



## Portfolio Commentary

Navigator<sup>®</sup> Fixed Income Total Return

## Portfolio Manager



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## Goldilocks Like

## Market Review

The investing environment year to date has been goldilocks like. The economy has been strong, fueled by labor market gains, seven consecutive quarters of GDP growth, declining inflation, and corporate earnings are at record highs. There is an almost universal belief that the U.S. economy is on course for a soft landing. The two most compelling arguments fueling that belief are easing inflation and a persistently strong labor market, although there are emerging signs of a cooling in the labor market.

Inflation continues to moderate. The Consumer Price Index (CPI) hit 3.3% year over year while the Producer Price Index (PPI) has risen just 2.2% year over year, down from peaks of 9.1% and 11.1%, respectively. It did tick higher to start the year, but we never expected inflation to come down in a straight line. Meanwhile, the Fed's preferred inflation gauge, Core PCE, has moderated to 2.6% year over year, the lowest reading in over 3 years and should give the Fed further comfort that the inflation trajectory continues to cool.

Equity markets have enjoyed strong, but very mixed gains year to date, led by large-cap U.S. indices with the S&P 500 gaining 15.29%, the Russell 2000 Index of small-cap stocks up only 1.79%, and the international stocks up 5.69%. Large-cap growth has led all styles with a sharp focus on Technology and high cash flow margin companies outpacing all others.

Fixed income returns were mixed with credit enjoying gains and duration largely flat after suffering losses early in the year as rates advanced and the curve shifted higher. The Bloomberg U.S. Corporate High Yield Index gained 2.58%, while the Aggregate Bond Index was down 0.71%, and the 7-10 Year Treasury Index declined by 0.86%. Rates moved higher as Fed officials squashed immediate rate cut expectations.

The gains have not all come in a straight line, and there are pretty significant differences between stocks of different market capitalizations. While the S&P 500 Index is trading in new high territory, the same index on an equal-weighted basis has lagged. Small-cap stocks peaked on 11/8/2021 and are still 12.90% below that high. Meanwhile, the cumulative advance-decline line is also lagging. These divergences deserve to be monitored and indicate that risks of a correction may be elevated if they persist.

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



## Second Quarter Portfolio Highlights

The primary drivers of Fixed Income Total Return over time are its macro allocations that are driven by our relative strength credit risk management models. Those models dictate the strategy's allocation to high yield bonds, U.S. Treasuries, and cash equivalents. Fixed Income Total Return entered and exited the quarter allocated to high yield. The strategy has been invested in high yield bonds since early November 2023 as credit has remained firm given the strength of the U.S. economy and risk assets.

- High yield bond indices ended the quarter near new all-time highs, up 1.09% during the quarter.
- Fixed income markets were mixed during the quarter. Broad-based high yield advanced 1.09%, CCC-rated bonds declined 0.43%, and 7-10 Year Treasuries lost 0.15%.
- Federal Reserve rate cut expectations shifted marginally during the quarter. At the start of the quarter the fed funds futures market was pricing in 2-3 cuts, with the first cut happening in July. At the end of the quarter, the market was pricing in 1-2 cuts, with the first cut expected in either September or November.
- The Treasury yield curve steepened through the quarter as expected rate cuts were pushed forward.
- High yield credit spreads remain historically tight, supporting the soft landing scenario.

## Positioning and Outlook

We are increasing our target for the S&P 500 to 5800 based on increasing forward earnings estimates, continued economic growth, and the likelihood of rate cuts in the second half of the year. We are also looking for market participation to broaden out.

Coming into the year, the market was expecting 6-7 rate cuts. Fast forward to today, and the fed funds futures market now expects the Fed to cut rates twice this year. There is an outside chance of a July policy move; however, given that the annual Jackson Hole Economic Policy Symposium is held in August, and the Fed uses that event to shape and message future policy, it is more likely that the first rate cut happens at the September FOMC meeting.

Economic growth remains firm, but slower than last year. High yield bond indices are trading at new all-time highs and credit spreads are very tight, indicating little evidence of stress in the economy. Credit spreads normally widen out considerably in advance of economic stress and that is not the case currently. So, our base case now remains that we will have continued economic growth in a soft landing scenario into the near future.



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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 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.

The US High-Yield Market Index is a US Dollar-denominated index which measures the performance of high-yield debt issued by corporations domiciled in the US or Canada.

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 iShares Russell 1000 Value ETF seeks to track the investment results of an index composed of large- and mid-capitalization U.S. equities that exhibit value characteristics.

The iShares Russell 1000 Growth ETF seeks to track the investment results of an index composed of large- and mid-capitalization U.S. equities that exhibit growth characteristics.

The Consumer Price Index (CPI) measures the overall change in consumer prices based on a representative basket of goods and services over time.

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 performance of 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 chartered financial analyst (CFA) charter is a globally-recognized professional designation offered by the CFA Institute, an organization that measures and certifies the competence and integrity of financial analysts.

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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