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A LETTER FROM THE CEO

R. THOMAS MANNING, CFA, CHIEF EXECUTIVE OFFICER AND PRESIDENT

Given the turbulence that marked 2016, it may not have felt like a year where equities posted their eighth consecutive year of gains. That said, stocks closed higher in December than they opened in January, as they have done in every year since 2009. Amidst the action, moves in bond yields may have also signaled the end of the decades-long bull market for bonds. Needless to say, it was an eventful year.

2016 began with a significant swoon in stocks fueled in part by growth concerns in China. Compounding matters, the Federal Reserve (the Fed) was expected to raise short-term interest rates as many as four times during the year. By mid February, global equities had entered bear market territory. U.S. markets had fallen to levels not seen since the spring of 2014.

Things turned around for equities as the year ground on, however. The Fed, as we now know, failed to raise rates until its most recent meeting in December. The first three quarters of the year were rife with excuses for the Fed to remain on the sideline: market declines, the surprise Brexit outcome, and the U.S. presidential election chief among them. Not until December, with the election in the rearview mirror and the stock market on solid ground, did a rate rise become reality. The Fed's delays, coupled with major changes in global bond markets, provided breathing room for further gains in stocks.

Indeed, 2016 saw remarkable moves in the fixed income markets (particularly the U.S. Treasury market) creating a level of scrutiny and conversation normally reserved for the gyrations of the stock market. The yield on the 10-year Treasury note (T-Note), to which many key interest rates are pegged, started the year at 2.26% and immediately began a precipitous descent, mirroring the decline in global equities. Reaching a low of 1.65% on February 11th, the yield on the T-Note hovered between 1.65% and 1.98% until mid June as investors eyed the impending Brexit referendum. In the days immediately following the surprise "Leave" result, the yield fell to 1.35%, marking the lowest level on record.

As the world began to digest the implications of Brexit, yields began to inch higher. By the time the U.S. began to tally the results of the presidential election, the yield on the T-Note stood at 1.85%. Since then, yields have skyrocketed, ending the year at 2.49%, almost twice their summer lows.

While the initial steady descent of interest rates in the United States was stunning, it paled in comparison to what was occurring in the rest of the world. Japan, along with a majority of European nations, saw interest rates plunge into unprecedented negative territory – with *investors* paying *banks* to hold deposits. While rates have recovered to a certain extent, they remain negative to this day in many parts of the world. Rates this low are hardly a sign that "all is well" with the global economy.

MARKET INSIGHT

Looking forward, we remain cautiously optimistic that markets can continue to move higher in the year ahead. The U.S. economy is showing signs of improvement, the job market continues to grow stronger, and economic growth rates appear to be accelerating – not only in the United States, but around the world as well. If these trends continue, we expect higher corporate profitability and potentially higher stock prices. However, much of this optimism is already built into U.S. stock prices today; we expect that at some point in the early part of next year, the market may pause for air or give back some of the gains we have seen since the U.S. presidential election.

As U.S. valuations have continued to rise, we have become increasingly interested in overseas opportunities. International equity valuations trade at more reasonable levels, meaning that even small gains in corporate profitability could lead to outsized returns relative to U.S. counterparts. As a result of consistent U.S. outperformance relative to emerging and developed markets, we have invested client assets largely within the confines of the U.S. for the better part of the last decade. This year, we will continue to monitor global trends for tactical investment opportunities on an international scale. The dollar's strength will undoubtedly ebb at some point during the course of the New Year; such a pullback could present a good entry point into international markets for our clients.

Given indications of multiple interest rate increases from the Fed in 2017, paired with other headwinds for fixed income investors related to fiscal policy, we will remain very conservative in positioning bond portfolios. As we have anticipated rising rates for quite some time, we are in a good position to take advantage of opportunities as they unfold. Consistently rising rates would most certainly be a very welcome change for those who rely on the income generated from their portfolios.

On a personnel note, we will be off to a busy start in 2017. Abby Psychogeos will join us as Private Client Advisor, initially operating out of our Wellesley office, and relocating to Portland in the spring. Matt Migliozi joins us as a Due Diligence Analyst working with our investment team and is located in Wellesley, and Jacqui Borukhov joins us as an Account Officer, also in Wellesley. Please join me in welcoming them to the team.

Thank you for your continued confidence in F.L.Putnam. On behalf of our staff, I wish you a very healthy and happy 2017.

2016 MARKET DIARY

U.S. Equities	Last 3 Months	Last 12 Months *
S&P 500	3.82%	11.95%
Dow Jones Industrials	8.66%	16.50%
Russell 2000	8.82%	21.28%
Russell 3000	4.20%	12.72%
International Equities		
MSCI World Index ex-US	-0.31%	3.29%
MSCI Emerging Markets	-4.31%	11.27%
Fixed Income		
Barclay's U.S. Int. Gov't/Corporate	-2.07%	2.08%
Barclay's U.S. High Yield	1.75%	17.13%

Source: Bloomberg Capital Markets

* Includes dividends for equity indices

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