Quarterly NEWSLETTER

FALL 2014

Commonwealth Bank & Trust Company

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Volatility, Pullbacks, Rebounds & Rallies...

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Chart 1

Q3 2014 Market Performance – Total Returns

	9.30.14 Level	Q3	YTD
Dow Jones	17043	1.29%	2.81%
S&P 500	1972	1.13%	8.34%
NASDAQ Composite	4493	2.24%	8.58%
Russell 2000	1102	-7.36%	-4.40%
S&P Midcap	1371	-3.99%	3.19%
Russell 1000 Growth	921	1.49%	7.89%
Russell 1000 Value	985	-0.19%	8.07%
MSCI EAFE	1972	-5.74%	-0.79%
	Yield	Q3	YTD
Barclays Municipal	2.19	0.75%	3.75%
Barclays Aggregate	2.36	0.17%	4.10%
Barclays High Yield	6.13	-1.92%	3.61%

Market volatility re-emerged during the third and early fourth quarter as a host of issues around the world (anemic global growth, Euro deflation-recession threats, Ebola, ISIS, Ukraine, etc...) caused institutional investors to hit the sell-sell-sell button while others were quick to seize on the dips as opportunities to buy- buy- buy, thus buoying markets. The resulting sharp swings in index value and magnified volume show the current fragile but resilient sentiment. The S&P 500 finished the quarter up 1.13% while the Dow finished with a 1.29% increase despite a weak September, which cut the quarter's gains at least in half. International markets, further weakened by political and economic worries in Europe and Asia, fared significantly worse than U.S. markets with the MSCI EAFE Index down 5.74% for the quarter and the MSCI Emerging Markets index down 4.33% as China's growth continued to slow.

While September closed the third quarter on a weak note, October brought the stock market's deepest pull back in several years with the Dow dropping more than 1,000 points from its record high set in mid-September and the S&P seeing its worst performance since November 2011 before once again rebounding. Although investors remain concerned that slower global growth could hinder the U.S. recovery and the surging U.S. dollar could jeopardize corporate profits and exports, the U.S. markets remain the best option for capital flows. The U.S. economy continues to show positive signs with rising auto sales and home prices, increasing consumer confidence, an improving job market, upward revision of second quarter GDP from 4.2% to 4.6%, and 3rd quarter GDP registering a preliminary rate of 3.5%.

Outlook for GDP and Inflation

Forecast	Real GDP		Headline Inflation	
	2014	2015	2014	2015
United States	2.2%	3.0%	1.7%	1.4%
Eurozone	0.7%	1.0%	0.5%	0.8%
United Kingdom	3.1%	3.0%	1.5%	1.5%
Japan	0.9%	1.1%	2.8%	1.7%
China	7.4%	7.2%	2.2%	2.5%
BRICS*	5.5%	5.9%	4.0%	4.0%
World**	3.0%	3.5%	3.5%	3.3%

Current data for real GDP and inflation four quarters ending Q2 2014
**BRICS = Brazil, Russia, India, China & South Africa*
***World is weighted average sum of countries in Golman Sachs private economic forecasts*
Source: Goldman Sachs

The S&P 500 increased 8% during the first nine months of the year with healthcare (17%) taking the lead from utilities (14%) during the third quarter. Information technology stocks (14%) continued to rally as capital spending steadily picked up. Additionally, healthcare and utilities are benefitting from a strong dollar, which is up 7% through September against a basket of currencies. The stronger dollar, seasonality and production surpluses sank energy stocks (-9%) during the quarter. Bonds have rebounded this year after losing money in 2013. The 10-year

(continued on back page)

Proprietary Performance Results

	3rd Quarter	1 Year	3 Year	5 Year	Since Inception
Focused Equity Fund [2]	1.34%	18.87%	19.65%	15.23%	16.78%
Aggressive Growth Fund [1,3]	-1.06%	12.02%	21.37%	15.61%	9.04%
Science/Technology Fund [4]	4.06%	23.17%	21.53%	14.23%	7.91%
S&P 500	1.13%	19.69%	22.94%	15.67%	17.03%[2], 9.81%[3], 7.33%[4]
Russell 2000	-7.35%	3.93%	21.24%	14.26%	16.31%[2], 7.74%[3], 5.78%[4]
MSCI EAFE	-5.74%	4.93%	14.39%	7.27%	11.21%[2], 2.90%[3], 3.75%[4]
Strategic Income Fund [5]	0.45%	12.93%	13.02%	10.91%	11.93%
60% Russell 3000 Val / 40% Barclay Agg	-0.44%	12.09%	14.92%	10.89%	11.57%

There is no assurance that any of these investment strategies will meet its investment objective. Performance results for each strategy are computed on the strategy's overall returns. Each strategy and index includes the reinvestment of dividends. Past performance does not guarantee future results. Current performance may be lower or higher than the performance results quoted. ***[1]*** *Net of management fees; performance results of SMC Capital and/or its principals as advisor from inception to 2/28/06 and as sub-advisors to CBandT since 3/1/06.* ***[2]*** *Inception date 12/31/2008.* ***[3]*** *Inception date 7/1/1989.* ***[4]*** *Inception date 3/31/2006.* ***[5]*** *Inception date 12/31/2008.*

Fixed Income

In October, the Federal Reserve ended its third round of quantitative easing (QE) announced in Sept. '12 and tapered asset purchases at both FOMC meetings again this quarter. The Fed's balance sheet grew by roughly $1.5 trillion during this period. To reduce market volatility, the Fed disclosed plans to normalize the balance sheet at the end of its Sept. meeting. Fed Chair Yellen said "it would take until the end of the decade to achieve" normal balance sheet levels. Committee guidance on the funds rate for '15 is mostly in the range of 1-2% while the futures market suggests rates will be lower for longer.

Previously, we pointed out the relative value of U.S. Treasury rates vs. other countries, particularly European. During the quarter, global U.S. bond investors were rewarded as the U.S. dollar rose nearly 8% against other major currencies. A stronger dollar helps keep inflation down by reducing the cost of imported goods and makes our markets more attractive to foreign investors. But, in a globally diversified portfolio, a rising dollar may mean more risk and lower returns from foreign bond holdings. These factors were evident within global bond market performance. Broad U.S. investment-grade indices finished the quarter slightly positive while foreign bonds struggled. The Citigroup World Gov't Bond Index (including U.S.) lost nearly 4% during the quarter. U.S. fixed income returns are roughly 4% for both trailing 12-mos and YTD before any currency adjustments. In this environment, where U.S. dollar outperformance is largely the result of expected central bank policy differentials and economic performance, short to intermediate-term debt will likely struggle, resulting in a flatter yield curve.

The low rate/default environment has benefited the high-yield bond market. Earlier this year we lowered our high-yield ranking due to valuations. Our call was validated again as investment-grade credit outperformed high-yield with returns of 0.0% vs.-1.9%. We have remained positive on emerging market bonds which have held up reasonably well. The iShares JPM US Emerging Markets Bond ETF (EMB) returned -1.2% during the quarter and 7.3% in '14. Local currency based funds had a difficult quarter given the U.S. dollar strength.

Municipal bonds continued to rally, returning 1.6% according to the BofA ML index and are up 8.3% in '14. This more than offset last year's -2.9% return. Long-term bonds (22+ yrs) were up 2.5% for the quarter and are up 13.1% in '14. We are not surprised by the recovery. In January, we wrote "We believe that the soon to be apparent higher tax rates (including the new 3.8% Medicare Tax) and projected net negative supply should provide some tailwinds this year. In addition, historical yields vs. Treasuries (often converted into ratios) are attractive." Given this strength, we now consider municipals slightly overvalued.

In general, we continue to recommend a tactical underweight to core fixed income in favor of absolute-return-oriented and other alternative strategies.

Focused Equity

For the quarter, the strategy was up 1.34% versus 1.13% for the S&P 500 Equity Index. Since inception, the strategy narrowly trails the benchmark's return of 17.03% by 0.25% with a gain of 16.78%. Year-to-date (YTD) and twelve month trailing returns are 8.68% and 18.87%, respectively versus 8.33% and 19.69% for the S&P 500. The strategy has a beta of 0.79, so we anticipate that it will lag in strong up markets and outperform in corrections. On a risk-adjusted basis, the results continue to be strong. The strategy has generated an annualized 2.49% alpha for the last five years. The risk adjusted return for Focused Equity would be 18.63%, if it took the same level of risk as the S&P 500.

Intel (INTC)
6/1/2014 – 9/30/2014

The top 4 performers for the quarter were also the top 4 for the year returning between 9% and 13% in 3Q14 and between 22% and 57% for the last 12 months. Apple's (AAPL) new iPhone 6 and 6+ record early sales indications sent Apple shares 9% higher in 3Q14. Intel (INTC) continued to rally during the quarter (+13%) buoyed by corporate PC refreshes after Microsoft discontinued support of Windows XP forcing conversion to Windows 7, which requires more advanced processors. Microsoft (MSFT) continued its march higher in the quarter (+12%) into October as new CEO, Satya Nadella, repositions the company as a leader in enterprise cloud systems and services. Our largest holding (7.3%), Berkshire Hathaway's (BRK.B) 9% return after releasing better than expected results in early August, made the largest contribution to the portfolio in 3Q14.

Energy companies were the biggest collective drag on the Focused Equity strategy during the quarter as oil prices fell to four year lows by mid-October. We are underweight energy (8% vs. 10%) in the portfolio. Collectively, Spectra Energy (SE), National Oilwell Varco (NOV) and Transocean (RIG) were only a -0.58% drag on the portfolio. Potash and salt producer, Compass Minerals (CMP) was off -11% in the quarter on weak potash forecasts. Also underperforming was Qualcomm (QCOM, –5%), as it and other U.S. tech companies are facing monopoly inquiries by Chinese regulators.

Strategic Income Builder

For the third quarter of 2014, the strategy was up 0.45%, again beating its blended benchmark return of -0.44%. Since inception, the SIB strategy has returned an annualized 11.93%, slightly ahead of its benchmark return of 11.57%. The yield (income) from the strategy has consistently exceeded that of its benchmark, which is comprised of a 60% weighting to the Russell 3000 Value Index and 40% to the Barclay's Aggregate Index. The success of the fund is the result of an attractive mix of income producing securities, exposure to global markets and tactical allocation. Since its inception (1/1/09), the strategy has generated a positive alpha of 2.06% annualized with a beta of 0.84.

Quarterly equity performance of +0.9% compares positively to the Russell 3000 Value's return of -0.9%. Previously out-of-favor consumer names such as Kohl's (KSS, +16.9%) and Darden Restaurants (DRI, +12.5%), which we have discussed at length, performed well during the quarter. In addition, "old tech" names like Intel (INTC +13.4%) and Microsoft (MSFT, +11.9%) were top performers.

We attribute Intel's solid performance in the third quarter to its second quarter earnings beat and promising outlook. Management provided good news during its June earnings call that adjusted earnings per share were $0.56, which was sharply above the prior-year result of $0.40. INTC prospered from a strategy to broaden its reach from data centers to PCs to the Internet of Things. It appears on track to reach its objective of 40 million tablets sold, while the ramp of its Baytrail SoC (system on a chip) is another reason for optimism. Overall, increases in the PC Client Group and Data Center division helped to offset a decrease in the Communications segment.

Energy (-8.6%) was by far the worst sector with respect to quarterly performance given declining oil prices. Though a small position, Transocean Ltd. (RIG -27.6%) was the worst performing stock held by the strategy. It continues to pay its $0.75 quarterly paid-in capital distributions for an indicated yield of roughly 10%. This position was recently doubled to potentially capture capital losses within the position.

One Fixed Income/Alternative position of note was the recently purchased DoubleLine Total Return Bond Fund (DBLTX), which was up 0.8% vs. 0.2% for the Barclays Aggregate. This fund is a notable choice for those exiting PIMCO Total Return Fund (PTTRX -0.4%) or PIMCO Unconstrained Bond Fund (PFIUX +0.2%) due to the Bill Gross departure news. PIMCO All Asset All Authority (PAUIX -3.8%) managed by Rob Arnott of Research Affiliates is an alternative position within the strategy. This PIMCO fund of funds had limited exposure to Bill Gross funds. Credit related & emerging market funds struggled during the third quarter. This includes Loomis Sayles Bond Fund (LSBDX -1.8%), T. Rowe Price High Yield Fund (PRHYX -1.5%) and T. Rowe Price Institutional Emerging Markets Bond (TREBX -1.6%).

Science & Technology Strategy

The Science & Technology strategy's 4.06% 3Q14 return lagged the S&P Information Technology and Healthcare sector results of 4.77% and 5.46% respectively, but beat Telecom sector results of 3.07%. It also trailed the Nasdaq

100 return of 5.52%, but beat and the broader the Nasdaq Composite return of 2.24%. The Science and Technology Strategy is solidly beating its closest benchmark proxy, the Lipper Science & Technology index, which was 0.51% for 3Q14. Year-to-date (YTD) and twelve month trailing returns are 10.80% and 23.35%, respectively. YTD and 12 month returns were 13.80% and 27.50% for the Nasdaq 100, while the Lipper Science & Technology index returned 6.86% and 17.89% for the Lipper Science & Technology index.

Neither the Nasdaq 100 index nor the Nasdaq Composite is a pure-play technology index as consumer product companies comprise about 15% of the Nasdaq 100 and about 20% of the Nasdaq Composite, while the Composite also has about 7% allocated to financials. A little over 90% of the difference in performance for the YTD period and over 100% of the difference for the 12 month period was a lower allocation in the Sci Tech fund vs. the Nasdaq 100 to Apple (9% vs. 13%) and Microsoft (2% vs. 8%). Both stocks are up over 25% YTD and over 40% for the 12 month period.

Medivation Inc. (MDVN)
6/1/2014 – 9/30/2014

Leaders: Gilead (GILD) rebounded 28% during 3Q14 as it became apparent its controversial $84,000 per treatment cycle Hepatitis C drug, Solvaldi and its reconstituted replacement, Harvoni, will become the first line of treatment and will be covered by most healthcare payors. The FDA approved Medivation's (MDVN) prostate cancer drug, Xtandi, sending the stock 28% higher in the quarter. Apple (AAPL +9%), eBay (EBAY +13%) and Facebook (FB +17%) were the largest contributors in technology. Apple's new iPhone 6 and 6+ record early sales indications sent Apple shares higher. As anticipated, eBay announced it would unlock value by spinning off its PayPal internet payment unit. Facebook demonstrated its mobile app may enable it to dominate the fastest-growing mobile advertising space.

Laggards: Consumer electronics makers Harman International (HAR) and iRobot (IRBT) were the biggest detractors for 3Q14, down 8% and 26%, respectively. Concerns that a global slowdown would hurt auto sales hurt Harman, while concerns that Dyson may release a robotic vacuum for Christmas sank our small position in iRobot. The portfolio returns were reduced by large positions in aerospace alloy producer, Precision Castparts (PCP -6%), mobile chipmaker Qualcomm (QCOM -5%). A stronger dollar and weak European demand slowed Precision Castparts sales. Qualcomm and other U.S. tech companies are facing monopoly inquiries by Chinese regulators.

Small Cap Composite

The Small Cap Value Composite returned -6.59% for the third quarter of 2014, versus -7.35% for the Russell 2000 index.

A top contributing holding in the Portfolio during Q3 was Blackhawk Network Holdings Inc. (Cl A) (HAWK, +15%), a prepaid payment network that offers a broad selection of gift cards and payment services at over 180,000 retail locations. In late September, HAWK signed a deal to acquire Parago Inc., a provider of rebates, incentives, and promotional solutions. The acquisition is expected to yield significant cost synergies using HAWK's platform as well as provide revenue synergies through content and distribution upsell opportunities. For the second consecutive quarter, private prison operator GEO Group Inc. (GEO, +8%) delivered solid quarterly earnings and increased its full-year AFFO (Adjusted Funds From Operations) guidance to reflect improved occupancy rates and the reactivation and expansion of several federal facilities. Another positive contributor during the quarter was White Mountains Insurance Group Ltd. (WTM, +4%), a specialty commercial and property insurer through its 75% ownership in OneBeacon (ticker: OB) and a global reinsurer through its ownership of Sirius Group. The company's Q2 results featured another quarter of steady premium growth and a sequential +1.7% increase in book value.

GEO Group Inc. (GEO)
6/1/2014 – 9/30/2014

A large negative contributor to performance in Q3 was Ascena Retail Group Inc. (ASNA, -22%), operator of dressbarn, maurices, Justice, Lane Bryant, and Catherines specialty apparel stores throughout the United States. ASNA reported disappointing fiscal Q4 results driven by a difficult competitive environment at Justice as well as poor merchandising decisions at Lane Bryant, driving an overall same-store sales decline of -4%. Another poor performer during the quarter was Miller Energy Resources Inc. (MILL, -31%), an independent oil and gas exploration and production company with operations in Alaska's Cook Inlet Basin. Despite receiving an improved third party reserve report during the quarter, Miller's stock fell from declines in global oil prices and a delayed announcement of operational results from an offshore well. Late in the quarter, MILL announced significant leadership changes that will bring institutional oil and gas experience to both its board of directors and management team, including a new CEO. Another negative contributor was Rovi Corp. (ROVI, -18%), a provider of interactive program guides to cable/satellite TV operators, consumer electronics manufacturers, and over-the-top distributors. Despite reporting Q2 results above expectations in late July, the stock drifted lower in the latter half of Q3 on concerns that customer consolidation (specifically Comcast/Time Warner Cable and AT&T/DirecTV) could delay some key contract renewals.

Kentucky Municipals

Quarterly bond issuance by Kentucky municipalities decreased to $359 million from $933.1 million (52 issues) which is typical during the third quarter. New issue size was also down averaging just $6.9 million. Bank-qualified "BQ" issuance was only $68 million or 19% while non-BQ issuance was $271 million or 76%. For our clients, we tend to utilize non-BQ bonds because yields are typically higher. Taxable issuance was $19 million or 5%. There was no AMT-subject issuance during the quarter. However, we are purchasing more of these bonds as our typical client is not impacted by the alternative minimum tax (AMT). Trading levels are more difficult to determine given the light issuance.

During the quarter, our 10-year Kentucky tax-exempt yield target fell just 0.05% to 2.75%. Our 15-year yield target fell 0.15% to 3.25% during the quarter.

Puerto Rico (PR) continues to be uneventful. PR bonds are widely held particularly in mutual funds due to their tax-exemption in all states. Given the higher yields available, they are quickly becoming a favorite of hedge funds and private capital. With the heightened liquidity, it appears PR will not spark a municipal market correction in the foreseeable future. In our portfolios, we have avoided this debt ridden territory other than escrowed bonds. Recently, PR's Senate approved selling as much as $1.2 billion of notes. This would be their first borrowing after enacting a law allowing some public agencies to restructure debt. The sale will gauge demand for the junk-rated securities as its leaders attempt to turn around a struggling economy. Officials said at least three-quarters of the sale may be privately placed.

We continue to think intermediate bonds are the most attractive part of the market, particularly given recent yield curve changes. Our bias remains defensive coupons of 4% or greater with a focus on premium callable municipals sometimes referred to as "cushion" or "kicker" bonds. Our performance themes continue to evolve around "rolling the steep yield curve" and opportunistic buying/selling within a somewhat volatile market. We continue to evaluate portfolio positioning, balancing risk/reward in a manner that is consistent with our longer-term philosophy and each client's objectives.

Volatility, Pullbacks, Rebounds & Rallies... *(continued from front page)*

Treasury's 7% return almost matches the S&P 500's 8% return as the yield on the 10-year remains near or sub 2.5%.

Lower interest rates partially explains why interest rate sensitive sectors such as utilities (14%) and REITs (13%) led in 1H14, but gave up some return in 3Q14 (~3%) as interest rates spiked in September, before falling again. While healthcare benefited from Obamacare expansion (Services +14%), M&A activity and new drug approvals drove larger cap sectors higher (Pharma +22%; Biotech+19%) (see chart 2). In late September, the Treasury Department issued new tax code rules, which makes "Tax Inversions" impractical. In a "Tax Inversion", a company can cut its tax rate by more than half by merging with a company in a low tax domicile such as Ireland. We purchased stock for accounts in our proprietary Common Trust Funds (CTFs) that benefited from the trend including Covidien (COV, +37%), Valeant (VRX, +5%) and Actavis (ACT, +45%). Despite the loss of the favorable tax treatment, these acquisitions appear to be going through without price adjustments thus far. The companies, however, are choosing to finance the acquisitions with debt as the repatriation tax on overseas cash will be higher than the debt costs in today's low interest rate environment.

For more details on market conditions, please see the enclosed insert outlining our Quarterly Review and Outlook.

Chart 2

Q3 2014
S&P 500 Sector Performance

	Q3	Year-to-Date
Healthcare	5.46%	16.62%
Information Technology	4.77%	14.13%
Telecommunication	3.07%	7.47%
Financials	2.33%	7.42%
Consumer Staples	1.95%	7.23%
Consumer Discretionary	0.26%	0.86%
Materials	0.22%	8.87%
Industrials	-1.09%	2.87%
Utilities	-3.96%	13.95%
Energy	-8.62%	3.23%

Commonwealth is a privately owned community bank offering a full complement of financial services including: Personal and Business Banking, Mortgage, Private Banking, Trust & Wealth Management. We are always looking for ways in which we can better serve customers and develop new relationships and encourage you to contact us for more information concerning any of our services. As the holiday season fast approaches, we want to take this opportunity to extend our best wishes for happy and prosperous times spent with family and friends. Cheers to all!

Our comprehensive wealth management service integrates Commonwealth Trust Company's wide-ranging capabilities and highly qualified staff, with a network of external resources and advisors you may designate, such as your personal attorney or accountant. Coordinating these resources, our team of professionals can provide you with the following services:

INVESTMENT MANAGEMENT:

Our staff of investment professionals can serve as a full-service investment advisor, establishing investment objectives, developing asset allocation, analyzing risk, constructing portfolios and monitoring and reporting on performance.

TRUST & ESTATE PLANNING:

Our staff of experts can help develop plans for the effective transfer of assets through wills and trusts. We have extensive expertise serving as trustee or co-trustee for all types of personal and corporate retirement plan trusts, including trusts that have direct investments in private companies, real estate or other less liquid assets. We may also assist with the settlement of estates, serving as executor or personal representative.

CHARITABLE PLANNING:

Our team is highly experienced in all aspects of charitable planning. We can help you locate worthy charities in your area of interest or help you leverage the value of charitable gifts to your pre-selected organization(s). Our expertise will allow you to maximize your charitable giving for the benefit of you and the recipient.

TAX, IRA, AND RETIREMENT PLANNING:

Our staff of experienced financial planning professionals can help minimize the burden of estate, inheritance and income tax through careful planning techniques. We can also assist with the creation or rollover of IRA assets.

CUSTODY SERVICES:

Commonwealth Trust Company's investment management service includes full custody services for all assets. For clients who employ multiple managers or for clients who prefer to self-direct a portion of their assets, we offer stand-alone custody services.

BANKING AND FAMILY OFFICE SERVICES:

At Commonwealth Trust Company, we provide customized deposit and lending banking services that give you access to your money when and where you need it. Our many services make it convenient for you to handle day-to-day transactions simply and efficiently, whether in person, over the phone or online. Some of the services we offer are: Concierge and Bill Paying, Mortgage Financing, Deposit Services, Business Banking, Secured/Unsecured Loans, Cash Management, and Fraud Prevention.

BROKERAGE & INSURANCE SERVICES:

Our staff of fully-licensed brokerage professionals can help you buy and sell a large selection of securities at competitive commission rates. We offer a variety of accounts designed to fit your individual investing needs and feature unique services to help you plan and implement your financial strategy. While still offering the strength and resources of a large financial organization, our personalized service will also provide you with a one-on-one approach and convenient local delivery.

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