# Portfolio Commentary

## Navigator® Opportunity Update

Author

**Mason Wev, CFA®, CMT®**
*Portfolio Manager*

Navigate Your Future. Enjoy the Journey.

# COVID-19 Feeds Dislocations Between Winners and Losers

Investors' burgeoning hope and subsequent buying frenzies led to a massive 20% rebound in the S&P 500 and other risk assets during the second quarter. Under the surface, however, there remain huge gaps between large-cap growth and Technology and most of the rest of the stocks and businesses in the everyday economy. With many limited to working from home, technology usage is more essential than ever, and its stock market value and relative strength reflect its importance. However, the massive spike in joblessness and existential struggles of industries like hotels, airlines, and restaurants show how deep and broad the sudden recession's effects are.

Stock market history reveals that you should avoid equities when their earnings are peaking and buy them when the bottom has dropped and earnings have become losses. The S&P 500 expected earnings growth have previously fallen below zero only four times– in 1991, 2001, 2008 and 2009, and now in 2020. Each of those first three instances have been during or after bear markets and recessions and proved to be excellent buying opportunities for stocks.

Today we face a recession and unemployment at 11.1%. As the industries hardest hit by the shutdown return to and establish normal operations and earnings, there is an exceptional opportunity to ride the wave of the earnings recovery. We believe that for those hard-hit industries, that path will be as true this time as it has been in the past. However, the size and scope of 2020's market rebound has left the S&P 500 not far from its pre-pandemic highs, but now with an economy in recession, high unemployment, and an uncertain path back towards normalcy. Much of the gains and recovery that happen after a recession appears to have occurred, at least in the less vulnerable sectors and segments of the economy. That leads us to believe that the huge performance dispersion between growth and value, and between Technology and the rest of the economy, will continue. We believe tactical and flexible trading investment strategies and risk management will be essential.

How did Clark Capital's strategies fare during the quarter? Were they able to enjoy the risk-on gains and keep up? Our Style Opportunity strategy favored large-cap growth during April and May, but then was drawn into mid- and small-caps, and value stocks, as investors bet on a V-shaped recovery. That very quickly proved to be unlikely. While the strategy produced plentiful gains, it lagged in June when its recovery reversed.

Tactical strategies that reduce risk and focus on defense and capital preservation, such as Fixed Income Total Return and Global Tactical, were able to de-risk in late February and early March before re-entering the market on March 27th. They participated in the rally and owned equities or high yield for almost all of the second quarter; however, as credit markets showed signs of stress in June, these portfolios de-risked into U.S. Treasuries. Our Alternative Opportunity portfolio produced solid gains and was greatly aided by Gold and precious metals.

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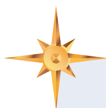

## Sector Opportunity Portfolio

The Sector Opportunity portfolio uses a relative strength methodology to rank the top performing sectors over the intermediate-term. The Sector portfolio began the quarter owning only broad Technology, Healthcare, and the S&P 500 (IVV). As the recovery rally took hold in April and May, we sold out of Healthcare and added risk-on sectors, most notably Consumer Discretionary (VCR), Homebuilders (XHB), Retailing (XRT), and Online Retail (IBUY) from the Consumer Discretionary sector. Online Retail has become a favorite with investors; it already had the general secular trend towards online retail and away from brick and mortar working in its favor. The COVID-19 pandemic and its effects magnified and accelerated this trend.

At the same time, the Retailing ETF, which owns many of the brick and mortar retailers that have suffered during the shutdown, also showed up in our rankings and became a holding. A shift into Consumer Discretionary and retailers right as a recession has begun might seem out of phase, but in fact the historical record shows that retailing is one of the best performing sectors during and coming out of a recession. As the rush into value commenced in May and early June, the portfolio had sold Technology and only owned Semiconductors. However, Technology (VGT) strength snapped back and made new relative highs as June concluded. The portfolio now devotes 43% to Technology, 40% to Consumer Discretionary, and the remainder to the S&P 500. Here were some further developments in the portfolio during the quarter:

- Technology has been unparalleled in its outperformance and contribution to broad market gains. It must be held in size just to keep up with broad passive indexes. As of June 30th, Technology beat the S&P 500 Index by 11.6% for the quarter (30.9% vs. 20.3%), by 26.4% for one year (33.8% vs. 7.4%), and tripled the S&P 500's three year annual gain (101.6% vs. 34.4%).
- The portfolio did make a brief foray into Energy, owning broad Energy (VDE) and Oil & Gas Exploration and Production (XOP) during May and June. Energy's relative strength peaked in mid-June, however, as governments began to slow their re-openings, the demand for energy quickly reversed back down.
- Consumer Discretionary (+38.0%), Energy (+33.2%), and Technology (VGT) were the strongest sectors in the second quarter, while Financials (VFH – up 12.8%), Utilities (XLU – up 2.7%), and Consumer Staples (XLP – up 8.5%) lagged the broad market.

| Ticker | Quarter Ending June 30, 2020 | Average Weight (%) | Contribution to Return (%) |
|---|---|---|---|
| **Top 3 Contributors** | | | |
| VGT | Vanguard Information Technology ETF | 23.72 | 8.23 |
| IVV | iShares Core S&P 500 ETF | 14.14 | 5.45 |
| IBUY | Amplify Online Retail ETF | 7.70 | 3.35 |
| **Top 3 Detractors** | | | |
| IJH | iShares Core S&P Mid-Cap ETF | 0.79 | -0.81 |
| VIS | Vanguard Industrials ETF | 1.36 | -0.70 |
| VAW | Vanguard Materials ETF | 2.11 | -0.64 |

*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.*

## International Opportunity Portfolio

The International Opportunity portfolio's stated mission is to allocate tactically between international style, factor, and region ETFs that are displaying significant relative strength (and avoiding those that do not), and in doing so to attempt to outperform the MSCI All Country World Ex-U.S. Index. The portfolio's universe of investments now includes factor, style box, and regional ETFs such as: International Value, Growth, Quality, Small-cap, Currency Hedged, Minimum Volatility, Buyback, and Momentum ETFs, along with Emerging Markets, Emerging Markets Small-cap, and Emerging Markets Minimum Volatility ETFs.

While International markets slightly lagged U.S. markets on the quarter, they at least broadly participated in market gains. U.S. short-term interest rates are now pretty much at zero, and this finally appears to have slowed the dollar's dominance. The dollar surged compared to developed and emerging currencies in the first quarter, but that trend reversed in the second quarter, with emerging currencies showing life. Though the divergences were not as dramatic, our rankings moved towards risk-on and higher beta ETFs as the second quarter developed, selling out of High Quality (IQLT) and Currency Hedged ETFs (DBEF) and purchasing EAFE Small Cap (SCZ) and International Buybacks (IPKW). Looking forward, we see Emerging Markets on the rise, as China's stock market has rebounded after struggling amidst trade and political tensions.

- Among the top performing international ETFs in our universe for the quarter were EAFE Small-cap (SCZ), International Momentum (IMTM), and Emerging Markets (VWO), Currency Hedged (DBEF), EAFE Value (EFV), and EAFE Minimum Volatility (EFAV) were laggards. The broad international benchmark ETF

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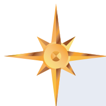

(VXUS) gained 17.8%, so the dispersion and dislocations amongst international ETFs was much smaller abroad than in the U.S.

- International equities have lagged for years, and one of the hardest hit areas has been International Buybacks (IPKW), which declined by 43% between June 2018 and the bottom in March. Since then the ETF has found life, with its focus on the Consumer Discretionary area providing a big boost. We began building a position in May.
- For the quarter, International Buybacks (IPKW) and EAFE Growth (EFG) were the top contributors, while the Eurozone(EZU) and U.S. Small Caps (IJR) were the largest detractors.

| Ticker | Quarter Ending June 30, 2020 | Average Weight (%) | Contribution to Return (%) |
|---|---|---|---|
| **Top 3 Contributors** | | | |
| EFG | iShares MSCI EAFE Growth ETF | 17.29 | 3.76 |
| IVV | iShares Core S&P 500 ETF | 16.19 | 3.66 |
| IMTM | iShares Edge MSCI Intl Momentum Factor ETF | 17.90 | 3.62 |
| **Top 3 Detractors** | | | |
| EZU | iShares MSCI Eurozone ETF | 5.30 | -0.73 |
| IJR | iShares Core S&P Small Cap ETF | 0.67 | -0.38 |
| IJH | iShares Core S&P Mid-Cap ETF | 2.36 | -0.09 |

*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.*

## Style Opportunity Portfolio

The Style Opportunity portfolio began the quarter in a narrow focus on two ETFs: large-cap growth (SPYG) and the S&P 500 itself. Both had proven to be solid defensive vehicles during the sudden decline. The market's rebound began in earnest in early April, and through the month large-cap growth maintained its leadership, as it has before, during, and after the market crash.

Another ETF entered the portfolio in May when we added mid-cap growth (MDYG); it has since maintained its relative strength and has become a portfolio mainstay. May also saw hopes for a V-shaped recovery and "resumption to normal" explode; between May 13th and June 8th small-caps and value stocks staged a furious rally. Mid-cap value (MDYV) and small-cap value (IJS) were up 32.2% and 36.9% over that less than one month period, while the S&P 500 only gained 14.8%. Naturally, value and small-caps rose to the top of our ETF rankings, but the trend would not last, as has all too often been the case after value stocks rallied over the past several years. This time the turnaround was sharp and dramatic, as it soon became clear that a second wave of COVID-19 was hitting America and the economy's re-opening would stall.

Our holdings in value-oriented stocks reversed fast and hard, and we ended up owning the ETFs for less than a month. As June came to an end, the S&P 500 Growth returned to a top holding, and that ETF is the clear performance leader. Its strength does not show signs of ending. The table below shows how each equity the Style Opportunity portfolio held fared during the second quarter and year to date:

| Index or ETF Name | Second Quarter 2020 | Year to Date (thru 06/30/20) |
|---|---|---|
| S&P 500 Index | +20.5% | -3.1% |
| S&P 500 Large Cap Value ETF (SPYV) | +13.0% | -15.6% |
| S&P 500 Large Cap Growth ETF (SPYG) | +26.0% | +8.0% |
| Small Cap Value ETF (IJS) | +21.0% | -24.4% |
| Small Cap Growth ETF (IJT) | +23.4% | -11.8% |
| iShares Momentum Factor ETF (MTUM) | +23.4% | +5.1% |

*Source: Bloomberg. For illustrative purposes only. Past performance does not guarantee future results.*

- Large-cap growth now has an over 19% performance gap vs. the next best equity style, small-cap growth. Large internet and technology names like Apple, Amazon, Microsoft, Google, Facebook, and Netflix have driven S&P 500 returns for years now, with no end in sight.
- The S&P 500 growth (SPYG) and mid-cap growth (MDYG) were the portfolio's top contributors, while mid-cap value (MDYV) and small-cap value (IJS) were leading detractors.
- Among major factors, momentum (MTUM) is closest to large-growth and is up 5.1% year to date. Other factors remain solidly in the red. Minimum Volatility (USMV) is down 6.6%, while High Dividend stocks (HDV) are down 15.2%. Buybacks (PKW) are down 15.7% and High Beta (SPHB) has declined by 12.3%.

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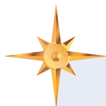

| Ticker | Quarter Ending June 30, 2020 | Average Weight (%) | Contribution to Return (%) |
|---|---|---|---|
| **Top 3 Contributors** | | | |
| SPYG | SPDR Portfolio S&P 500 Growth ETF | 36.49 | 10.10 |
| IVV | iShares Core S&P 500 ETF | 32.81 | 7.93 |
| MDYG | SPDR S&P 400 Mid Cap Growth ETF | 16.41 | 1.90 |
| **Top 3 Detractors** | | | |
| MDYV | SPDR S&P 400 Mid Cap Value ETF | 4.55 | -2.59 |
| IJS | iShares S&P Small-Cap 600 Value ETF | 1.49 | -1.06 |
| IJT | iShares S&P Small-Cap 600 Growth ETF | 3.71 | -0.00 |

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## Global Tactical Portfolio

The methodology of the Global Tactical portfolio uses broad domestic and international equity ETFs as vehicles to own equity risk when our indicators favor taking risk, and defensive U.S. Treasuries or cash to play defense. The portfolio uses the Fixed Income Total Return credit market model as an overlay to manage risk. When the credit market model is positive towards high yield bonds (and thus on credit risk and market risk in general), the portfolio will own broad, ultra-low cost U.S. and International equity ETFs. However, when the credit model turns negative, the portfolio sells equities and owns cash or Treasury bonds that are in line with the Fixed Income Total Return portfolio's holdings.

As the market staged a nearly 20% rally during the quarter, our credit models favored equities and made new highs through April, May, and early June. As June developed, it quickly became apparent the nation faced a resurgence of coronavirus and peak in equity optimism; quickly our credit models began to weaken and on June 29th we sold entirely out of our equity positions and became defensive in U.S. Treasuries.

Below are the results of the portfolio's four aggressive equity holdings and two defensive Treasury holdings for the period that the portfolio became aggressive and fully invested in equities (03/27 to 06/29):

| ETF Name & Ticker | 03/27 – 06/29 |
|---|---|
| SPDR S&P 500 ETF (SPLG) | 20.6% |
| iShares Core S&P Small Cap ETF (IJR) | 23.0% |
| iShares Total International Stock ETF (IXUS) | 19.9% |
| Vanguard World Ex-U.S. International Small Cap ETF (VSS) | 24.6% |
| SPDR Barclays Intermediate-Term Treasury ETF (SPTI) | 0.72% |
| iShares 7-10 Year Treasury ETF (IEF) | 1.24% |

*Source: Bloomberg. For illustrative purposes only. Past performance does not guarantee future results.*

| Ticker | Quarter Ending June 30, 2020 | Average Weight (%) | Contribution to Return (%) |
|---|---|---|---|
| **Top 3 Contributors** | | | |
| SPLG | SPDR Portfolio S&P 500 ETF | 47.71 | 9.35 |
| IJR | iShares Core S&P Small Cap ETF | 20.84 | 4.23 |
| IXUS | iShares Core MSCI Total International Stock ETF | 19.48 | 3.37 |
| **Top 3 Detractors** | | | |
| VSS | Vanguard FTSE All-World ex-US Small-Cap ETF | 9.07 | 2.05 |
| IEF | iShares 7-10 Year Treasury Bond ETF | 0.75 | -0.09 |
| SPTI | SPDR Portfolio Intermediate Term Treasury ETF | 0.75 | -0.01 |

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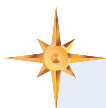

## Alternative Opportunity Portfolio

We recommend that investors view the Alternative portfolio as a source of alternative beta while exposures look to capture available risk premia and tactical trading gains. The strategy is seeks to serve as a diversifier to a traditional portfolio. The portfolio contains a broad mix of themes which breaks down as follows: Alternative-Oriented Mutual Funds and ETFs 50.0%, Commodities and Commodity Equity 15.0%, Tactical Global Equity 11.0%, Fixed Income 11.0%, and Cash 13.0%. The following are some important events that occurred in the portfolio during the quarter:

- The primary purpose of the core liquid alternative portion of the portfolio is to provide non-correlated alternative exposure and to include eight mutual funds (and one ETF) in the alternative credit, long/short equity, long/short commodity, managed futures, options-based, long/short real estate, alternative income, and merger arbitrage areas. We added Long/Short Real Estate and Market Neutral Income during the quarter, looking to reduce correlations to equities within the portfolio's core.
- Alternative investing indexes enjoyed strong returns on the quarter, highlighted by Gold again. The Bloomberg Commodity Index gained 5.1% but is still down 19.4% on the year. Gold (GLDM) was up 13.0% and is up 17.3% on the year, showing gains during both bear and bull markets this year. The HFR X Event Driven Equity Index gained 7.5%. The SG Trend Index, a trend-following managed futures index, lost 3.1% as market trends reversed sharply. Our Alternative portfolio benchmark, the HFRX Global Hedge Fund Index, gained 6.19% and is down 1.1% for the year.
- We owned large-cap growth for much of the quarter, but sold it as it reached its prior February highs. The portfolio continues to own Gold (GLDM at 7%) and Gold Miners (GDX at 4%) but reduced them slightly after sizeable gains. The portfolio expanded its precious metals exposure by adding Silver (SLV); its cycle profile is relatively attractive, and Silver's relative ratios to Gold look to be reversing from extreme levels.
- Brandywine Global Alternative Credit (LMANX), Gold (GLDM) and Gold Miners (GDX) were the top contributors, while Managed Futures (AHLYX), Long/Short Commodities (LCSIX), and Long/Short Real Estate (GUMNX) were detractors.

| Ticker | Quarter Ending June 30, 2020 | Average Weight (%) | Contribution to Return (%) |
|---|---|---|---|
| **Top 3 Contributors** | | | |
| GDX | VanEck Vectors Gold Miners ETF | 4.91 | 2.56 |
| GLDM | SPDR Gold MiniShares Trust | 8.64 | 1.23 |
| SCHG | Schwab U.S. Large-Cap Growth ETF | 3.92 | 1.09 |
| **Top 3 Detractors** | | | |
| LCSIX | LoCorr Long/Short Commodities Strategy Fd Cl I | 6.70 | -0.28 |
| EUFN | iShares MSCI Europe Financials ETF | 0.10 | -0.21 |
| AHLYX | American Beacon AHL Managed Futures Strategy Fund - Y Class | 2.92 | -0.18 |

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## Fixed Income Total Return

The Fixed Income Total Return strategy was very active during the first quarter, de-risking the portfolio out of high yield as the downturn progressed, and eventually on March 27th re-entered high yield at lower prices and higher yields. The portfolio owned high yield for almost the entirety of the second quarter, exiting the position only on June 29th. High yield bonds produced strong returns, especially when compared to Treasuries.

Just as value stocks peaked in relative performance in mid-June, so did high yield bonds. As a second wave of COVID-19 began to spread and the economic re-opening came into question, high yield bonds, particularly the resurgent energy sector, came under stress again. U.S. Treasuries began to outperform and produce small gains, and after a few weeks of the slow drip of a delayed recovery, our credit-based models turned defensive, moving us into U.S. Treasuries.

During 2020 Fixed Income Total Return has been very active within credit, and that activity is summarized below in terms of the average price of the bonds in the S&P 500 High Yield Bond Index:

| Date | Event |
|---|---|
| January 17th | Average high yield bond price peaked at 102.49. |
| February 26th | Sold half of our high yield bond position and bought Treasuries; average price at 101.28. |
| March 9th | Sold other half of our high yield position; average price at 95.56. |
| March 23rd | Markets bottomed; average price at 80.05. |
| March 27th | Re-entered high yield bonds when average price was at 85.29. |
| June 29th | Sold our high yield bond positions at an average price of 96.49. |

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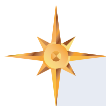

As risk conscious managers, we are first and foremost focused on risk and avoiding substantial loss. Thus, we have de-risked our fixed income exposure despite the fact that high yield bond spreads remain wide and at historically attractive levels. One area that has us particularly concerned has been the poor performance of very low-quality credits, which have been persistently weak amidst a dramatic increase in bankruptcies and whose recovery value has come into question. Our models have indicated that a possible downtrend is in place. We are willing to give up possible upside because our models indicate the potential for serious losses remains. It is a trade we are always content to make, even if it may limit upside at times.

## Sentry Managed Volatility Portfolio

Hedging one's equity exposure during a strong market for equities, or even just a flat market for equities, is an exercise in patience and understanding the proper role of a hedge in a broader portfolio. Sometimes that patience pays off when markets are hit by a sudden shock and unexpected strike of lightning. When the economy ground to a startling halt, the Sentry portfolio's equity hedge and negative correlation to market declines helped reduce the pain in equity portfolios. The global COVID-19 pandemic proved to be an unprecedented disruption, creating a liquidity event across most asset classes, as the S&P 500 collapsed by over 33% between late February and March 23rd. Markets have staged a huge recovery, but the pace and progress of recovery remains uncertain.

We have commented many times how an equity hedge gains from spikes in volatility, but those gains are very fleeting indeed. When the decline becomes a bear market and something much more than a correction, we look to capitalize on those gains, take profits, and employ those monies back into our other equity portfolios, particularly in the Global Balanced and Global Equity ETF Hedged portfolios. Thus, we were able to add some additional equity exposure at relatively attractive prices and if there is a longer-term turnaround, enhance the portfolio upside. We had not gotten the chance to reallocate into equities and act on such a large decline since 2016.

Looking forward, with a massive spike, decline and then a sudden recovery having taken place, does a hedged position have a role in a portfolio? We are currently seeing the lifting of restrictions on travel and conducting business has not led to a return back to January's levels of economic activity. Further disappointments along the health and jobs front are likely, and the uncertainty of a presidential election stands right before us. Volatility is likely over the next few quarters, and investor anxiety as measured by the VIX index remains stubbornly high. We may see another opportunity to take gains on our equity hedge in the second half of 2020.

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The SG Trend Index is a trend-following index that measures managed futures.

The Bloomberg Commodity Index is a highly liquid and diversified benchmark for commodity investments.

Fixed income securities are subject to 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 as anticipated, causing the expected maturity of a security to increase).

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

Foreign securities are more volatile, harder to price and less liquid than U.S. securities. They are subject to different accounting and regulatory standards, and political and economic risks. These risks are enhanced in emerging markets countries.

The HRFX Event Driven Index maintain positions in companies currently or prospectively involved in corporate transactions of a wide variety including but not limited to mergers, restructurings, financial distress, tender offers, shareholder buybacks, debt exchanges, security issuance or other capital structure adjustments. Security types can range from most senior in the capital structure to most junior or subordinated, and frequently involve additional derivative securities.

The HFRX Global Hedge Fund Index is designed to be representative of the overall composition of the hedge fund universe. It is comprised of all eligible hedge fund strategies; including but not limited to convertible arbitrage, distressed securities, equity hedge, equity market neutral, event driven, macro, merger arbitrage, and relative value arbitrage.

The MSCI ACWI ex USA Index captures large and mid cap representation across 22 of 23 Developed Markets (DM) countries (excluding the US) and 26 Emerging Markets (EM) countries*. With 2,206 constituents, the index covers approximately 85% of the global equity opportunity set outside the US.

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 S&P 500 High Yield Corporate Bond Index, a subindex of the S&P 500 Bond Index, seeks to measure the performance of U.S. corporate debt issued by constituents in the S&P 500 with a high-yield rating. The S&P 500 Bond Index is designed to be a corporate-bond counterpart to the S&P 500, which is widely regarded as the best single gauge of large-cap U.S. equities.

The CBOE Volatility Index, or VIX, is a real-time market index representing the market's expectations for volatility over the coming 30 days. Investors use the VIX to measure the level of risk, fear, or stress in the market when making investment decisions.

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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