Quarterly NEWSLETTER

Summer 2014

Commonwealth Bank & Trust Company

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Economic Momentum vs. Market Correction...

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During the second quarter, despite investor concerns that a correction appeared imminent, markets resumed their upward climb amid mostly positive economic news and data points. The S&P 500 ended the quarter up 5.22% and year to date has gained 7.12%. The Dow Jones Industrial Average gained 2.24% for the quarter and stands at 1.51% for the year to date. Despite Europe's slow growth and deteriorating situations in Iraq and the Ukraine, international markets fared well, with the MSCI EAFE and the MSCI Emerging Market Index returning 4.32% and 6.71% respectively for the second quarter. The small cap Russell 2000 index and the technology heavy Nasdaq continued the positive trend, with gains of 2.05% and 5.32%, respectively. Although many pundits argue that the "central bank induced" market rise will not continue, in the US, at least, economic fundamentals have shown surprising resilience in defiance of the naysayers and the backdrop of an increasingly negative geopolitical climate. Consumer confidence jumped to its highest level since January 2008 while average monthly job gains in 2014 have advanced to 214,000 and initial claims for unemployment have steadily dropped to 300,000 per month, levels we saw before the recession began. For more details on market conditions, please see the enclosed insert outlining our Mid-Year Recap and Outlook.

Chart 1

Q2 2014
Market Performance – Total Returns

	6.30.14 Level	Q2	YTD
Dow Jones	16956	2.24%	1.51%
S&P 500	1973	5.23%	7.13%
NASDAQ Composite	4459	5.32%	6.20%
Russell 2000	1206	2.05%	3.19%
S&P Midcap	1445	4.32%	7.48%
Russell 1000 Growth	910	5.13%	6.31%
Russell 1000 Value	993	5.10%	8.28%
MSCI EAFE	1972	4.32%	5.24%
	Yield	Q2	YTD
Barclays Municipal	16956	2.24%	1.51%
Barclays Aggregate	1973	5.23%	7.13%
Barclays High Yield	4459	5.32%	6.20%

Chart 2

Q2 2014
S&P 500 Sector Performance

	Q2	Year-to-Date
Utilities	7.77%	18.65%
Healthcare	4.51%	10.59%
Materials	5.60%	8.62%
Financials	2.30%	4.97%
Information Technology	6.51%	8.94%
Energy	12.08%	12.96%
Consumer Staples	4.65%	5.18%
Telecommunication	3.78%	4.27%
Industrials	3.85%	4.00%
Consumer Discretionary	3.50%	-0.60%

As Commonwealth Trust reaches the $1.5 billion asset level this summer and looks toward the $2.0 billion mark, we wanted to take this opportunity to inform you about several investments the firm has made in people and operational resources to enhance customer service, support recent business growth and accommodate future needs. Mike Motsinger and Fran Clark joined the firm during the spring as additions to the Administration staff along with Robin Barnett who arrived in June. Mike, Fran and Robin are all seasoned administrators with exceptional customer service skills. Also joining in August as Associate Trust Counsel is Alex Croft who has served the firm as a legal intern over the past 2 years. On the investment front, Erik Evans and Pete Ward have joined as investment officers and Nathan Kinney as a Research Analyst. Erik and Pete are experienced investment professionals and Nathan has proven himself working as an investment intern during the past year. In January, Steve Zeitz joined the firm as a top flight Operations Manager and we recently hired Patricia Pearl to provide additional back office support to our front line personnel.

(continued on back page)

Proprietary Performance Results

	2nd Quarter	1 Year	3 Year	5 Year	Since Inception
Focused Equity Fund [2]	5.13%	20.40%	15.37%	18.35%	17.32%
Aggressive Growth Fund [1, 3]	3.45%	25.30%	17.76%	18.35%	9.04%
Science/Technology Fund [4]	4.84%	27.42%	15.64%	17.12%	7.64%
S&P 500	5.22%	24.57%	16.54%	18.80%	17.64%[2], 9.87%[3], 7.42%[4]
Russell 2000	2.04%	23.63%	14.55%	20.18%	18.76%[2], 8.17%[3], 6.95%[4]
MSCI EAFE	4.31%	24.38%	8.81%	12.48%	12.96%[2], 3.20%[3], 4.62%[4]
Strategic Income Fund [5]	4.78%	14.52%	10.42%	13.07%	12.42%
60% Russell 3000 Val / 40% Barclay Agg	3.75%	15.74%	11.61%	13.63%	12.22%

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

The Federal Reserve continued its $10 billion taper in asset purchases at both FOMC meetings again this quarter. The Fed recognized the rebound in the economy, but did not acknowledge the pick-up in inflation. The latter was a surprise. The median Funds forecast for '15 rose from 1% to 1.125% and from 2.25% to 2.5% in '16. The long run rate forecast fell from 4% to 3.75%. In his July commentary, PIMCO's Bill Gross discussed their "New Neutral" interest rate thesis. It argues for short-term "real" rates to be 0% rather than the historical 2%. In other words, a longer run Funds rate of 2% if the inflation target remains in check. PIMCO says that "stocks, bonds and risk assets in general should appear less bubbly than some presume". We appreciate their logic and do not totally dismiss the concept.

Broad investment-grade indices finished the quarter with returns over 2% and are now up 4% in '14. This compares to -2% returns in '13. Previously we cited research suggesting back-to-back down years for the bond market is fairly rare. We reiterate that the steepest calendar year decline of 5% should be indicative of a worst case scenario for a 12-month period. Contrary to year-end sentiment, long-term investment grade bonds are leading most sub-asset classes with returns approaching 12%.

While the consensus is for rising rates from here, a number of analysts are pointing out the relative value of U.S. Treasury rates. These comparisons are particularly compelling vs. the recently embattled European countries. On June 5th, the ECB announced additional accommodation measures in keeping with its "whatever it takes" monetary policy. This is obviously supporting a low rate environment even as our economy is picking up. For example, nonfarm payrolls are encouraging, averaging 272k per month during the quarter, while the unemployment rate fell to 6.1% from 6.7%.

The low rate/default environment has benefited the high-yield bond market. Last quarter we lowered our high-yield ranking due to valuations. Our call was somewhat validated as investment-grade credit outperformed high-yield with returns of 2.8% vs. 2.5%. We have remained positive on emerging market bonds which have been great performers of late. The iShares JPM US Emerging Markets Bond ETF (EMB) was up 4.6% during the quarter and 8.6% in '14.

Municipal bonds returned 2.7% according to the BofA ML index and are up 6.6% in '14. This more than offset last year's -2.9% return. Long-term bonds (22+ yrs) were up 4.0% and are up 10.4% 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." However, given this strength, we now consider municipals slightly overvalued.

We continue to recommend a tactical underweight to core bonds, and an overweight to taxable absolute-return-oriented fixed-income and other alternative strategies.

Focused Equity

For the quarter, the strategy was up 5.13% versus 5.22% for the S&P 500 Equity Index. Since inception, the strategy narrowly trails the benchmark's return of 17.64% by 0.32% with a gain of 17.32%. The strategy has a beta of 0.80, 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 2.91% alpha since its inception (1/1/09).

The top 4 performers for the quarter were also the top 4 for the year returning between 16% and 22%. Apple (AAPL) returned to darling status in 2Q14 rallying 22% after better than expected results and anticipation of a larger iPhone 6 this fall as well as new products (iWatch?). After the quarter Apple released another positive earnings result on 7/22/14. Intel (INTL) rallied 22% during the quarter and returned to levels not seen in several years buoyed by corporate PC refreshes after Microsoft discontinued support of Windows XP forcing conversion to Windows 7, which requires more advanced processors. Both Spectra Energy (SE) and Compass Minerals (CMP) benefited from the heavy winter and increased16% and 18%, respectively, and both are up 21% YTD. Spectra experienced 24 peak demand days for its natural gas pipelines and has a significant backlog of expansion opportunities. Compass Mineral's salt business increased 8% during the harsh winter and specialty fertilizer sales increased more than 20%.

Compass Minerals Intl, Inc. (CMP)
4/1/2014 – 6/30/2014

Laggards in the fund included Express Scripts (ESRX) and eBay (EBAY) falling 8% and 9%, respectively. Express Scripts lowered its volume guidance slightly due to fewer than expected sign ups from healthcare reform as well as concerns over Gilead's (GILD) expensive Hepatitis C drug. Note: GILD is one of the Science & Technology funds largest holdings. We will likely be adding to ESRX if its second quarter earnings call goes well on July 29. EBay continues to struggle with slower than expected auction growth. We are encouraged by the involvement of activist investor Carl Icahn and expect him to work with management to wring out additional value from the firm.

Strategic Income Builder

For the quarter, the strategy was up 4.78%, soundly beating its blended benchmark return of 3.75%. Since inception, the SIB strategy has returned an annualized 12.42%, slightly ahead of its benchmark return of 12.22%. 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 2.01% annualized with a beta of 0.84.

Quarterly equity performance of 6.0% was driven by ConocoPhillips (COP), Apple (AAPL) and Intel (INTC), with returns ranging from 21-23%. COP, and the energy sector in general, benefited from rising oil prices. COP beat consensus earnings estimates by 16.6% in May though its stock price was a steady climb during the quarter. In July, COP increased its dividend 5.9% to a yield of 3.4%. Energy led the S&P 500 GICS sectors returning 12.1% for the quarter which was timely in that we recently raised this sector to an overweight given its relative underperformance. Apple and Intel are discussed further within our Focused Equity commentary.

Darden Restaurants, Inc. (DRI) continues to disappoint, falling 7.9% during the 2nd quarter. Recently, DRI completed its $2.1B sale of its Red Lobster chain to Golden Gate Capital. The company has earmarked $1B of the net proceeds to be used to retire outstanding debt with the remaining to be deployed for a new share repurchase program of up to $700 million in fiscal '15. Now that Red Lobster has been sold, DRI is expected to focus its efforts on rebuilding the Olive Garden chain where comp sales fell off 3.5% in FQ4. In the meantime, DRI is yielding close to 5% though they chose to not raise the dividend as is typical in June.

Fixed income/Alternative positions of note were the Loomis Sayles Bond (LSBDX +3.9%), T Rowe Price Institutional Emerging Markets Bond (TREBX +4.7%) and PIMCO All Asset All Authority (PAUIX +4.0%).

Science & Technology Strategy

The Science & Technology strategy's 4.84% 2Q14 return lagged the S&P Information Technology sector results of 6.51%, but beat Healthcare and Telecom sector results of 4.51% and 3.78%, respectively. It also trailed the Nasdaq 100 return of 7.41% and the broader Nasdaq Composite return of 5.31%. Neither index 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.

LEADERS: Even though technology outperformed healthcare in 2Q14, biotech stocks were the biggest contributors during the quarter. Laggards for 1Q14, Celgene (CELG) and Gilead (GILD) sold off strongly at the end of March and in early April. We trimmed into the decline and bought shares back as they started to rally and ahead of positive announcements. Gilead and Celgene led in 2Q14 by increasing 17% and 23%, respectively. Our patience over the last twelve months with Covidien (COV) paid off as shares rose 23% after Medtronic (MDT) announced a tax-inversion driven merger with Covidien. Our largest holding, Apple (AAPL), rallied 22% after announcing better than expected results and anticipation of a larger iPhone 6 this fall as well as new products (iWatch?).

LAGGARDS: Laggards in the strategy included Express Scripts (ESRX) and eBay (EBAY) falling 8% and 9%, respectively. Express Scripts lowered its volume guidance slightly due to fewer than expected sign ups from healthcare reform as well as concerns over Gilead's (GILD) expensive Hepatitis C drug. As you can see above, we are playing both sides in the Gilead-Express Script conflict. We believe an expensive Hep C cure ($84,000) is considerably cheaper than a $500,000 liver transplant or death, while expensive drugs will need to be effectively managed by Express Scripts in a reform environment. EBay continues to struggle with slower than expected auction growth, but we are encouraged by the involvement of activist investors and the hidden value of PayPal. We also saw small positions in Big Data stock, Splunk (SPLK), and internet advertising auction site, Criteo (CRTO), fall 23% and 17%, respectively after almost doubling in the last 12 months.

Gilead Sciences, Inc. (GILD)
4/1/2014 – 6/30/2014

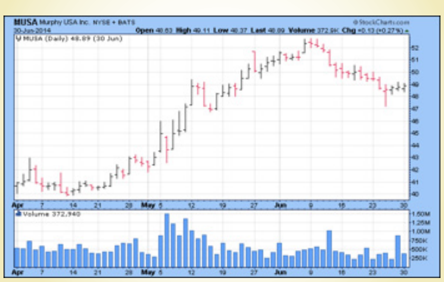
Small Cap Composite

The Small Cap Value Composite returned -0.62% for the second quarter of 2014, versus 2.04% for the Russell 2000 index.

The sectors with the highest contribution to the Portfolio's relative return in Q2 were Financials and Consumer Staples. Both sectors benefited from strong stock selection. One top contributing holding was Murphy USA Inc. (MUSA, 20.45%), one of the largest convenience store chains in the U.S. with more than 1,220 stations – nearly all of which are located next to Walmart stores in the South and Midwest. Despite posting lackluster quarterly earnings due to weak fuel margins, MUSA generated an impressive $89 MM of free cash flow from ongoing operational and inventory efficiency improvements. Management subsequently authorized a new $50 MM share repurchase authorization.

The sectors with the lowest contribution to relative return in Q2 were Energy and Materials. Both sectors underperformed as a result of poor stock selection. The largest negative contributor to performance was American Vanguard Corp. (AVD, -38.94%). The company develops, manufactures and sells branded crop protection chemicals (insecticides and pesticides). The company reported weak Q1 results due to higher than usual inventory levels from persistent wet weather at the end of the 2013 planting season and severe winter weather that delayed the start of the 2014 season. While the entire Ag Chem industry is facing these temporary headwinds, the impact felt by AVD is more acute given its product portfolio's higher concentration to corn (and lack of offsetting soybean exposure).

Murphy USA Inc. (MUSA)
4/1/2014 – 6/30/2014



Market returns and reported earnings are in line with our initial expectations for 2014, leaving our outlook for the remainder of the year largely unchanged.

Kentucky Municipals

Quarterly bond issuance by Kentucky municipalities increased to $933.1 million from $734.3 million (57 issues). New issue size was down, averaging $16.4 million. Non-BQ issuance was $498 million or 53% with bank-qualified "BQ" issuance of only $100 million or 11%. For our clients, we tend to utilize non-BQ because yields are typically higher. Taxable issuance was $194 million or 21%. AMT-subject issuance was notable at $141 million or 15%. We find ourselves participating in more of these deals as our typical client is not impacted by the alternative minimum tax (AMT). KY new issue levels of late have been on the pricey side in our opinion.

On June 2nd, "Moody's Investors Service has revised the outlook on the Commonwealth of Kentucky to stable from negative and affirmed the Aa2 issuer rating and the related Aa3 and A1 ratings of the commonwealth's appropriation-backed lease debt and intercept programs." While we view this rating action as a positive, market values were not impacted by this move.

In May, a federal bankruptcy court found that Seven Counties Services may leave KY's troubled retirement system. This ruling could lead to other quasi-governmental agencies leaving the system and leaving their unfunded liabilities. The U.S. Bankruptcy Judge also weighed in on the "inviolable contract" but said that contract exists between pension members and the state and not Seven Counties. In June, The Kentucky Retirement Systems Board of Trustees unanimously voted to seek an appeal. We believe this could prompt the state to consider more long-term solutions and reform.

During the quarter, our 10-year Kentucky tax-exempt yield target fell another 0.25% to 2.8%. However, our 15-year yield target rose 0.1% to 3.7% during the quarter.

Previously we discussed that Puerto Rico was a visible wild card but that much of the uncertainty seemed behind us. That changed recently with legislation allowing government entities to restructure debt outside bankruptcy. Rating agencies have responded by lowering them further into junk status. Moody's stated "On 28 June, Puerto Rico (B2 negative) adopted a debt relief law that provides a clear path to default for public corporations. The law is credit negative because it signals Puerto Rico's diminished willingness to support public corporations that have historically relied on the commonwealth's general fund revenues to pay for operating deficits. The government's willingness to tolerate the restructuring of public corporations' debt may further limit the commonwealth's own market access, leaving it more vulnerable to default."

Puerto Rico bonds are widely held due to tax-exemption in all states; particularly in mutual funds. In our portfolios, we have avoided this debt ridden territory other than escrowed bonds. While some PR bonds are trading at $40 cents on the dollar, the overall market has been relatively stable as have fund flows. We will be watching this situation closely and suspect that it could create a buying opportunity soon.

We continue to think intermediate bonds are the most attractive part of the market, particularly given recent 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.

Economic Momentum vs. Market Correction... *(continued from front page)*

Each of these exceptional individuals are dedicated to providing you with an outstanding customer experience, one that anticipates your needs and goes beyond your wildest expectations. We are delighted they have joined the team and look forward to their contributions in serving our clients. We invite you to learn more about our new staff members and current staff by referencing their biographical profiles at: **www.cbandt.com/wealth_and_trust/about_us/meet_the_team/** or by clicking on the accompanying picture if you are viewing this newsletter online.

We have also made several significant investments to our operational and systems infrastructure over the past year that will provide enhanced reporting tools for clients with more efficient production and delivery capabilities. Clients will soon have access to online performance reporting with more detailed graphics and depth on asset category performance. We have also made substantial commitments to enhancing our trust accounting systems and client web portals which we will be unveiling in the near future. Trust and Investment Management services continue to be an important and significant line of business for Commonwealth; as such we are committed to devoting all necessary resources to properly staff and equip this very important area. As you know, Commonwealth is a privately owned community bank offering a full complement of financial services including: Personal and Business banking, Mortgages, Private Banking, Trust and Wealth Management. We are always looking for ways in which we can better serve our customers and develop new relationships. We encourage you, or any of your friends or family, to contact us for more information concerning any of our services.

Back Row (L to R) – Pete Ward, Patricia Pearl, Erik Evans, Steve Zeitz, Mike Motsinger, Alex Croft; Front Row (L to R) – Nathan Kinney, Robin Barnett, Fran Clark

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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