

July, 2016

2016 Second Quarter Update

Review: Domestic equities rose 2.5% primarily due to price/earnings multiple expansion from falling interest rates. Developed international equity markets fell 1.2% in U.S. dollar terms when Britain passed its referendum to leave the European Union (“Brexit”), raising investor concerns about negative economic impacts. Emerging market returns were essentially flat. Softer Chinese economic growth was offset by stronger growth in India. Domestic taxable bonds returned 2.2% and municipal bonds 2.7% due to diminishing expectations for Federal Reserve rate hikes this year and, in the case of U.S. Treasuries, the relative attractiveness of U.S. yields to foreign buyers.

Period	2Q16	1Q16	4Q15	2015
S&P 500	2.5%	1.4%	7.0%	1.4%
EAFE*	-1.2%	-3.0%	4.7%	-0.8%
Emerging Markets	0.8%	5.7%	0.7%	-14.9%
Barclays U.S. Aggregate Bond	2.2%	3.0%	-0.6%	0.6%

*Europe, Australia, Far East

Domestic Economy: First quarter U.S. GDP growth (the most recent federal data available) slowed to 1.1% versus 1.4% in the fourth quarter of 2015. Personal consumption expenditures and state and local spending rose while fixed investment and federal spending fell. Second quarter GDP is currently tracking closer to 2.5% based upon improving retail sales and strengthening manufacturing data. Employment continued to rise in the quarter with a 3-month average gain of 147,000 jobs. Though lower than the 209,000 average for the first quarter, it is not unusual for the mature stage of our current economic cycle.

For 2016, we expect the U.S. economy to grow 1.8%-2.2% with 2% average growth in the second half. Private consumption expenditures and residential investment should remain firm whereas cautious business spending and softer exports due to a strong U.S. dollar will be headwinds. Overall, inflation should remain at or below 2% this year; however, underlying rising healthcare and housing costs will continue to push total inflation higher and impact consumer discretionary purchases.

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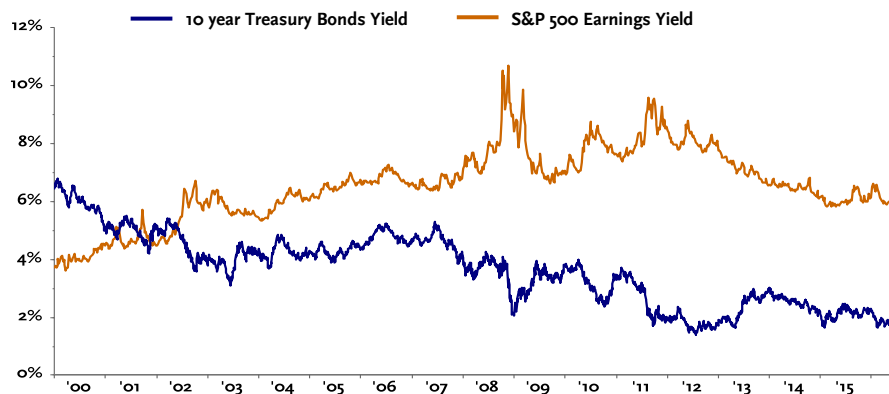


International Economies: We expect subdued European growth of 1.4-1.6%, hindered by structurally high unemployment of 10% and uncertainty over Brexit's economic impact. Japan's growth should remain at approximately 1% as monetary stimulus still fails to boost sustainable consumer spending. Emerging economies growth, though relatively better at 4%, will be at risk of slowing due to export weakness from decelerating growth and a strong U.S. dollar.

Strategy: In general, we expect market volatility to remain elevated due to economic, monetary and political uncertainty. Given recent price/earnings multiple expansion, domestic equity prices will need to be validated by earnings growth, especially in the telecom and utility sectors where current record low interest rates have potentially overvalued their future stream of dividends.

Bond yields are unattractive as global central bank buying continues to drive U.S. rates lower-in many cases below both current and expected long term inflation. We continue to utilize LIBOR-based floating rate notes as a hedge against the eventual rise in rates.

As shown in the chart below, the recent fall in interest rates is also reflected in a lower S&P 500 earnings yield, which is the inverse of a higher price/earnings multiple. The pronounced gap between the two continues to favor equities over bonds.



Source: FactSet Research Systems

Our investment strategy emphasizes companies with attractive and sustainable business models, strong managements, and solid balance sheets that can deliver steady secular earnings growth at attractive valuation levels. This approach requires discipline and patience in the current volatile market environment. We continue to overweight the healthcare and information technology sectors where underlying, long term fundamentals remain positive and selective valuations reasonable.