ClarkCapital MANAGEMENT GROUP

Navigator® Market Update

K. Sean Clark, CFA, Chief Investment Officer

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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.

GLOBAL TURMOIL WHILE THE U.S. MARKET STAYS HOOKED ON LOW RATES

Equity

The third quarter of 2015 finally brought a long-awaited correction to the global equity markets. By any measure, the correction was well overdue. After four years, the S&P 500 had a better than 10% correction, falling 12.4% from May 21st to August 25th. For the quarter, the benchmark shed 6.9%, its biggest quarterly decline since the third quarter of 2011. As bad as that sounds, large cap U.S. equities were among the least affected by the global carnage. Every country in the MSCI ACWI lost ground in the third quarter, all nine Russell style boxes ended the quarter negative on the year, Chinese equity benchmarks were cut in half, and commodity indices hit six-year lows. The reasons for the carnage are many: fears of a Chinese hard landing, uncertainty over the potential end of the Zero Interest Rate Policy (ZIRP), and the biggest earnings decline since the Great Recession. On the international front, Brazil, Indonesia, Malaysia, Turkey, and Russia have all entered dramatic bear markets, all of which have featured collapsing currencies, as the strong dollar puts each of these countries into funding crises.

Now that the markets have had their biggest corrections since 2011, heading into the fourth quarter, the question is whether the markets are going through a bottoming process ahead of the most bullish seasonal period of the year or setting up for another downleg. Our assessment of the current market environment is that with U.S. recession risks low, the longer-term uptrends still intact, and investor sentiment pessimistic following the declines, a bottoming process is likely. We are giving a bottoming process the benefit of the doubt and expect the global markets to rebound in the fourth quarter with a yearend rally. In the longer-term, we expect the major indexes to make new highs, but that course will almost certainly be more turbulent than the past few years' extreme low volatility.

Fixed Income

The third quarter was a volatile quarter for equity and credit markets alike. The global equity markets suffered a long-awaited correction and that was accompanied by lower-quality credit suffering its largest drawdown since the U.S. debt downgrade in 2011. The Barclays High Yield index fell 6.3% from its high on May 29th through the end of the quarter. As high yield debt has come under pressure, credit spreads (yield on high yield bonds minus 10-year Treasury yield) have widened out to 598 basis points at quarter end, their highest level in three years. For the quarter, the Barclays High Yield Index declined 4.86% while the Barclays Aggregate Bond Index rose 1.23%. It was a quarter in which the risk off trade was prevalent. However, the normal risk off benefactors, including Treasury bonds, advanced but not as aggressively given their

low yields and concerns about the Federal Reserve and looming rate hikes.

Most investors expected the Federal Reserve to finally pull the trigger and hike rates in September. However, the Fed decided to punt again and left the overnight bank lending rate unchanged. We are of the opinion it would be better to rip the Band Aid off and hike rates. The Fed has kept rates artificially low for too long and that has forced investors to assume more risk to gain yield and it has distorted asset valuation. A problem now is not if or when the Fed will raise rates, it is the paralyzing discussion about when they will eventually raise rates.

It's one thing to acknowledge that rates are likely to stay low because we are in a deflationary world, but it is another thing altogether to leave rates zero bound. Lower or near zero rates and QE were necessary at the beginning of the Great Recession, but the Fed has now created an environment where the market needs low rates like a junkie needs his next fix. A legitimate fear is that the longer the Fed postpones normalization, the more difficult the return to normal markets is going to be. The Fed needs to rip the Band Aid off sooner rather than later.

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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.

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

The MSCI All Country Europe is a free float-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 and 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 dollar-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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