70	1.60	2.78
Bloomberg Barclays Long US Government Bond Index	14.61	13.02	11.07	5.48	7.97
Bloomberg Barclays Municipal Bond Index	4.01	5.58	5.54	4.48	4.75
Bloomberg Barclays US Aggregate Bond Index	5.80	5.19	4.03	3.08	4.79
Bloomberg Barclays US Corporate High Yield Index	15.11	12.73	5.28	8.34	7.71
Bloomberg Barclays US TIPS Index	7.27	6.58	2.40	1.93	4.48

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Presidential Elections and the Stock Market

Third Quarter 2016

Next month, Americans will head to the polls to elect the next president of the United States. While the outcome is unknown, one thing is for certain: There will be a steady stream of opinions from pundits and prognosticators about how the election will impact the stock market.

As we explain below, investors would be well-served to avoid the temptation to make significant changes to a long-term investment plan based upon these sorts of predictions.

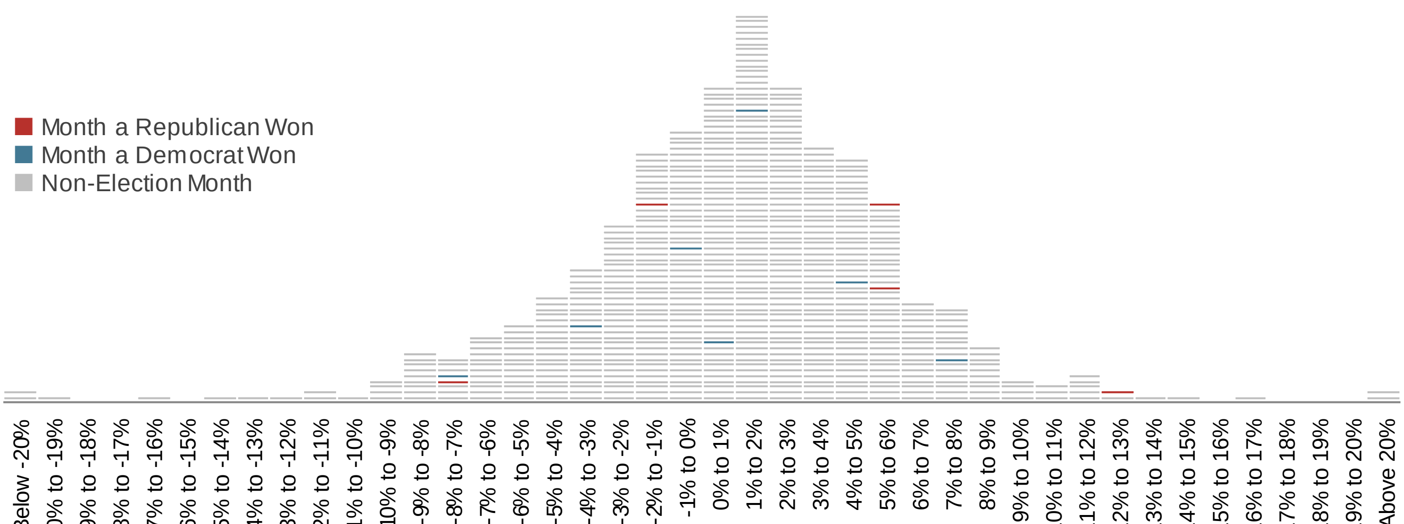
Short-Term Trading and Presidential Election Results

Trying to outguess the market is often a losing game. Current market prices offer an up-to-the-minute snapshot of the aggregate expectations of market participants. This includes expectations about the outcome and impact of elections. While unanticipated future events—surprises relative to those expectations—may trigger price changes in the future, the nature of these surprises cannot be known by investors today. As a result, it is difficult, if not impossible, to systematically benefit from trying to identify mispriced securities.

This suggests it is unlikely that investors can gain an edge by attempting to predict what will happen to the stock market after a presidential election.

Exhibit 1 shows the frequency of monthly returns (expressed in 1% increments) for the S&P 500 Index from January 1926 to June 2016. Each horizontal dash represents one month, and each vertical bar shows the cumulative number of months for which returns were within a given 1% range (e.g., the tallest bar shows all months where returns were between 1% and 2%). The blue and red horizontal lines represent months during which a presidential election was held. Red corresponds with a resulting win for the Republican Party and blue with a win for the Democratic Party. This graphic illustrates that election month returns were well within the typical range of returns, regardless of which party won the election. *(continues on page 16)*

Exhibit 1. Presidential Elections and S&P 500 Returns Histogram of Monthly Returns, January 1926–June 2016



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Presidential Elections and the Stock Market

Continued from page 15

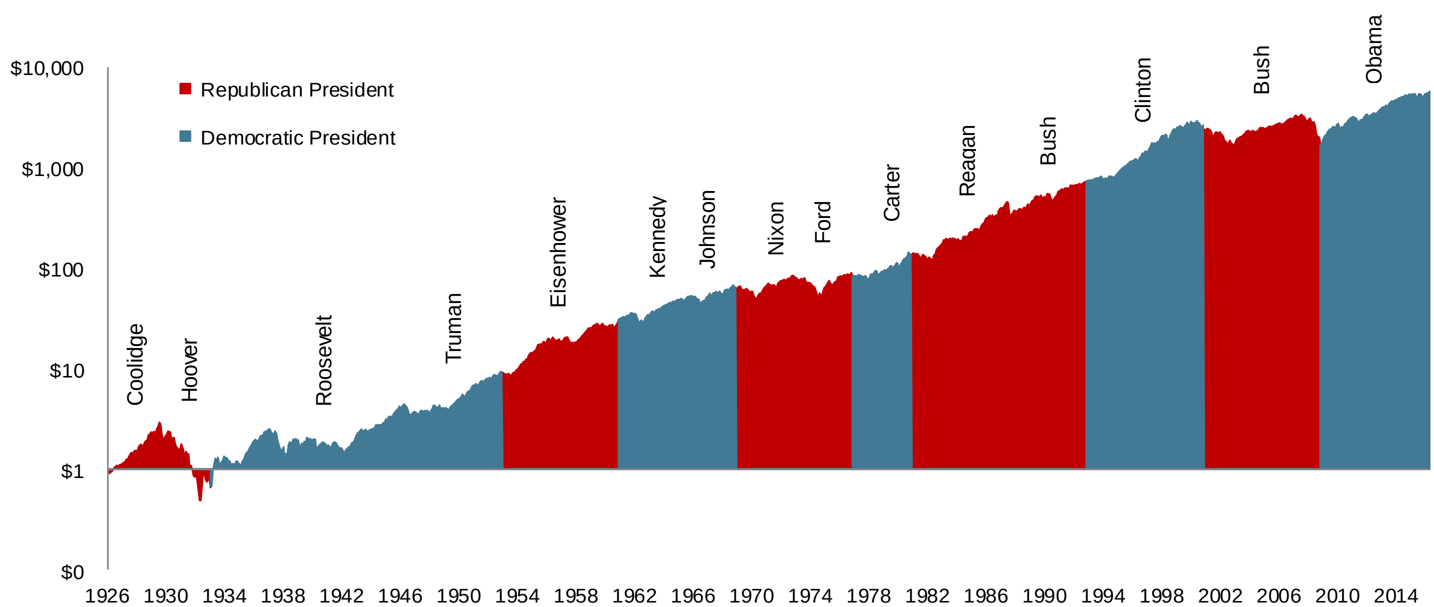
Long-Term Investing: Bulls & Bears ≠ Donkeys & Elephants

Predictions about presidential elections and the stock market often focus on which party or candidate will be "better for the market" over the long run. **Exhibit 2** shows the growth of one dollar invested in the S&P 500 Index over nine decades and 15 presidencies (from Coolidge to Obama). This data does not suggest an obvious pattern of long-term stock market performance based upon which party holds the Oval Office. The key takeaway here is that over the long run, the market has provided substantial returns regardless of who controlled the executive branch.

Conclusion

Equity markets can help investors grow their assets, but investing is a long-term endeavor. Trying to make investment decisions based upon the outcome of presidential elections is unlikely to result in reliable excess returns for investors. At best, any positive outcome based on such a strategy will likely be the result of random luck. At worst, it can lead to costly mistakes. Accordingly, there is a strong case for investors to rely on patience and portfolio structure, rather than trying to outguess the market, in order to pursue investment returns.

Exhibit 2. Growth of a Dollar Invested in the S&P 500, January 1926–June 2016



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Source: Dimensional Fund Advisors LP.

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