Annual Investment Update

ECONOMIC REVIEW AND OUTLOOK

DECEMBER 31, 2014

Welcome 2015!

We are coming off a solid economic performance in 2014 marked by improvements in hiring, wages and corporate investments. It has been a magnificent year for both the stock and bond markets, even with a slight wobble in the equity markets at the end of the year. U.S. stocks were bolstered by an expanding, if uneven, economic recovery, surprising strong earnings growth and a Federal Reserve that remained accommodative even as it wound down a post-crisis stimulus program.

We expect the Federal Reserve to increase rates this year in a slow and steady approach, which should not diminish the appeal for U.S. stocks. The average forecast for stocks in 2015—a year when the bull market will most likely turn six years old—is around 10%. In this context, another quick shake out where stocks pull back hard without creating a lasting disturbance to economic fundamentals would probably be the healthiest, most welcome outcome for long-term investors. Thanks for taking a look and all the best health, happiness and prosperity in the new year!

Third quarter GDP growth highest since 2003.

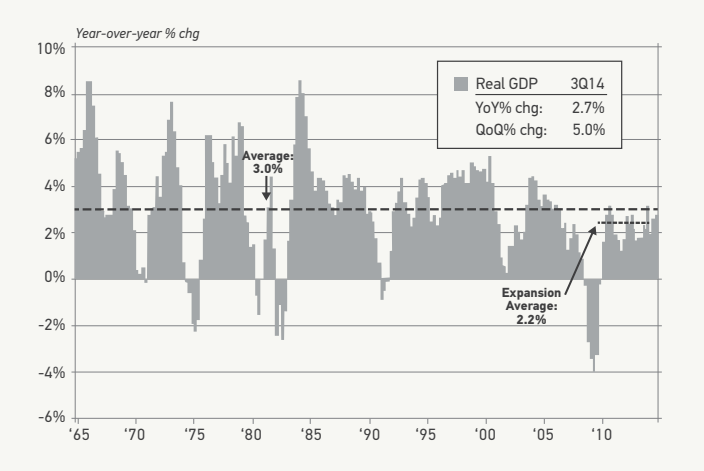
After several revisions, the Commerce Department announced that the growth rate for GDP in the U.S. was 5% for the third quarter. Consumer spending improved, spending on information technology surged at a double-digit pace, and U.S. government spending jumped 9.9%, led by a 16% increase in defense spending. Fiscal austerity in the U.S. has just about ended with the federal and state and local governments contributing to GDP for the first time since 2009. This follows a robust 4.6% rate for the 2nd quarter. The U.S. economy has not put together back-to-back quarters like these since 2003. Only China, India and Hong Kong posted stronger results in 2014. Looking into 2015, the U.S. economy should continue to be the principal engine of the global recovery, with growth moving above trend. Japan is expected to rebound from its 2014 weakness and the Eurozone and emerging markets should accelerate modestly, however with growth still weak relative to potential.

KEY ECONOMIC RELEASES

EMPLOYMENT	As of	Expected	Actual	Prior Period	12 Months Ago
Unit Labor Costs	DEC	-0.2%	-1.0%	-0.5%	1.4%
Unemployment Rate	DEC	5.7%	5.6%	5.8%	6.7%
Change in Non-Farm Payrolls	DEC	240K	252K	353K	203K
INFLATION (year over year)	**As of**	**Expected**	**Actual**	**Prior Period**	**12 Months Ago**
Consumer Price Index	NOV	1.4%	1.3%	1.7%	1.2%
CPI Ex Food & Energy	NOV	1.8%	1.7%	1.8%	1.7%
Producer Price Index	NOV	1.5%	1.4%	1.5%	1.1%
HOME PRICES (year over year)	**As of**	**Expected**	**Actual**	**Prior Period**	**12 Months Ago**
S&P/Case Shiller Top 20 Mkts.	OCT	4.4%	4.5%	4.8%	13.6%
MANUFACTURING ACTIVITY	**As of**	**Expected**	**Actual**	**Prior Period**	**12 Months Ago**
Capacity Utilization	NOV	79.4%	80.1%	79.3%	79.0%
Leading Indicators	NOV	0.5%	0.6%	0.6%	0.8%
GDP Annualized (3rd Quarter)	DEC	4.3%	5.0%	4.6%	4.1%

Source: Bloomberg

REAL GDP YEAR OVER YEAR SEASONALLY ADJUSTED ANNUAL RATE



Source: J.P. Morgan Asset Management

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PERKINS COIE TRUST COMPANY

ECONOMIC REVIEW AND OUTLOOK (CONT'D.)

Unemployment rate falls below historical average.

The jobless rate now stands at 5.8%, below the historical average of 6.1%. The U.S. economy has created jobs at a rate of greater than 200,000 per month for 10 months in a row. This brightening employment picture is one of the key reasons we think the economy is in good shape. The December payroll gain of 252,000 jobs topped forecasts and is consistent with an expanding labor force and a GDP growth rate of around 3% for 2015. The energy sector could create a headwind for the recovery, however. Since the peak in non-farm payrolls in January 2008, energy-related employment has accounted for 15.8% of total job gains. Other sectors will have to pick up the slack if energy is rolling over.

2014, the year of lower oil and gas prices.

Drivers celebrated throughout the second half of 2014 as the price of gasoline fell to five-year lows. Oil prices fell by 50% as a flood of crude from U.S. shale disrupted the global oil market. The price of oil in the U.S. began the year above $90, peaked at $107 in June and finished the year at $53. Part of the slump in prices can be traced to the Organization of the Petroleum Exporting Countries (OPEC), which voted to maintain its production quotas despite the increase in supply from the U.S. Prices will continue to decline as long as there is worldwide oversupply.

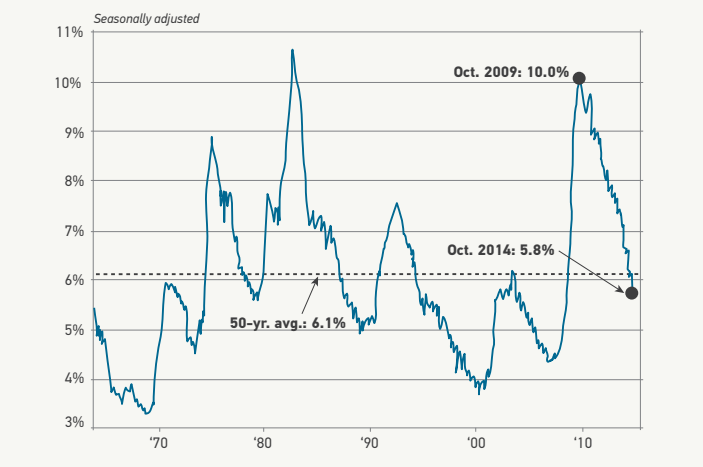
Housing market slows.

Strong employment growth and lower gas prices have had little impact on the housing market. Existing home sales were down 6.1% in November while new home sales slid 1.6%. Home prices nationwide increased 4.5% for the year ending October 31st. This is down sharply from the 10%+ gains earlier in the year and may suggest that the housing market is settling in to a more sustainable recovery. The slowing trend in prices and unit sales could be positive for the 2015 housing outlook. Price appreciation of around 4-5% won't force new buyers out of the market, and current homeowners can accumulate housing wealth without the risk of another housing bubble.

Inflation likely to remain below 2% of the Fed target.

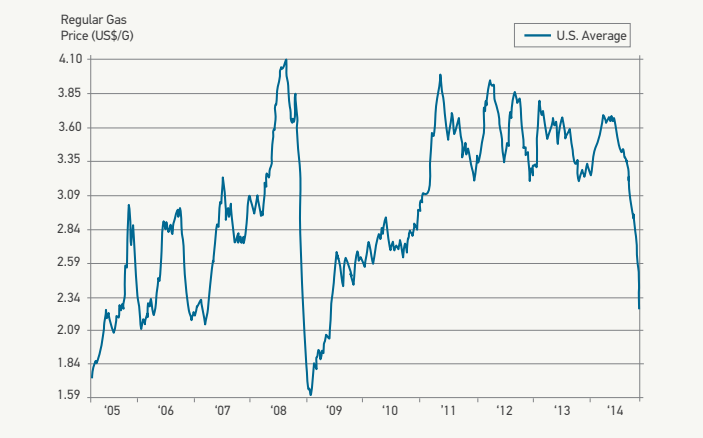
The Consumer Price Index (CPI), including food and energy, fell 0.3% in November, to a 1.3% annual rate. Inflation could move even lower in the near term, pushed down by tumbling energy prices, a strong dollar and low wage growth.

U.S. UNEMPLOYMENT RATE



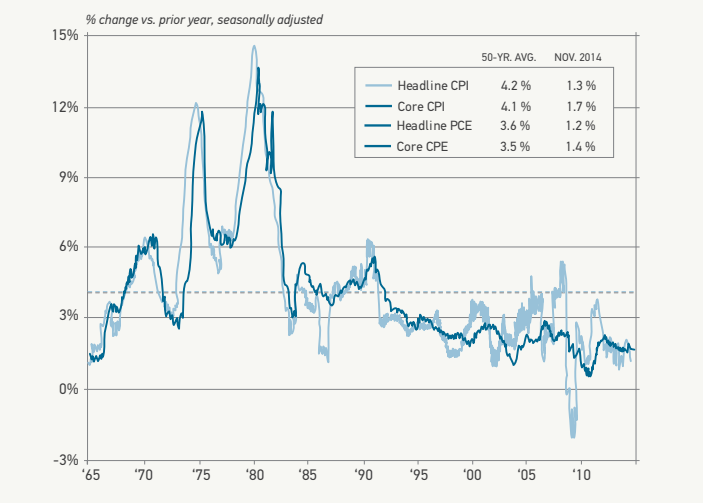
Source: J.P. Morgan Asset Management

GAS PRICES LAST 10 YEARS



Source: 2014 GasBuddy.com

CPI AND HEADLINE CPI



Source: J.P. Morgan Asset Management

BOND MARKET REVIEW

DECEMBER 31, 2014

Longer dated government bonds best performers in 2014.

A year ago, we assumed interest rates would end the year at modestly higher levels thanks to a global economic recovery and the end of quantitative easing. Yields actually did rise for much of the year for shorter maturities, i.e., 5 years and less, due to expectations for interest rate hikes sometime in 2015. Longer-term rates, however, plunged due to declining inflation expectations, geopolitical challenges (Russia/Ukraine, Syria) and the fear of another recession in Europe. Despite an average year-end forecast for the 10-year Treasury of 3.34%, its yield actually fell from 3% to 2.17%, while the 30-year rate dropped from 3.94% to 2.75%. Bonds with long maturities react most dramatically to changes in interest rates. The 20-year Treasury index, for example, gained an astounding 25% in 2014.

Municipal bond investor had a good year.

Rebounding from losses in 2013, munis posted positive returns in every month of 2014, an unprecedented streak. The full year gain of 8.7% for the Barclays 10-Year Muni index exceeded expectations and outperformed nearly all other asset classes with the exception of large-cap U.S. equities, long-dated treasuries and U.S. REITS. Individuals, the largest owners of the $3.6-trillion municipal market, returned to tax-exempt debt after Detroit's bankruptcy and Puerto Rico's economic crisis prompted them to sell in 2013. Investors have added about $21 billion to muni mutual funds in 2014 after extracting a record $63 billion last year. Muni bond supply in the new issue markets has been relatively heavy recently. However, year-to-date issuance of $295 billion is down about 4% from the same period last year. The size of the muni market has been contracting since 2010 as the high volume of bond redemptions (maturities and calls) has exceeded the supply of new bonds.

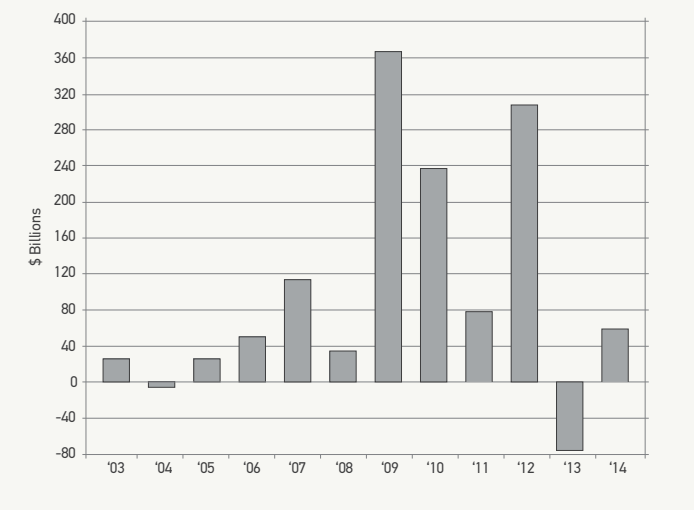
High-yield bonds impacted by energy sector.

High-yield bonds had a modestly positive year with a gain of 2.5%. This includes coupon interest, meaning junk bond prices actually fell in 2014. Bonds issued by companies in the energy sector make up an increasingly significant percent of the high-yield market. As of September, the percentage of these bonds in the Barclays High-Yield bond index was 16%, the second largest. The collapse in this sector has taken its toll on performance. Investment grade corporate bonds had a better year, gaining 8%. Our primary benchmark for taxable bonds, the Barclays Intermediate Gov/Credit index, rose 3.1%.

BOND MARKET RETURNS	Latest Quarter	12 Months	Last 3 Years
Barclays Intermed. Gov/Credit	0.9%	3.1%	2.0%
Barclays 10-Year Municipal	1.4%	8.7%	4.0%
Barclays High Yield	-1.0%	2.5%	8.4%
Merrill Lynch 90-Day T-Bill	0.0%	0.0%	0.2%
Treasury Infl. Protected Sec.	0.3%	0.5%	0.6%

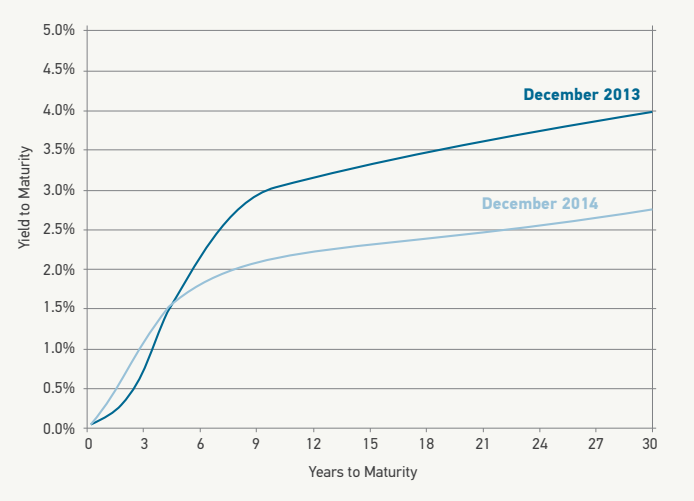
Source: Bloomberg, Vanguard, Bank of America, Merrill Lynch

ANNUAL BOND MUTUAL FUND FLOWS



Source: Bloomberg

U.S. TREASURY YIELD CURVE COMPARISON



Source: Bloomberg

BOND MARKET OUTLOOK

DECEMBER 31, 2014

Will 2015 finally see higher interest rates?

Over the past five years, bond experts have been consistently wrong with their rate forecasts. One of the primary reasons for the missed calls is that U.S. rates, while quite low on an absolute basis, look relatively good compared to yields on other countries government debt. The recent 2.17% yield may seem low to an American investor but not to a German investor looking at 0.68% for a comparable bond. U.S. Treasury yields are also higher than bonds issued by other less credit-worthy governments including Italy, Spain, and the UK. Foreign buyers with cash will continue to favor the U.S.

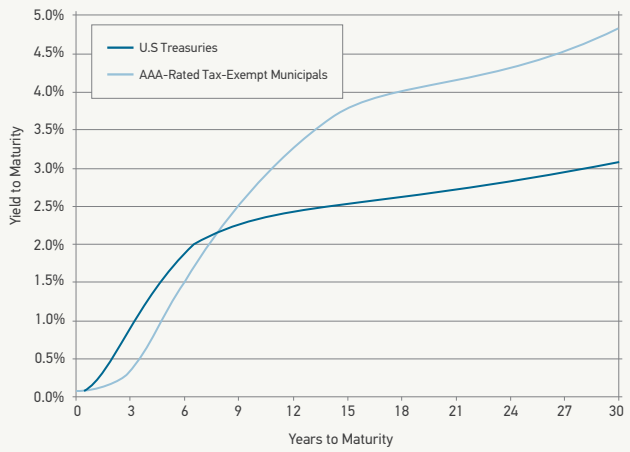
Current yields are lower to start off 2015, with the exception of high-yield bonds.

For investors looking for income, traditional bond sectors, unfortunately offer less yield than a year ago. Yields for 10-year municipal bonds declined a full percentage point from 3.0% to around 2.0%, investment grade corporate bond yields fell just 0.15% to 3.1% high-yield bond yields, however, actually rose to 6.6%. We continue to favor corporate bonds and government agencies over treasuries. We also recommend that investors hold some cash and short-term fixed income vehicles in anticipation of Fed rate hikes in 2015, but continue to maintain a larger allocation to intermediate-term maturities. Though interest rates remain near historic lows, we hold out the possibility for even lower rates in the short-term due to falling energy costs and slowing growth overseas. Investors should be prepared for more volatility in the fixed income markets as traders try to gauge the speed and magnitude of the Fed's plans.

Muni bond supply remains limited.

A limited supply of new bonds and increasing demand from investors looking for tax-free income should help the muni market in the coming year. Balance sheets for cities and states across the country are generally much stronger than they were during the period leading up to the financial crisis, with some exceptions. Illinois, for example, the state with the most dire fiscal outlook, may have to cut income tax rates by 25% even as it faces a budget shortfall, a deeply underfunded retirement system and billions of dollars of unpaid bills. We have a cautious outlook for states like Illinois, New Jersey and Connecticut with underfunded employee pension systems and for states that are heavily dependent on the energy sector.

BOND YIELDS



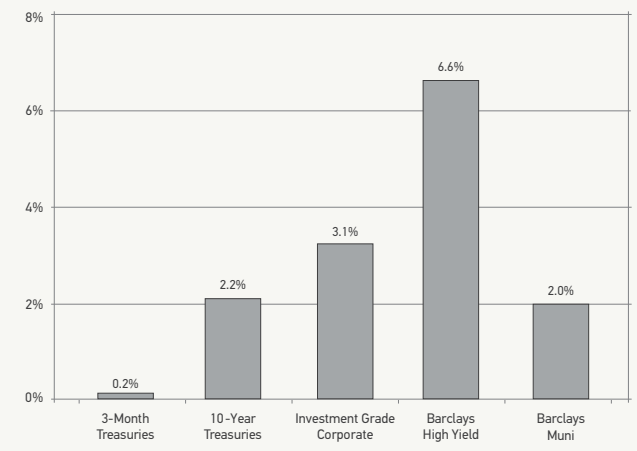
Source: Bloomberg

DEVELOPED COUNTRY 10-YEAR GOVERNMENT BOND YIELDS

Developed Countries	10-Year Yield %
Switzerland	0.49%
Japan	0.53%
Germany	0.95%
France	1.29%
Ireland	1.65%
Spain	2.14%
Canada	2.15%
Italy	2.33%
United Kingdom	2.39%
United States	**2.49%**

Source: Fidelity Investments

SELECT FIXED INCOME YIELD TO MATURITIES



Source: J.P. Morgan Asset Management

STOCK MARKET REVIEW

DECEMBER 31, 2014

U.S. equities reach multiple record highs.

In the final week of 2014, the S&P 500 reached a 53rd all-time high, its third best year for record highs in the last 25 years. Including dividends, the index returned 13.7%. The current bull market, which started in March 2009, has risen 209% and is moving into its sixth year, has now surpassed the average bull market duration by a year.

Merger activity contributed to sector returns.

The market sectors that outperformed in 2014 were Utilities, Health Care and Technology, soaring 29%, 25% and 20%, respectively. Utilities, which were the second worst performing sector next to Telecom in 2013, made a swift comeback as retreating interest rates brought yield investors back into the sector. Merger activity benefited all three sectors. Additionally, strength in the biotech industry drove returns in Health Care, and higher investment spending by businesses boosted returns for Technology. The energy sector fared the worst losing 7.8% on sinking oil prices.

Asset classes experienced a wide range of returns in 2014.

After steadily beating large cap stocks since 2011, small cap stocks, which had become relatively pricy, lost their lead rising only 4.9%, as measured by the Russell 2000. International markets struggled over the past year with threats of a deepening recession in Europe, further slowing in China and negative currency translation due to a strong dollar. The MSCI EAFE index and the MSCI Emerging Markets index slid 4.2% and 2.2%, respectively. The Real Estate sector surged over 15% with the recovery of global real estate markets. Plummeting oil prices drove the DJ-UBS Commodity Index down 17%.

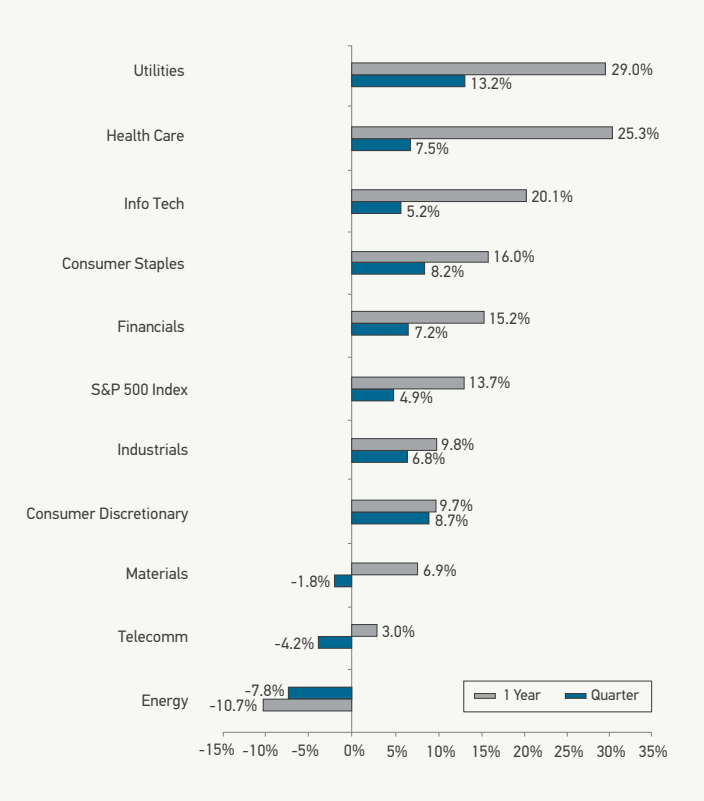
Our projections underestimated the strength in U.S. equities.

We were pleasantly surprised that the S&P 500 produced a double-digit return with lower than average volatility. We anticipated a modest rise in the market multiple, which closed the year at 16.2 times earnings, 2.6% higher from a year ago, as measured by the forward price earnings ratio of the S&P 500. Revenues increased moderately, as we expected, supporting earnings growth. Unexpectedly, longer-term interest rates fell, which also benefited corporate profits. The labor market improved as anticipated, yet wage inflation remains tame.

STOCK MARKET RETURNS	Latest Quarter	12 Months	Last 3 Years
S&P 500	4.9%	13.7%	20.4%
Russell 1000 Growth	4.8%	13.0%	20.2%
Russell 1000 Value	5.0%	13.4%	20.9%
S&P 400 Midcap	6.3%	9.7%	19.9%
Russell 2000	9.7%	4.9%	19.2%
MSCI Developed (EAFE)	-3.5%	-4.2%	11.8%
MSCI Emerging Markets	-4.5%	-2.2%	4.0%
Alternative Asset Returns			
DJ-UBS Commodity	-12.1%	-17.0%	-9.4%
MSCI World Real Estate Index	7.1%	15.2%	15.6%

Source: Bloomberg

S&P 500 RETURNS BY SECTOR FOR 2014



Source: Strategas

STOCK MARKET OUTLOOK

DECEMBER 31, 2014

Price to Earnings ratio slightly stretched.

The S&P 500 Forward Price to Earnings ratio expanded moderately in 2014 to 16.2 times earnings. It now lies above its 10-year average of 13.8x and is relatively pricier than both developed and emerging markets valuations as shown in the chart at right. Although, the S&P 500 is slightly stretched based on historical levels, reversion to the average could take some time. Further valuation expansion is possible in 2015, though we expect it to be very limited.

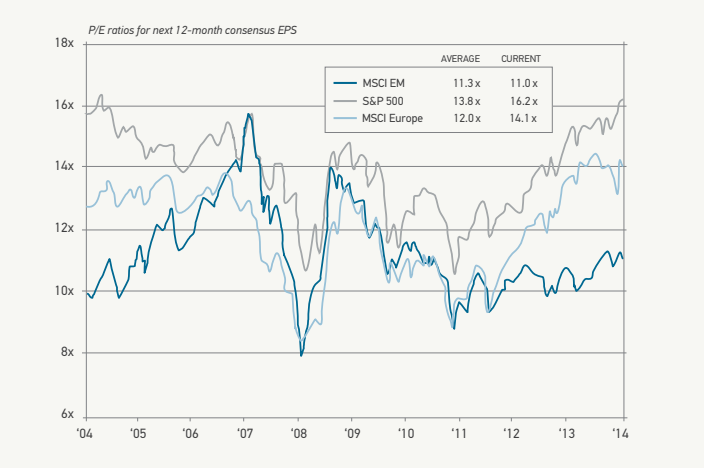
Earnings growth to continue.

Earnings growth provided the bulk, or 8.8%, of the S&P 500's 13.7% return. Multiple expansion and dividends in roughly equal amounts made up the remainder. This year, we project earnings growth to deliver in the mid to high single digits. Factors driving returns should include accelerating revenue growth from industries benefiting from lower oil and gas prices and greater merger and acquisition activity, which rose 20% globally in 2014. Dividends should stay fairly steady, providing approximately 2% to the market return. Based on the pace of the economic recovery, the Federal Reserve plans to start raising interest rates by mid-year, the first time in almost a decade. While the economy may be on strong enough footing to withstand rate hikes, investors fear higher borrowing costs will hamper corporate margins and that high-yield stocks will be sold in favor of bonds paying higher coupons. Thus, we expect volatility to pick up again in 2015.

Valuations of international stocks becoming attractive.

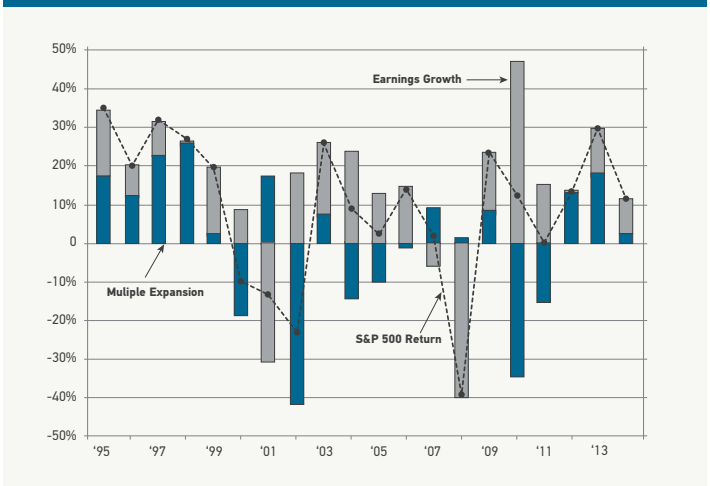
Valuations of developed and emerging markets are relatively more attractive than U.S. equities, as displayed at right. While the U.S. enters its tightening phase, the European Central Bank's stimulative monetary policies could soon gain traction instilling confidence that economic growth can be restored overseas. While it is expected to be a bumpy ride, international markets could potentially provide greater returns than the U.S. equity markets in the coming years. Correlations between U.S. equities and international stocks have been falling to pre-recession levels, as shown at right, signifying the increased long-term benefits of maintaining a globally diversified equity portfolio for its better long-term risk-adjusted returns.

FORWARD P/E RATIOS



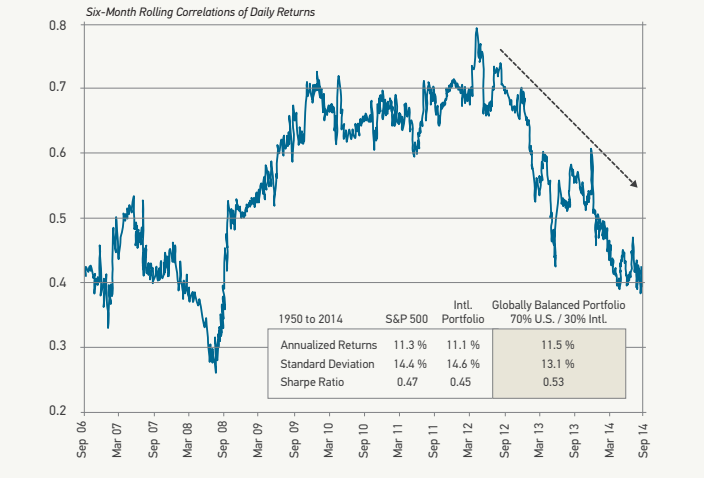
Source: J.P. Morgan Asset Management

S&P 500 SOURCES OF RETURN



Source: Strategas

CORRELATIONS INTERNATIONAL AND U.S. EQUITIES



Source: Fidelity Investments

Perkins Coie Trust Company offers investment management services for trusts and estates, personal investment portfolios, individual retirement accounts, private foundations and endowments.

PATRICK A. CASEY, CTFA, is President and Chief Executive Officer of Perkins Coie Trust Company. He has over 30 years of experience in the financial services industry advising private clients in the areas of banking, trust and investment management, and wealth planning. He graduated from St. John's University with a Bachelor of Science in finance and received his MBA in management from Fairleigh Dickinson University. Patrick is a Certified Trust and Financial Advisor. He is involved with the Fred Hutch Planned Giving Advisory Committee and is a member of the Seattle Estate Planning Council.

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KIM MCARDLE is a Trading & Portfolio Administrator with Perkins Coie Trust Company and provides support in all aspects of investment management including trade execution, investment research and analysis, performance measurement, investment compliance and client reporting. Kim graduated from Western Washington University with a Bachelor of Arts in English literature. Kim also holds her Series 7 and 66 licenses.

INVESTMENT PROCESS

1. **LEARN** CLIENT GOALS AND NEEDS
2. **ESTABLISH** CLIENT INVESTMENT OBJECTIVE & STRATEGY
3. **DETERMINE** ASSET ALLOCATION STRATEGY
4. **CONSTRUCT** & MONITOR INVESTMENT PORTFOLIO
5. **REVIEW** AND REASSESS CLIENT NEEDS

The investment process at Perkins Coie Trust Company is always client-driven. We meet routinely with clients to ensure that we incorporate changing life-cycle needs into our investment strategies.

PERKINS COIE
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WORTH KNOWING®

Annual Investment Update

Charitable Gifts

Get a Jump Start on Your Charitable Gifts.
You might want to consider whether you want to make any gifts this year to your favorite charities. If you do, you will be in good company.

According to the National Philanthropic Trust, 95.4% of households gave to charity in 2013 for a total of over $241 billion in charitable gifts. High net worth donors gave to charity to support education (80%), basic needs (79%), arts (69%), health (65%) and religion (65%). The most common reason cited for charitable giving is to give back to the community. When considering gifts to charities, we recommend that you research the charities, consider whether you want to give cash or other property, pay attention to the timing of gifts and make sure you receive and retain the receipts that prove you donated.

CHARITABLE GIFTS

As you consider where to "spend" your charitable dollars, you may want to spend some time checking out the charities asking you for money. Are they legitimate? Do they use their money wisely? How much do they spend on fund-raising?

There are many ways to check up on charities.

- You can use Charity Navigator at *charitynavigator.org* to see whether the charity is rated.
- You can also check your state's charitable database. For example, in Washington, you can go to *sos.wa.gov/charities/DatabaseSearch.aspx*.
- To see whether an organization is actually a charitable organization that qualifies for a charitable deduction, you can search for the organization on the IRS website. *irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Select-Check*
- Depending on the size and type of charitable organization, you could even look at the charity's most recent tax filing by going to *www.guidestar.org*.
- Sometimes a general search in your favorite search engine will yield a plethora of information on your favorite charities, including their websites and comments by donors, stakeholders and others.

GIFTS OF CASH, SECURITIES OR OTHER PROPERTY

According to the IRS, most individuals simply give cash to their favorite charities. Less than 130,000 households made gifts of stock or other property. Depending on your circumstances, a gift of securities or other property could be smart tax planning. Individuals may deduct up to 50% of their adjusted gross income (AGI) for cash gifts made to public charities and up to 30% of their AGI for gifts of securities or other property to public charities. Individuals may deduct up to 30% of their AGI for cash gifts made to private foundations and up to 20% of their AGI for gifts of securities or other property to private foundations. When making gifts of securities

and other property to private foundations, the amount of the deduction is limited to your basis in the securities and other property, except for qualified (marketable) securities.

Making a gift of appreciated property, such as securities, can be a very smart strategy. By giving appreciated stock to your favorite charity, you incur no capital gains tax with respect to that gift yet you still can deduct the gift's full fair market value. If you have stock that has depreciated in value, generally the best practice from an income tax perspective is not to give the stock directly to charity, but instead, to sell the stock, take a loss on your tax return, and then give the proceeds from the sale to charity.

NO TIME LIKE THE PRESENT

Contributions are deductible in the year that they are made so be sure to make your charitable gifts by December 31. Credit card charges made before the end of the year are deductible even if the credit card bill isn't paid until the next year. Similarly, checks that are written and mailed by the end of the year will still be deductible in the year mailed even if they aren't cashed by the charity until the following year. While pledges are great, there will not be a charitable deduction until the pledge is actually paid.

Don't forget to check to see whether your employer matches your charitable contributions. If your employer offers this benefit you can make your gift go even further.

THANK YOU NOTES ARE IMPORTANT

There are strict substantiation requirements in order for you to claim a charitable deduction for your charitable gift. No deduction is allowed for cash gifts less than $250 unless you have either a bank record documenting the gift or a written communication from the charity indicating your name and the amount and date of donation. For contributions of $250 or more, you must obtain a contemporaneous written acknowledgment from the charity. If you make a noncash contribution valued above $500, you must file Form 8283 with your return. If the noncash contribution of property is in excess of $5,000, a qualified appraisal of the donated property must be obtained.

IF YOU STILL FEEL GENEROUS

Depending on your capacity to give and your appetite for complexity, you could consider establishing a donor-advised fund or forming your own private foundation. You could also do some planning to benefit both your family and your favorite charity by creating a charitable lead trust or a charitable remainder trust. These strategies take time to implement so allow yourself time to work out the details before the end of the year.

We hope these smart strategies help you to donate to your favorite charities while also maximizing your charitable deductions.

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