Clark Capital Management Group

Portfolio Commentary

Navigator® All Cap Core U.S. Equity

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Survival Requires Change

The global equity bear market made significant negative progress in 2020's 1st quarter as the COVID-19 virus spread exponentially from China through Europe and to the U.S. Global infections neared 900,000 by quarter-end (they are up to 1.5 million now), with the U.S. leading the way with nearly 200,000 cases (400,000 now). Global economic expectations have been devasted with many expecting Q2 2020 U.S. GDP declines in excess of -15%. Q1 2020 GDP growth may also be reported as negative as many states and large cities began "shelter-in-place" restrictions in mid-March.

Drastically lower economic growth expectations spread quickly to credit and equity markets. Uncertainty and fear spiked the S&P 500 Volatility Index to a record 82.89 coincident with the expansion in the high-yield corporate bond spread to 10.62%. From their highs to the March 23, 2020 low, the S&P 500 and the Russell 2000 declined 34% and 44%, respectively.

Flatten the Curve

For the greater societal good, humans worldwide have either voluntarily or have been forced to engage in isolation measures thus enduring economic, social, physical and mental suffering to fight the COVID-19 virus. Our coordinated efforts of social distance, shelter-in-place and work- from-home have appeared to "flatten the curve" of new infections/day. Hopefully, our coordinated sacrifice will both reduce the stress on the healthcare system and bide time for virologists to discover and manufacture a vaccine.

For many introverts, social distancing has been a life-long practice and thus the current social regime is not so burdensome. For extroverts starved for frequent human interaction however, new societal behaviors can be painful or stressful. While for most of us, any change in our daily routines is difficult, my biggest concern is for those who suffered job loss. Unfortunately, the March Employment Report confirmed that a recession began in March as nonfarm payrolls fell by 701,000, or the most since March 2009.

As many non-essential businesses have shuttered their doors during the preponderance of current shelter-in-place restrictions, employers will continue their effort to control labor costs. Efforts have included temporary layoffs, shortened work weeks, and the conversion of full-time workers to part-time employees. The personal and familial damage associated with unemployment can be extraordinary, and thus a quick and forceful countercyclical/counter pandemic response is critical.

Trillions and Trillions

Fortunately, the coronavirus pandemic has been met with quick and forceful global monetary and fiscal policy responses. All of the world's major central banks have committed to providing the liquidity needed to ensure smoothly functioning credit markets by executing open-ended asset purchases and by driving short-term lending rates to zero.

On February 16th, the U.S. Fed, for instance, lowered the federal funds rate to 0-0.25% and then committed to increasing its balance sheet by more than $1.1 trillion in just two weeks. Global fiscal stimulus is also providing a needed economic backstop to combat the virus as Germany intends to provide programs representing of about 5% of GDP. Japan approved a nearly $1 trillion plan or 20% of GDP and the US $2+ trillion CARES act should be 10% of GDP.

Enormous global stimulus combined with social constraints and their initial impact on new infection rates is beginning to give equity investors much needed visibility as the length and depth of the current virus crisis and its impact on economic growth.

All Cap Focused on Survive and Thrive

For the first quarter of 2020, the Navigator® All Cap Core U.S. Equity strategy had a return of -25.42% (-26.03% net) vs. a -20.90% loss in the Russell 3000 Index. Our positioning in Healthcare and Materials helped relative performance while our positioning in Information Technology and Consumer Discretionary acted as a drag in the first quarter of 2020.

Portfolio holdings in the Hershey Company and Amazon.com helped relative performance while holdings in Alaska Air Group and Continental Resources hurt performance. During the quarter, the strategy was overweight large-cap companies with market capitalizations above $15 billion. The value and quality characteristics of the All Cap strategy remain solid in comparison to the S&P 500 as it possesses a lower P/E of 15.8 vs. 16.6 and lower earnings variability combined with higher gross and net profit margins with similar business growth characteristics.

All Cap continues to focus on the highest quality companies throughout the U.S. market capitalization range from $2 billion to $1 trillion. As investors have indiscriminately sold many value and small/mid-cap companies without regard to their financial statements or business prospects over the first quarter (and last 3 years), we believe this strategy has a unique opportunity to benefit from a mispricing of these securities relative to their value in the past. As of mid-March, large-cap value stocks were trading at 4.5 standard deviations away from their normal relationship to the rest of the equity market. Similarly, small and mid-cap companies were trading at extreme long-term relative value discounts.

Ticker	Quarter Ending March 31, 2020	Average Weight (%)	Contribution to Return (%)
Top 5 Contributors			
HSY	Hershey Company	0.29	0.25
AMZN	Amazon.com, Inc.	1.55	0.14
REGN	Regeneron Pharmaceuticals, Inc.	0.36	0.10
MSFT	Microsoft Corporation	2.80	0.07
UTX	United Technologies Corporation	0.67	0.03
Top 5 Detractors			
ALK	Alaska Air Group, Inc.	1.47	-1.45
CLR	Continental Resources, Inc.	0.91	-1.41
EAT	Brinker International, Inc.	1.16	-1.16
PHM	PulteGroup, Inc.	2.01	-1.07
JLL	Jones Lang LaSalle Incorporated	2.34	-1.06

Source: Factset. For illustrative purposes only. Past performance does not guarantee future results. The holdings identified do not represent all of the securities purchased, sold or recommended for advisory clients. In the chart above, "weight" is the average percentage weight of the holding during the period, and "contribution" is the contribution to overall performance during the period. To obtain the calculation methodology and a list showing every holding's contribution to the overall composite during the period, contact: PortfolioAnalytics@ccmg.com.

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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 VIX Index is a volatility index derived from S&P 500 options, with the price of each option representing the market's expectation of 30-day forward-looking volatility. The resulting VIX index formulation provides a measure of expected market volatility on which expectations of further stock market volatility in the near future might be based.

The Russell 2000 Index measures the performance of the 2000 smallest U.S. companies based on total market capitalization in the Russell 3000, whichrepresents 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 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.

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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