Portfolio Commentary

Navigator® Fixed Income Total Return

Portfolio Manager

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Markets Remain Resilient

Market Review

Markets have performed exceptionally well in the face of continued Fed tightening, calls for an imminent recession, a regional banking crisis, the debt ceiling debate, and drama around an 11th hour deal to avoid a default on U.S. debt. The markets continued to power ahead in the second quarter, ignoring persistent concerns about inflation, 14 consecutive months of declining Leading Economic Indicators, and the inverted yield curve.

While the Federal Reserve paused and didn't hike interest rates at the June FOMC meeting, they did emphasize that they are data dependent and concerned about inflation. This rhetoric drove interest rates higher and increased the likelihood of further rate hikes later this year. The market is now pricing in a greater than 90% chance that the Fed hikes again in July.

The bear market lows were on October 12th last year and since then, the S&P 500 is up 25.94% on a total return basis. Stock performance has been concentrated in mega-cap growth companies, but we are starting to see the market's participation broaden out. Strong gains to finish the quarter capped a historic rally with one of the best first halves for the market on record.

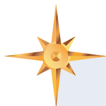
Year to date through June 30th, the S&P 500 is up 16.88%, the best start since 2019, second best this century, and 12th-best since 1926. The Russell 2000 Small Cap Index is up 8.06%, and the MSCI All Country ex-US gained 9.47%. The standout so far has been large-cap growth. The Russell 1000 Growth Index is up 29.01% and is outperforming the Russell 1000 Value Index large-cap value by almost 2400 basis points.

Fixed income has also posted gains following the worst bond market on record. Credit is outperforming duration with the Bloomberg Barclays High Yield Index and Investment Grade Corporate indices up 5.38% and 3.21%, respectively, the Aggregate Bond Index advanced 2.09%, while the 7-10 Year Treasury Index posted a more modest 1.62% gain.

Second Quarter Portfolio Highlights

The primary drivers of Fixed Income Total Return over time are its macro allocations that are guided by our relative strength-based credit risk management models. Those models dictate the strategy's allocation to high yield bonds, U.S. Treasuries, and cash equivalents.

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



- The strategy came into the second quarter allocated to U.S. Treasuries, but by mid-April, credit began to strengthen, and the models began favoring high yield bonds. The strategy remained allocated to high yield bonds from April 13th through the end of the quarter. Over that period, the Bloomberg U.S. Corporate High Yield Index gained 2.06% while the ICE U.S. Treasury 7-10 Year Bond Index lost 2.34%. The strategy picked up a fair amount of relative outperformance compared to U.S. Treasuries.
- Spreads narrowed throughout the quarter as the economy remained resilient in the face of recession fears and inflation pressures moderated.
- CCC and below rated high yield bonds outperformed higher quality high yield bonds, investment grade corporate bonds, and U.S. Treasuries. The outperformance of lower quality debt highlighted the strength of the economy and overall risk-on appetite environment.
- Yields across the U.S. Treasury curve advanced during the quarter, even though the Fed paused at the June FOMC meeting. Expectations are for at least one more rate hike at the July FOMC meeting. As the quarter ended, 2-year yields approached 5% and 10-year yields traded close to 4%.

Positioning and Outlook

Halfway through 2023, calls for recession have fallen on deaf ears and the economy continues to expand on the back of a strong labor market. The strength of the economy resides in the labor market and as long as the labor market remains strong, we believe any chance of a recession will keep getting kicked down the road. We expect economic growth to moderate in the second half of the year with inflation continuing to fall. We believe the Fed is in the very late innings of the rate hike cycle with the market pricing in one more rate hike at the July FOMC meeting. History suggests that yields usually begin declining after the last rate hike.

The stock market is following the script we laid out in our annual Market Outlook with gains front loaded before a potential second half consolidation. Mega-cap growth has led the indices higher, but we are now beginning to see signs of participation broadening out.

At the conclusion of our last quarterly commentary, we stated, "The S&P 500 gained over 7% in the first quarter and that bodes well for the market for the remainder of the year. When the S&P 500 gained more than 7% in the first quarter, the full year has been positive every time 16 of 16 cases with an average 23.1% gain. In addition, in the 11 previous cases when the S&P 500 fell the previous year and rallied in the first quarter, over the last nine months of the year the index was up every time by a median of 11.2%."

The major indices have also now put in three consecutive quarters of gains. Strong credit conditions, record amounts of cash sitting in money market funds, and declining inflation remain some of the underpinnings of this market. The strong rebound has left the S&P 500 about 10% below its all-time high and we think it eclipses that level over the next 12 months. When the S&P 500 rose at least 10% over the first six months, the index rose in the following six months 75% of the time by a median 9.7%.

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The manager utilizes a proprietary investment model to assist with the construction of the strategy and to assist the manager with making investment decisions. Investments selected using this process may perform differently than expected as a result of the factors used in the model, the weight placed on each factor, and changes from the factors' historical trends. There is no guarantee that Clark Capital's use of a model will result in effective investment decisions.

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.

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 Bloomberg Barclays US Treasury: 7-10 Year Index measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury with 7-9.9999 years to maturity.

The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate pass-throughs), ABS and CMBS (agency and non-agency).

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

The Bloomberg Global Investment Grade Corporate Bond Index is a rules-based market-value-weighted index engineered to measure the investment-grade, fixed rate, global corporate bond market.

The Russell 1000 Index is a stock market index that tracks the highest-ranking 1,000 stocks in the Russell 3000 Index, which represent about 93% of the total market capitalization of that index.

Russell 1000 Value Index refers to a composite of large and mid-cap companies located in the United States that also exhibit a value probability.

The Russell 2000 Index is a small-cap U.S. stock market index that makes up the smallest 2,000 stocks in the Russell 3000 Index.

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.

A CCC bond rating is considered to be speculative or junk grade, indicating that the issuer has a high risk of defaulting on its debt obligations. CCC credit ratings are often given to companies that are experiencing financial difficulties or have a high level of debt.

A Leading Economic Indicator is a measurable set of data that may help to forecast future economic activity.

A Treasury yield is how much investors can earn when they purchase one of those government debt obligations.

The ICE U.S. Treasury 7-10 Year Bond Index is part of a series of indices intended to assess the U.S. Treasury market. The Index is market value weighted and is designed to measure the performanceof U.S. dollar-denominated, fixed rate securities with minimum term to maturity greater than seven years and less than or equal to ten years

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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