ClarkCapital
MANAGEMENT GROUP

Navigator® Global Opportunity

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Second Quarter — Portfolio Commentary

COMPLACENCY & UNINTENDED CONSEQUENCES

"There is something strange about fighting debt by incentivizing more debt." *Jaime Caruana, Head of the Bank for International Settlements (BIS)*

Debt has always been the "elephant in the room" in this financial crisis and recovery. This crisis, which we believe was spawned by mal-investment and excessive leverage, was initially addressed by a series of asymmetric monetary policy measures which redistributed bad debt from private to public institutions such as the Fed. Although this was highly successful in avoiding a massive collapse in financial asset prices, it appears that the process did little to clear the majority of bad debt, necessary in rebuilding balance sheets. In fact, debt levels have continued to rise as a percentage of GDP, primarily through the Fed's balance sheet expansion. Beginning with the Troubled Asset Relief Program (TARP), continuing with Zero Interest Rate Policy (ZIRP) and three Quantitative Easing (QE) programs, our monetary policy has essentially been crisis driven. The macro-pur-

Executive Summary

Debt is still a problem and may constitute a drag on future growth.

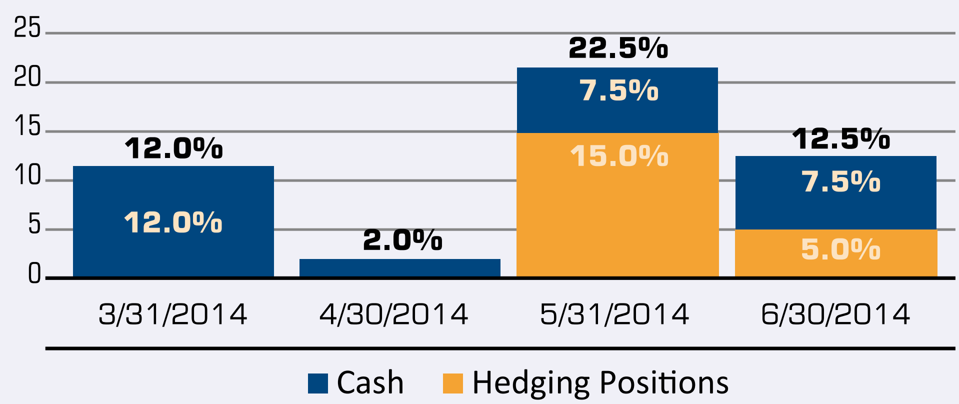
The markets are under the spell of the Fed "put," which has served as a substitute for confidence in fundamentals.

Liquidity is the all important element that has been driving markets. Quantitative easing has provided the liquidity that has driven asset prices upward, and the lack of growth of the Fed's balance sheet could arouse fear of a market correction, if the past is any indication of the future.

We have enjoyed the fruits of this liquidity (i.e., financial asset price growth) but may be subject to the future unintended consequences of its application.

Our management tactics remain the same. Stay with the trend as best we can, while controlling risk at the position level as well as the portfolio level.

Defensive Positions (Last Four Months)



Past performance is not indicative of future results.

This is not a recommendation to buy or sell a particular security. Please see attached disclosures.

John E. Clark, IV, CFP®
Portfolio Manager

John serves as a Portfolio Manager on the Navigator Global Opportunity management team, focusing on trend and risk analysis and is a member of the Clark Capital Investment Committee. John has over 20 years of experience in the investment advisory business. Prior to joining Clark Capital in 2011, John spent 15 years at Wachovia Securities and its predecessor firm Wheat First Butcher Singer, where he spent his last two years managing the Absolute Return ETF portfolio. John holds a degree in Economics from Millersville University and pursued graduate studies in economics at Lehigh University, with an emphasis in Econometrics. He is a Certified Financial Planner (CFP®) licensee and a Chartered Financial Consultant (ChFC) with the American College. He is also an Affiliate of the Market Technicians Association, a professional organization of market analysts, and is currently studying for Level III of the Chartered Market Technician's examination.

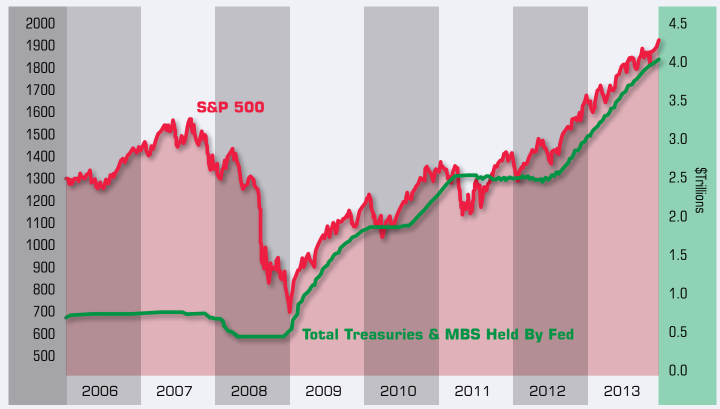
pose has been to give financial institutions time to repair their balance sheets and provide a stronger buffer against future shocks through more robust capital reserve requirements.

It is our opinion that essentially, there are three policy venues by which our economy can be repaired: monetary, fiscal and macroprudential (regulatory frameworks through which future systematic risk can be mitigated). Although it appears that there have been some positive effects from implemented macroprudential policies, monetary policy has done all the heavy lifting. There has been virtually little in meaningful fiscal policy employed in this crisis. Without this, we may be quickly approaching the limits of monetary policy efficacy. More importantly we very well may face quite a few unintended consequences because of our exclusive reliance on this monetary policy, such as:

- ZIRP has driven markets to divert funds away from capital investment for real economic activity to the lowest level in decades (as a percentage of GDP). Instead ZIRP has encouraged financial engineering activities such as stock buybacks using the issuance of new low-cost debt.
- ZIRP has provided an unrelenting multi-year drop in interest rates, accompanied by an increase in debt levels. This in turn we contend makes the economy more sensitive to future rate hikes that can damage the economy, creating a debt trap.
- We have a jobless economic recovery, where the "wealth effect" of increasing asset prices and low interest rates has not contributed to commensurate increases in full time employment.
- Fed policy has created extraordinary financial market complacency where markets have fallen under the spell of monetary policy the so called Fed "put." This complacency has helped foster very low volatility in the equity, treasury and currency markets which currently are at multi-year lows. However, when there is more than a 5% equity market drawdown, this complacency may quickly turn into fear. The Fed "put" has in effect become a substitute for confidence in fundamentals, but not a strong substitute.
- In our view, only with the addition of structural fiscal reforms, especially comprehensive tax reform, can growth be restored and debt reduced. The success of monetary policy has allowed the political establishment to avoid this painful process. If they continue to avoid the necessary policy actions and we enter a recession, we would enter that recession with very little monetary policy maneuvering room.

This is the macro background. Let us look what lies ahead. In the long run, we remain optimistic (despite the above) we believe eventually the right policy moves will be effected. We may experience a disruptive intermediate term in the markets until the global economic order finds its new policy mix.

Let us look at the chart recently published by Tom McClellan of McClellan Financial Publications under the headline of "Still The Only Chart That Matters."



Source: McClellan Financial Publication

Overlaid upon the chart of the S&P 500 is the Federal Reserve's balance sheet size (scale on the right), which reflects the massive purchases of Treasuries and Mortgage Backed Securities through their quantitative easing programs. The high correlation between the trend of the Fed's balance sheet and the S&P 500 is obvious. When the rate of growth of their balance sheet falls to zero, market corrections have occurred. One month following the termination of QE1 in April 2010, the equity markets experienced the "Flash Crash." The month following the end of QE2 in June 2011, we experienced the sharp 20% correction in July 2011. Ostensibly, the Feds "tapering" program is meant to avoid these sudden market disruptions. In their June policy meeting, the end of this QE program was set for October 2014. Until then, the Fed's balance sheet continues to grow.

As we've stated many times, liquidity has been the mother's milk of this bull cycle; so we view this chart as more than a coincidental curiosity. We are in the midst of a rally which is quite extended in time. Currently, we have gone over 1000 calendar days without a 10% correction. Since 1945, we have only experienced this four times. Three of those four times have been followed by corrections of 20% or more. Combining the end of the Fed's QE with the extended nature of our rally creates concern for us. Our next chart is the monthly chart of the S&P 500 which we have shown in prior commentaries. Note the three ascending trend lines, where each successive trend line becomes steeper and steeper. Also, one notices each corrective action within the trend becomes less and less in terms of price and time. We refer to this as a "blow off" trend; this type of trend can end suddenly without a multi-week distribution.

Source: Bloomberg

So our tactics remain the same. Stay with the trend as best we can, while controlling risk at the position level as well as the portfolio level. Be vigilant, but don't fight the trend until clarity from the weight of evidence dictates it. Viewing our cash and hedging history on the first page, it is evident we add and detract from our defensive positions at the margins on an ongoing basis always staying cognizant of possible risks to the trend but not going against it.

It is important to remember that in upside "blow offs," such as the S&P 500 is experiencing:

- Overvaluation can become more overvalued.
- Normal seasonality and price cycles are thwarted.
- Sentiment can become frothy and complacent, yet become even more frothy and complacent.

As portfolio managers, we're tasked with the duty of assessing financial risks, requiring us to make ongoing judgments as to how much risk to incur in order to produce portfolio returns. We are not hired to be risk complacent — foregoing that risk assessment function to the belief the Federal Reserve will maintain market stability at all costs. Unfortunately, as a practical matter, much of today's portfolio management world has devolved into that mindset. We at Clark Capital shall not.

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The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 75% of U.S. equities.

The Dow Jones Industrial Average is a stock market index that shows how 30 large publicly owned companies based in the U.S. have traded during a standard trading session in the stock market.

The NASDAQ Index is a market-weighted index of all common stocks listed on the NASDAQ exchange.

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performers of developed markets outside the U.S. and Canada.

The MSCI World Index is a freefloat-adjusted market capitalization index that is designed to measure global developed market equity performance.

The MSCI World Index ex. U.S. is a freefloat-adjusted market capitalization index that is designed to measure global developed market equity performance excluding the U.S.

The MSCI Emerging Markets Index is a freefloat-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

The MSCI All Country Europe is a freefloat-adjusted market capitalization index that is designed to measure the performance of European equity markets.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index.

The Russell 3000® Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

The VIX Index is a forward looking index of market risk which shows expectation of volatility over the coming 30 days.

Barclays U.S. Government/Credit Bond Index measures the performance of U.S. dollar denominated U.S. Treasuries and government-related & investment grade U.S. Corporate securities that have a remaining maturity of greater than one year.

The Barclays U.S. Aggregate Bond Index covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities. To qualify for inclusion, a bond or security must have at least one year to final maturity, and be rated investment grade Baa3 or better, dollar denominated, non-convertible, fixed rate and publicly issued.

The Barclays U.S. Corporate High-Yield Index covers the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below.

Index returns include the reinvestment of income and dividends. The returns for these unmanaged indexes do not include any transaction costs, management fees or other costs. It is not possible to make an investment directly in any index.

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