Clark Capital MANAGEMENT GROUP

Navigator® Fixed Income

Jamie Mullen, Senior Portfolio Manager

First Quarter 2015 — Portfolio Commentary

EUROPE JOINS THE QE PARTY

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Senior Portfolio Manager

As Senior Portfolio Manager, Jamie developed and manages the Navigator Global Opportunity portfolio and manages the Premier Fixed Income Strategies. In addition, Jamie manages covered call options deployed on individual stocks and exchange traded funds in the Premier Portfolio Group and implements collar strategies on individual blocks of stocks. He is a member of the Clark Capital Investment Committee. Jamie has over 25 years of experience with fixed income securities. He began in municipal credit research and worked in public finance before moving to a position in trading where his experience included trading municipal bonds and employing fixed income futures and futures options. He has extensive experience in dealing with mutual funds, and trust departments and money managers. He received his degree from St. Joseph's University.

The Year in U.S. Treasury Interest Rates

	6/30/14	9/30/14	12/31/14	3/31/15
2 year	0.45%	0.57%	0.66%	0.55%
5 year	1.63%	1.75%	1.65%	1.37%
7 year	2.13%	2.20%	1.97%	1.70%
10 year	2.53%	2.49%	2.17%	1.92%
30 year	3.36%	3.16%	2.75%	2.53%

Source: Bloomberg

"Patience? We don't need no stinking patience."

This is what bond traders would have said to Humphrey Bogart if he were on the FOMC with Janet Yellen after the March 18, 2015 rate decision.

Executive Summary

Fed removes the word "patience" from the rate decision: U.S. interest rates remain low as the Fed worries about the economic data that appears to slow versus when to start raising rates.

Europe Starts QE: Interest rates continue to fall in Europe as a result of QE. The result has been a move towards negative yields in the front end of European sovereign debt.

Currency War: The euro closes 2014 at $1.20. The announcement of QE causes a dip below $1.05 by mid-March. Will a lower euro spur economic growth?

Quantitative Easing (QE) ended in the fourth quarter of 2014 and the 10-year U.S. Treasury bond began 2015 at a 2.17% yield. The low yield for the quarter was 1.64% on January 30th and the high of 2.24% was on March 6th. The January rally occurred after the European Central Bank (ECB) announced a QE program. The yield high in March was a result of the market trying to interpret results of the Fed's first interest rate hike, to possibly occur in 2015.

The long-awaited March Fed meeting resulted in the removal of the word "patience" in their statement on rates. The removal of patience was supposed to signal a ¼ point increase in the Fed Funds rate as soon as the second quarter of 2015. But as the Fed's minutes of the meeting were digested and Yellen began to speak, it became clearer that the Fed was still dovish. Yields began to decline again.

How could that be? First, economic figures weakened except for the unemployment report. Second, a harsh winter in the Northeast has been blamed for everything from a slowdown in durable goods to the decline in retail sales. Third, the U.S. dollar continues to rise against all major currencies, putting pressure on large cap stocks with sales outside the U.S.

Past performance is not indicative of future results.

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

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We are of the macro opinion that the Fed will not be able to exit QE and gradually raise interest rates without some unintended consequences. Much of the world's interest rates are trading at negative yields. This continues to put downward pressure on U.S. interest rates, as they provide relative value versus alternative sovereign debt. That pressure can flatten the yield curve and continue to keep rates lower for longer.

Here is a snapshot of global interest rates before and after ECB President Draghi enacted QE:

Global Government Bonds as of 3/31/2015

	5 year		10 year	
	12/31	3/31	12/31	3/31
France	0.16%	0.05%	0.82%	0.47%
Germany	0.01%	-0.10%	0.53%	0.17%
Italy	0.93%	0.53%	1.87%	1.23%
Spain	0.86%	0.52%	1.59%	1.20%
Portugal	1.43%	0.89%	2.65%	1.66%

Source: Bloomberg

On January 16, 2015 the Swiss central bank removed its peg to the euro and the Swiss currency soared against the euro. The Swiss Bank refused to continue to expand its balance sheet by buying the euro. This can only be seen as a condemnation of ECB policy and a return to defending the Swiss franc. It clearly foreshadowed the long awaited stimulus plan by the ECB the following week.

Finally, on January 21, 2015 Mario Draghi announced a $60 billion euro per month bond buying program until September 2016. The result is that rates across Europe have imploded with France, Germany, Sweden, Netherlands and Switzerland having negative two-year interest rates by quarter end. The German two-year yield turned negative on August 25, 2014 and is still below zero.

The response to these measures was a breathtaking devaluation of the euro. At the end of 2014 the euro was trading at $1.20. Before the ECB QE announcement it was at $1.16 and then traded at the low for the quarter on March 16th below $1.05.

The winners in the first quarter of the euro devaluation have been holders of European equity and the German economy. Maybe the plan is to make an American-made Jeep cost the same amount as a Mercedes and let the consumer decide what to buy. The real proof will be if the peripheral countries around Germany can expand their economies with a lower euro.

So the question going into the second quarter of 2015 is:

Did Draghi pull a rabbit out of the hat? Or did he finally find the rabbit in the hat after years of reaching around for one?

The Taxable Portfolios

Oil prices stabilized and energy sector bonds that were hardest hit in the fourth quarter of 2014 rallied in January after tax loss selling was complete and liquidity returned for the start of 2015. Since we think rates may continue to remain low, we like investment grade credits when the 10-year yield moves higher than 2%.

The Tax Free Portfolios

We continued to add to our holdings in AA or better credits with 4% coupons in 15 to 20 year maturities. We have seen that January tends to come in like a lion with lots of reinvestment money from January 1st interest payments and maturities. Conversely it tends to go out like a lamb in March with new issues greeted with lower demand and buyers being able to have better inputs on price and therefore value.

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The Barclays 30-Year U.S. Treasury Bellwethers Index is a universe of Treasury bonds, and used as a benchmark against the market for long-term maturity fixed-income securities. The index assumes reinvestment of all distributions and interest payments.

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