K. Sean Clark, CFA
Chief Investment Officer

As Clark Capital's Chief Investment Officer, Sean oversees all of the Firm's investment activities and heads the Firm's portfolio team. Sean joined the Firm in 1993 and is responsible for asset allocation and investment selection for Navigator Investment Solutions as well as directing ongoing market research and contributing to the development of proprietary products. Sean is a member of the Clark Capital Board of Directors, the Investment Committee and the Management Committee. He graduated from the University of Delaware, earning a B.S. and an M.A. in Economics. Sean is a Chartered Financial Analyst and a member of the CFA Institute (formerly AIMR) and the Financial Analysts of Philadelphia, Inc. Sean is considered an industry expert and is often asked to appear on CNBC and Bloomberg television to share his views on the market. In addition, Sean has been featured in a number of articles in nationally distributed business journals and newspapers.

Greece and Puerto Rico Spark Global Volatility

THE GREEK TRAGEDY UNFOLDS BEFORE OUR EYES

More than five years after first entering investors' view, the Greek drama has again hit center stage and has investors fretting about a market collapse. The European authorities and Greek officials have failed to negotiate an agreement of further bailout money prior to the expiration of the current bailout program on June 30. A big part of the problem is that Greek Prime Minister Tsipras has squandered the past five months since he came into office and left Greece in a very vulnerable position. Last Friday night, Tsipras called off negotiations and announced plans to hold a referendum, scheduled for July 5th, on the reform proposals made by Greece creditors. This has brought the Greek economy to a complete halt, with capital controls put in place, long lines at ATMs as Greek depositors try to withdraw money and banks closed for the week after a Bank Holiday was declared.

Greece defaulted on its debt obligations to the International Monetary Fund (IMF) by failing to pay on June 30. Without another bailout Greece won't have the funds to meet its payments to the European Central Bank (ECB) due on July 20th. This doesn't mean that Greece will automatically leave the euro. If the Greek people accept the terms of the bailout in the referendum, which is the most likely outcome according to recent opinion polls, Greek Prime Minister Tsipras has said that the government will abide by voters' wishes. If, on the other hand, the Greek people vote "no," the likely outcome would be an eventual exit from the euro and a return to drachmas.

Some pundits and financial media have said the current Greek event is the equivalent of a Lehman event for the eurozone. In our opinion, that is a stretch, especially since there are firewalls in place and the markets and authorities have had five years to prepare for the prospect of a Greek default. It is very likely that the long-term repercussions from Greece defaulting and leaving the eurozone, if it happens, would be minimal outside of Greece. But the damage to Greece would be monumental. Greece represents only about 1.8% of the eurozone economy, so the economic impact would be minimal for the rest of Europe. In addition, over the past five years most of Greece's debt has been scrubbed off the books of Europe's banks, either written down or sold to the ECB and other central banks, therefore removing the accelerant that in the past acted as such an efficient mechanism for spreading the crisis throughout Europe and the rest of the world.

It looks like pressure on Greece is mounting as just this morning Tsipras signaled he's ready to end his standoff with creditors as the country gets a taste of financial meltdown. However, German Chancellor Angela Merkel refused to engage until after the July 5 referendum called by Tsipras on budget cuts demanded by creditors. Merkel said

"There can be no negotiations for a new credit program before the referendum," Greece has provided "no basis for talking about any serious measures" to break the deadlock. Rightly so, Merkel and the European finance ministers have been burned by five months of Tsipras' brinkmanship, this just appears to be another negotiating tactic and a ploy to save his job. Merkel has no incentive to negotiate before the referendum. It comes down to the July 5 vote. It looks likely that the Greek populace will vote "yes" to the creditor demands and that likely means the Tsipras government will crumble and Greece would get additional bailout funding. A "no" vote would mean pressure on the Greek banking system would ratchet up quickly, leaving Greece little choice but to consider printing its own money.

Puerto Rico - Trouble on the Island

After a multi-year struggle with an excessive debt burden, the Governor of Puerto Rico has publically stated that the Commonwealth cannot pay back its debt and is likely to run out of cash in July. For years Puerto Rico has closed budget shortfalls by borrowing through the bond market. Unfortunately the economy has continued to decline and the revenue projections made in past years have not materialized.

Up until this past Sunday, the market perception was that Puerto Rico would honor its debts, particularly the general obligation (GO) bonds. Last week, the congress in Puerto Rico voted on a balanced budget and addressing paying their debt service. The consensus was that this would pave the way for a new bond sale in the $1 billion range.

However, yesterday, June 29th the Governor changed his tone and announced that the island cannot pay its debts, catching everyone off guard. The Government Development Bank (GDB) owes over $840 million to banks today and July 1st is the date for an interest and principal payment for most of the issuers on the island. So, as of today, it is unclear if debt service will be paid on July 1.

Here are three points taken from the governor's speech dealing with an effort to resolve this crisis:

1. The governor by executive order has created, "The working Group for the Economic Recovery of Puerto Rico." It appears to be a seven person committee charged with beginning conversations to restructure the public debt. The governor is looking for a postponement of debt payments to creditors in order to re-invest in the economy of Puerto Rico.
2. The governor wants Washington to change chapter 9 of the Bankruptcy Code to provide Puerto Rico with the same protections other jurisdictions have.
3. The governor wants to be exempted from the Jones Act Cabotage Law. This is a maritime law put in place in 1920 to protect the U.S. maritime industry from competition. This act is surrounded by many economic arguments. The ports are an important part of industry in Puerto Rico. The impact of what an exemption would mean is not clear.

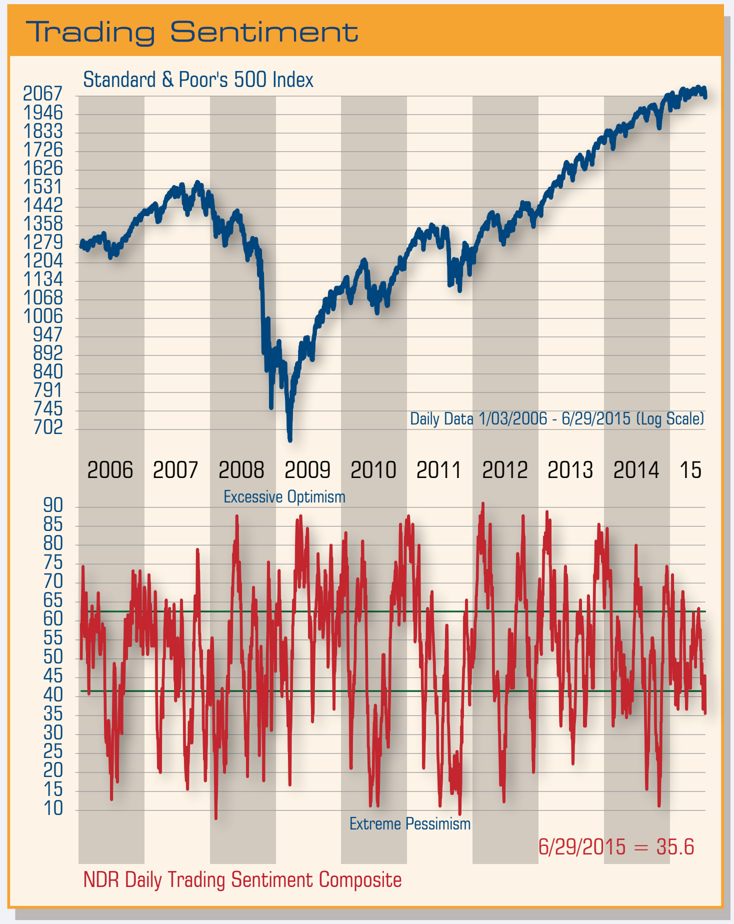
Conclusion

Puerto Rico bonds have been pricing in a very high chance of default for the past year, though most market participants expected the government to be able to kick the can down the road a few more years with hope of assistance from Washington. Municipal market investors were therefore surprised at the rapid decline from a distressed situation to a potential default. The jolt to the market was due to the sudden write down in the GO market. The question is: "Does this become a tail risk event for the municipal high yield market?" If mutual funds are forced to sell Puerto Rico bonds and they cannot, then the funds would look to sell other names. Relying on changes in Washington to help with this situation would seem to involve a long and winding timeline.

Market Impact

There was definitely a sense of fear in the market yesterday as investors fretted over the consequence of a Greek exit from the European Union (EU) and a Puerto Rican default. The uncertainty caused a massive spike in volatility, with the CBOE Volatility Index (VIX) surging 34.5%. Volatility futures also spiked. According to Janus Capital, VIX Futures rose 17.16%, which was the eighth largest daily advance since the inception of the Short Term VIX Futures Index nearly ten years ago. The move was associated with heavy volumes, with approximately $5.8 billion notionally traded in the first and second month VIX futures contracts yesterday, compared to an average daily value traded over the last year of $2.2 billion.

In addition, investor sentiment soured as worries mounted. Stocks fell sharply across the globe yesterday as risk appetites withered. The major stock index in Germany lost 3.6%, Japan lost 2.9%, and the S&P 500 lost 2.1%. The mini panic did help rebuild a wall of worry and a favorite sentiment indicator we look at, the Ned Davis Research Daily Trading Sentiment Composite, slipped to just 35.6% bulls, one of the most extremely pessimistic readings since the October 2014 lows and into a zone where the market has historically performed very well. In addition, the selling pressure took the S&P down into a zone of strong technical support. The S&P 500 closed at 2057.64, just above support in the 2040-2060 area and just above its rising 200-day moving average, which is at 2053. The short-term panic, strong support, and oversold condition should allow the market to find its footing.



Source: Ned Davis Research

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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 free float-adjusted market capitalization index that is designed to measure global developed market equity performance.

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

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

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