Navigator®
Fixed Income Total Return
K. Sean Clark, CFA®, Chief Investment Officer

Fourth Quarter 2018 — Portfolio Commentary

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 Team and the Executive Team. 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.

THE WHIPLASH MARKET

Investors and asset managers alike are happy to turn the page from 2018 to 2019. Last year was a tough year for the markets. While 2018 started strong on the heels of tax legislation, it then faded as trade tensions, rising interest rates, peak earnings growth, and geopolitical concerns at home and abroad weighed heavily on the global markets. In hindsight, it looks like 2018 turned out to be a year of consolidating the strong gains achieved since the Presidential Election in 2016.

Our expectations coming in to 2018 called for an uptick in volatility and the return of normal market corrections. We have certainly seen both of these expectations realized with risk assets suffering through several declines and the S&P 500 suffering two 10% corrections.

Domestic Equity	Q4 2018	2nd Half 2018	2018
S&P 500	-13.52%	-6.85%	-4.39%
Russell 1000	-13.83%	-7.42%	-4.79%
Russell 2000	-20.21%	-17.35%	-11.03%
Russell 3000	-14.31%	-8.20%	-5.25%
Russell 1000 Value	-11.73%	-6.69%	-8.28%
Russell 1000 Growth	-15.89%	-8.17%	-1.52%
International Equity			
MSCI Emerging Market	-7.47%	-8.49%	-14.58%
MSCI All Country World (ex US)	-11.49%	-10.84%	-14.20%
Fixed Income			
BBgBarc U.S. Aggregate Bond	1.64%	1.65%	0.01%
BBgBarc U.S. Treasury	2.57%	1.96%	0.86%
BBgBarc U.S. Corporate	-0.18%	0.79%	-2.51%
BBgBarc U.S. Corporate High Yield	-4.53%	-2.24%	-2.08%
BBgBarc Municipal	1.69%	1.53%	1.28%

Source: Morningstar Direct

In review, the second half of 2018 was lower for all risk-on asset classes from U.S. equity to foreign equity, high yield debt, and commodities. Risk-off asset classes ended the year higher with Treasuries and investment grade debt benefitting from a flight to safety and municipal bonds ending with the highest returns.

Past performance is not indicative of future results.
This is not a recommendation to buy or sell a particular security. Please see attached disclosures.

Fourth Quarter Attribution

For the quarter, the Fixed Income Total Return (FITR) portfolio outperformed the Bloomberg Barclays Corporate High Yield Bond Index (gross and net of fees) while underperforming the Bloomberg Barclays Aggregate Bond Index. During the period, fixed income markets came under some selling pressure as risk assets in general weakened. While high yield bonds had previously held up well compared to U.S. Treasuries and investment grade corporate debt, the weakness spread to high yield debt as tariff concerns and commodity market weakness impacted the asset class.

As a result, in mid-November, the strategy's allocation model shifted from favoring high yield bonds to cash equivalents, ending the year in a defensive position. The change in the portfolio's allocation marked the end of 32 consecutive months allocated to high yield bonds. In the previous quarter's commentary, we said that "the alpha of the strategy is driven by the disciplined and quantitative top down relative strength research process that determines the strategy's sector exposure within fixed income."

Since the strategy's allocation to high yield debt in February 2016 through the mid-November allocation change, high yield bonds outperformed other fixed income sectors. Over that period, the Bloomberg Barclays Corporate High Yield Index gained 27.15%, the Bloomberg Barclays Aggregate Bond Index advanced 2.07%, and the Bloomberg Barclays US Treasury 7-10 Year Index lost 3.35%.

Outlook

We enter 2019 in the midst of a correction with a ton of uncertainty hanging over the markets. While there are risks that the markets and economy face, we believe there is no immediate risk of a recession in the U.S. economy. A lot of the same headwinds that pushed against the market in the second half of 2018 will continue to be concerns in 2019 such as slowing earnings growth, Brexit and the Italian budget standoff with the European Union, the China trade war, the growing budget deficit here in the U.S., and the risk of a Fed policy mistake. However, we feel confident that the U.S. economy will continue growing, although at a slower pace, and expect a 2.3% GDP growth rate in 2019.

In a year that saw a wide variety of asset classes decline in value, credit markets were no exception. For high yield, 2018 goes down as the fifth worst year on record. Since the data begins in 1987, this is only the fourth year where total return has been negative for both investment grade and high yield bonds. The only other years were 1994 (when the Fed surprised the markets and aggressively hiked rates), 2008 (the global credit crisis), and 2015 (when commodity weakness drove asset prices lower).

With the major central banks data-dependent, we anticipate another volatile year for credit, which we believe requires an active approach to managing fixed income. The current correction should be viewed within the context of continued economic expansion and once the correction runs its course, the secular tailwinds for the market should kick in and a new cyclical bull market will begin.

Source: Bloomberg, FactSet, Moody's Corporation

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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 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 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 Russell 2000 Index measures the performance of the 2000 smallest U.S. companies based on total market capitalization in the Russell 3000, which represents approximately 11% of Russell 3000 total market capitalization.

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

The volatility (beta) of a client's portfolio may be greater or less than its respective benchmark. It is not possible to invest in these indices.

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

The Bloomberg 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 BofA Merrill Lynch U.S. High Yield Index tracks the performance of below investment grade U.S. dollar-denominated corporate bonds publicly issued in the U.S. domestic market.

The Bloomberg Barclays 7-10 Year Treasury Index tracks the investment results of an index comprised of the U.S. Treasury bonds with remaining maturities between seven and ten years.

The Bloomberg Barclays 20+ Year Treasury Index tracks the investment results of an index comprised of the U.S. Treasury bonds with remaining maturities greater than twenty years.

The Bloomberg Barclays Long-Term Treasury Index tracks the performance of the long-term U.S. government bond market.

The Bloomberg Barclays U.S. Corporate High-Yield Index covers the U.S. 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.

The Bloomberg Barclays U.S. Treasury Bond Index is an issuances-weighted index measuring the performance of the U.S. Treasury bond market, one of the largest and most liquid government bond markets in the world.

Bloomberg Barclays U.S. Aggregate Bond Index: The index is unmanaged and measures the performance of the investment grade, U.S. dollar denominated, fixed-rate taxable bond market, including Treasuries and government-related and corporate securities that have a remaining maturity of at least one year.

MSCI All Country World Index is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. The MSCI ACWI is maintained by Morgan Stanley and is comprised of stocks from both developed and emerging markets.

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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