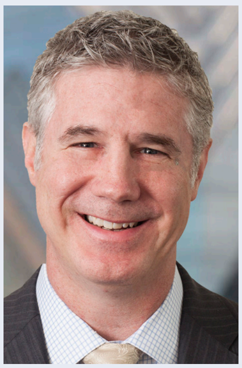
Portfolio Commentary

Navigator® Fixed Income Total Return

Author



K. Sean Clark, CFA®
EVP, Chief Investment Officer

Navigate Your Future. Enjoy the Journey.

Coronavirus Turmoil

The U.S. economy came into the year on solid footing with jobless claims and the unemployment rate hovering near 50-year lows, and housing starts and building permits hitting cycle highs. It appeared that the U.S. economy was going to continue its record long expansion, but that all changed quickly. A global recession and bear market took hold in March as governments around the world implemented social distancing and "shelter-in-place" restrictions to slow the spread of the COVID-19 pandemic.

This is something that we have never seen before as it is a combination of a global health and economic crisis, that led to a market liquidity crisis. As the quarter came to a close, there were 900,000 global cases of the virus with the U.S. leading the way with nearly 200,000 cases. Countries representing an estimated 92% of global GDP are under some form of social distancing, which caused a sudden stop to economic activity to the likes of which we have never seen before. The U.S. economy will suffer its largest ever quarterly decline in GDP in the second quarter, likely -15% or worse.

The Federal Reserve has gone all in, pulling out their entire playbook from 2008 and executing it in a matter of weeks. They dropped interest rates to the zero bound, massively stepped into the repo market, established increased dollar swap lines, a Commercial Paper Facility, infinite QE, MM Liquidity Facility, Primary Market Corporate Credit Facility, and they are buying short duration municipal debt and corporate debt. The Fed's balance sheet has swelled to a record high and is likely to hit $9 trillion by year end. Monetary policy followed with a $2 trillion fiscal stimulus package aimed at delivering relief for businesses and workers affected by the economic shutdown.

No risk asset class was spared in the carnage as the turmoil roiled both the equity and fixed income markets. The S&P 500 experienced its fastest ever slide into bear market territory from new all-time highs, falling almost 34% from peak to bottom, before rallying into month end. In the midst of the decline, volatility spiked with the CBOE Volatility Index hitting it highest level ever. For the quarter, the S&P 500 declined 19.6%, the MSCI All Country World Index fell 23.4%, and the Bloomberg Barclays U.S. Corporate High Yield Index declined 12.68%.

Treasuries were the main benefactor of the risk-off environment as yields across the curve sank to record lows with the 10-year U.S. Treasury yield hitting a low of 40 basis points on March 9th. The Bloomberg Barclays U.S. Aggregate Bond Index gained 3.15% and the Bloomberg Barclays U.S. 7-10 Year Treasury Index gained 10.15% during the quarter.

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

First Quarter Attribution

Fixed Income Total Return came into 2020 fully allocated to high yield as risk asset classes enjoyed strong momentum from a record long economic expansion and bull market. However, the strategy had several allocation changes during the quarter as the investing environment changed as a result of COVID-19 spreading and roiling the markets.

The High Yield Index hit a record high on February 20th and just four trading days later, Fixed Income Total Return began de-risking with COVID-19 fears hitting the markets as concerns mounted that the virus was accelerating outside of China. At that point, high yield bonds had held up well and the allocation shift was more a result of Treasury strength than high yield weakness. The strategy sold half of its high yield exposure and bought intermediate term U.S. Treasuries.

On March 9th, the strategy de-risked further as weakness in credit and astonishing strength in U.S. Treasuries prompted a further allocation shift. The strategy sold the remaining high yield exposure and its intermediate-term U.S. Treasuries with yields hitting record lows, rolling down into 2-year U.S. Treasuries.

While the strategy was in a risk-off position, credit conditions deteriorated with high yield bonds pressured along with deteriorating economic expectations. Credit spreads of high yield bonds over Treasuries surged to 1100 basis points and yields on the High Yield Bond Index rose to 11.69%. Both spreads and yields on high yield bonds hit their highest levels since the 2008/09 Credit Crisis.

The strategy returned to a risk-on position in late March as the markets staged a remarkable recovery rally. Aggressive monetary and fiscal stimulus plans settled the markets, with credit stabilizing and risk assets staging a recovery. The stabilization in credit markets turned our Fixed Income Total Return models positive on high yield debt, and as a result, the strategy allocated back into high yield bonds, where it stands today.

Amidst the turmoil, it was a relatively good quarter for Fixed Income Total Return. For the quarter, the strategy handily outperformed the Bloomberg Barclays U.S. Corporate High Yield Index (gross and net of fees) and underperformed the Bloomberg Barclays U.S. Aggregate Bond Index (gross and net of fees).

Outlook

In our opinion, the outlook for the markets is dependent on several factors:

- Stabilization or flattening of the infection rate curve
- Sufficiently large global monetary and fiscal stimulus
- Improvement in credit conditions

There is no doubt that economic data is going to deteriorate further and that the economy is facing its worst quarterly contraction in history. We are already seeing the signs of economic damage with nearly 10 million people filing for first time unemployment benefits during the last two weeks of March. We know that the news will get worse before it gets better.

We expect second quarter GDP to contract between 15-20% and then begin to stabilize as social distancing measure are relaxed, the record amount of global stimulus takes hold, and credit conditions show signs of improvement. At some point, the markets will look past the economic chasm because markets are forward looking. The layoffs, downgrades and defaults won't be a surprise—markets typically bottom before the worst of the news is out.

As always, we continue to utilize our disciplined investment process, using a relative strength approach to seek higher returns while managing risk. We believe this tactical approach to fixed income can help clients maintain a durable portfolio through various market conditions, helping them stay on track to reach their investment goals.

The views expressed are those of the author(s) and do not necessarily reflect the views of Clark Capital Management Group. The opinions referenced are as of the date of publication and are subject to change due to changes in the market or economic conditions and may not necessarily come to pass. There is no guarantee of the future performance of any Clark Capital investments portfolio. Material presented has been derived from sources considered to be reliable, but the accuracy and completeness cannot be guaranteed. Nothing herein should be construed as a solicitation, recommendation or an offer to buy, sell or hold any securities, other investments or to adopt any investment strategy or strategies. For educational use only. This information is not intended to serve as investment advice. This material is not intended to be relied upon as a forecast or research. The investment or strategy discussed may not be suitable for all investors. Investors must make their own decisions based on their specific investment objectives and financial circumstances. Past performance does not guarantee future results.

This document may contain certain information that constitutes forward-looking statements which can be identified by the use of forward-looking terminology such as "may," "expect," "will," "hope," "forecast," "intend," "target," "believe," and/or comparable terminology (or the negative thereof). Forward looking statements cannot be guaranteed. No assurance, representation, or warranty is made by any person that any of Clark Capital's assumptions, expectations, objectives, and/or goals will be achieved. Nothing contained in this document may be relied upon as a guarantee, promise, assurance, or representation as to the future.

S&P Global Ratings issue credit rating is a forward-looking opinion about the creditworthiness of an obligor with respect to a specific financial obligation, a specific class of financial obligations, or a specific financial program (including ratings on medium-term note programs and commercial paper programs). It takes into consideration the creditworthiness of guarantors, insurers, or other forms of credit enhancement on the obligation and takes into account the currency in which the obligation is denominated. The opinion reflects S&P Global Ratings' view of the obligor's capacity and willingness to meet its financial commitment as they come due, and this opinion may assess terms, such as collateral security and subordination, which could affect ultimate payment in the event of default.

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.

A S&P 'BBB' rated obligation exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to weaken the obligor's capacity to meet its financial commitments on the obligation.

Fixed Income securities are subject ro certain risks including, but not limited to: interest rate (changes in interest rates may cause a decline in market value or an investment), credit, prepayment, call (some bonds allow the issuer to call a bond for redemption before it matures), and extension (principal repayments may not occur as quickly anticipated, causing the expected maturity of a security to increase).

Non-investment trade debt securities (high yield/junk bonds) may be subject to greater market flunctuations, risk of default or loss of income and principal than higher-rated securities.

The CBOE Volatility Index, known by its ticker symbol VIX, is a popular measure of the stock market's expectation of volatility implied by S&P 500 index options.

The MSCI All Country World is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world.

The 10 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 10 year. The 10 year treasury yield is included on the longer end of the yield curve. Many analysts will use the 10 year yield as the "risk free" rate when valuing the markets or an individual security.

The Bloomberg Barclays US Treasury Index measures US dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury.

The Bloomberg Barclays US Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate 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. 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.

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.

Clark Capital Management Group, Inc. reserves the right to modify its current investment strategies and techniques based on changing market dynamics or client needs. The information provided in this report should not be considered a recommendation to purchase or sell any particular security, sector or industry. There is no assurance that any securities, sectors or industries discussed herein will be included in an account's portfolio.

Clark Capital Management Group, Inc. is an investment adviser registered with the U.S. Securities and Exchange Commission. Registration does not imply a certain level of skill or training. More information about Clark Capital's advisory services and fees can be found in its Form ADV which is available upon request.

CCM-505