Clark Capital Management Group

Portfolio Commentary

Navigator® Taxable Fixed Income

Portfolio Manager

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Interest Rate Cut Hopes Lead to Strong Year End Rally

Market Review

The Federal Reserve remained on pause throughout the 4th quarter. In December, the dot plot revealed that the Fed was forecasting 4 cuts throughout 2024. Core Personal Consumption Expenditures (PCE), the Fed's preferred inflation gauge, continued its trend lower toward the Fed's 2% target. This pivot from a hiking environment to an expected cutting environment, coupled with the continued decrease in inflation expectations, drove interest rates lower throughout the quarter and specifically the last month and a half of the year.

After briefly hitting 5% in October, the 10-year Treasury rallied more than 100 basis points into year end and closed the year at 3.88%. The 2-year Treasury also rallied, but still lagged the 10-year, closing out the year at 4.25%, more than 75 basis points lower on the quarter.

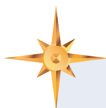
The market is currently pricing in more cuts in the Fed Funds Rate than the Fed is projecting, closing the year with expectations for 6 cuts in 2024, with the first one coming in March. Credit spread levels, as measured by the Bloomberg Barclays Intermediate US Corporate Bond Index, followed the Treasury move lower. After underperforming in October, the bond market rallied significantly during the last 2 months of the year to close the quarter 34 basis points tighter. This also brought credit spreads to their lowest level in two years.

Overall, this combined move in interest rates and credit spreads left the total return on the intermediate corporate bond market at positive 5.86% for the quarter and 7.29% for the year. After a historically poor start to 2022, the intermediate bond market has now returned over 10% over the last 15 months.

Fourth Quarter Portfolio Highlights

- The duration of the portfolio was slightly below 4 years, which was marginally lower than the position that it has been in all year. It is also underweight the index.
- The best-performing sector for the quarter on a total return basis was the Telecommunications sector. The continued improvement in credit fundamentals combined with higher average duration in the sector led to this outperformance and reversal from the previous quarter. The worst performing sector for the quarter was Technology. This sector has become one of the higher quality, lower credit spread sectors in the market and thus did not participate in the spread rally to the same extent as lower rated, higher yielding names did.

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 Telecommunications sector also added the most value to the portfolio during the quarter. The portfolio benefited its overweight position in the sector combined with the higher duration, as the portfolio held mostly longer 10-year bonds.
- The Energy sector reversed its gains from the previous quarter and was the largest detractor from the portfolio. Two of the three largest mergers ever in the sector happened during the quarter. This increased expectations that there would be continued M&A. Credit spreads underperformed the overall market based on these assumptions.

Positioning and Outlook

The main themes of the portfolio remained consistent through the first two months of the quarter but began to shift slightly as the year ended. Most of the credit risk remained in the very front end (0-3 years) of the portfolio in an attempt to take advantage of the higher yields and income that these bonds provide.

The slight shift that began during December was the move from 10-year bonds to bonds with 5-7 years in duration. The difference in yield between these two parts of the credit curve narrowed during the quarter to a point where investors weren't being fully compensated for the added risk from the longer bonds. As the bonds on the very front end mature throughout the coming months, the proceeds should be reinvested in that 5-7 year portion of the curve, adding to this new overall strategy and position.

The portfolio continues to seek to maximize yield and income in the front end while owning names in the middle to slightly longer part of the interest rate curve. We believe this strategy can help ensure that positive total returns can be realized with a continued rally in interest rates.

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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.

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 ecurity to increase).

Personal consumption expenditures (PCE) is the primary measure of consumer spending on goods and services in the U.S. economy.

The Bloomberg Barclays US Intermediate Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by US and non-US industrial, utility and financial issuers that have between 1 and up to, but not including, 10 years to maturity.

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 2 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 2 years. The 2 year treasury yield is included on the shorter end of the yield curve and is important when looking at the overall US economy.

The 10-Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 10 years.

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