Clark Capital Management Group

# Benchmark Review
## & Monthly Recap

# Second Half Off to a Strong Start – Broad Gains Enjoyed in July

## Equity Markets

Equity markets continued to climb the wall of worry in July. After coming off the best quarter in decades in the second quarter, stocks advanced further to start the second half of 2020. Just over four months after the S&P 500 hit its 2020 low on March 23, a -34% drop from the all-time high in late February, this index went back into positive territory year to date with gains in July. The largest, tech-focused companies have driven this index and the broader markets higher. The NASDAQ Composite has been a clear beneficiary of these strong gains as it led U.S. markets in July, has dominated results year to date, and put in new all-time highs last month.

In July, the CBOE Volatility Index or VIX Index, fell to its lowest level since before the pandemic began in late February. The VIX Index remained choppy at the beginning of July but moved below 30 mid-month and settled into a range around 25, closing the month just below that mark. This is still roughly double the VIX levels we were enjoying in late 2019 and early 2020, but a clear improvement from the all-time closing high of 82.69 hit on March 16. Historically, the VIX spends about 28% of the time between 20 and 30 and less than 10% of the time above 30, so volatility is still elevated. We anticipate higher than normal volatility will remain the case as the reopening of the U.S. economy goes through expected ups and downs and the presidential election in November nears.

After seeing some modest signs of a broadening of the rally in the second quarter, the trends reverted to a familiar theme: the largest, growth-focused companies were outperforming. We at Clark Capital continue to use our disciplined approach of seeking out high-quality businesses at what we believe are good prices. The value/growth disparity has become more and more stretched and any reversion to the mean should benefit value-focused names. As always, we will continue to make purposeful investments in both stocks and bonds as we move forward in what we believe will be a period of wider outcomes of investment results.

Ultimately, July turned out to be a solid month across most equity categories. The numbers for July were as follows: the S&P 500 gained 5.64%, the Dow Jones Industrial Average improved by 2.51%, the Russell 3000 advanced 5.68%, the NASDAQ Composite rallied 6.85% and the Russell 2000 Index, a measure of small-cap companies, gained 2.77%. The year-to-date results were still mixed for these indices and continued to show the significant dispersion across U.S. equities. Year-to-date returns through July, in the same order, were as follows: 2.38%, -6.14%, 2.01%, 20.40%, and -10.57%, respectively. The Equal-Weighted S&P 500 is down -6.45% year to date, which shows how much of the S&P 500 return was driven by the largest companies.

### Highlights

The NASDAQ Composite continued to stand out among U.S. equity indices with strong gains in July, YTD up over 20% and new all-time highs achieved.

Meanwhile, the S&P 500 rose enough in July to push it into positive YTD territory, but the Dow lagged and is in the red through seven months of 2020.

Volatility, as measured by the VIX Index, dropped to its lowest closing level in late July since the pandemic began. By month's end, the VIX closed at 24.46.

The 10-year U.S. Treasury yield flirted with its all-time closing low hit in March at 0.54% as it ended July just one basis point higher at 0.55%.

We had anticipated a bumpy road to recovery, and we experienced that in July as several Sun Belt states struggled with a resurgence in COVID-19 cases. We continue to expect a choppy road ahead, but equity markets looked beyond the current challenges and forward toward ongoing improvements in the U.S.

Public policy will likely take center stage in early July as Congress was unable to pass a new stimulus package by month's end. For millions of Americans, this means an end to the $600 per week supplemental unemployment check and a potential "fiscal cliff" if nothing replaces that spending.

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As can be seen above, market cap has been an important differentiator of stock market results this year, but style has mattered even more. For some perspective on the divergence between value and growth stocks, consider the Russell 1000 Index is up 2.88% year to date after gaining 5.86% in July. However, the Russell 1000 Growth Index has advanced 18.26% year to date (up 7.69% in July) compared to the Russell 1000 Value index, which has declined -12.95% year to date (up 3.95% in July), a more than 3100 bps difference between growth and value over a seven-month period. In our opinion, this is extreme and an unsustainable spread between growth and value, which at some point will return closer to longer-term norms.

International equities showed broad gains in July, but emerging markets showed some of the best results of any equity market category for the month and have recovered much of their year-to-date declines. The U.S. dollar reversed its pattern of recent strength as it weakened over the course of July. The U.S. Dollar Index ended June just above 97, but it dropped to just above 93 by the end of July, a two-year low. This dollar weakness provided a tailwind to international stocks. The MSCI Emerging Markets Index gained 8.94% in July and the MSCI ACWI ex USA Index, a broad measure of international equities, advanced 4.46% with year-to-date returns of -1.72% and -7.03%, respectively.

## Fixed Income

Bond yields drifted lower throughout the month across the yield curve. For example, the 1, 5, 7 and 30-year U.S. Treasury yields closed June at 0.16%, 0.29%, 0.49% and 1.41%, respectively. By the end of July, those yields were at 0.11%, 0.21%, 0.39% and 1.20%, respectively. The benchmark 10-year U.S. Treasury yield ended the month at 0.55%, down from the prior month's close at 0.66% and just 1 basis point shy of its all-time closing low of 0.54% recorded on March 9. The ongoing and massive support from the Federal Reserve is keeping a lid on interest rates and we expect a "lower for longer" interest rate environment to persist for the foreseeable future. After a clear flight to quality into U.S. Treasuries in the first quarter, corporate bonds and municipals outperformed in the second quarter, and most categories of fixed income enjoyed gains in July with credit holding the clear advantage.

Fixed income returns were as follows for July: the Bloomberg Barclays U.S. Aggregate Bond Index gained 1.49%, the Bloomberg Barclays U.S. Credit Index advanced 3.08%, the Bloomberg Barclays U.S. Corporate High Yield Index rallied 4.69% and the Bloomberg Barclays Municipal Index rose 1.68%. Treasuries still show the best results year to date driven by powerful first quarter returns, but of note, high yield bonds have moved back into positive territory year to date, up 0.71%, having recovered from a sharp first quarter decline.

## Economic Data and Outlook

The National Bureau of Economic Research declared the recession started in March, and second quarter GDP data, released in late July, illustrated how sharp of an economic contraction we endured. U.S. gross domestic product dropped by -32.9% on an annualized basis in the second quarter, the worst economic decline in history, following the -5.0% annualized decline in the first quarter. We expected the second quarter would bear the brunt of this pandemic-caused recession and this level of decline had been expected by the market. For the record, the Q2 reading was actually slightly better than expectations, which called for a drop of -34.5%. While not trying to minimize the tremendous decline in economic activity due to the shutdown, it is important to note that GDP readings are always rearview looking. The stock market is forward looking and focuses more on earnings. Just over 60% of the S&P 500 companies have reported Q2 earnings. So far, a record high 82% of those companies that have reported have exceeded analysts' expectations and in aggregate earnings are expected to be +16% in Q2.

The market will also continue to be focused on the reopening process and how that is progressing. The reopening continued in July, but with some clear bumps along the way as several Sun Belt states struggled with a resurgence in COVID-19 cases. Many states slowed their reopening and that has been reflected in some recent economic data. For example, initial jobless claims rose over the last two weeks of July after reporting 15 straight weeks of improvement. This reflected states that needed to close certain businesses again and those workers, likely recently rehired, needing to file for unemployment benefits once again. To be clear, we have expected a bumpy reopening process and we experienced just that in July. We believe this choppy recovery will continue for some time.

Other economic data points reported in July, that largely covered June, showed some of the improvements taking place after the sharp declines in activity. The widely followed ISM Manufacturing Index rose to 52.6 in June, ahead of the expected reading of 49.8 and importantly back into expansion territory above 50. The ISM Non-Manufacturing or Services Index, which covers the much larger service industries in the U.S. economy, showed even more progress, jumping to 57.1 compared to expectations of 50.2 and the prior month's mark of 45.4. Clearly, manufacturing and service industries have improved from the shutdown period.

Job market data surprised to the upside again in June with 4.8 million people added to payrolls during the month. This surpassed expectations of just over 3.2 million and the prior month's gains of about 2.7 million. Please keep in mind that we are still recovering from the drop in payrolls of -20.7 mil-

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lion in April. The unemployment rate fell to 11.1%, which was an improvement on May's reading of 13.3% and the anticipated rate of 12.5%.

Retail sales continued to rebound as well in June with a monthly gain of 6.7% (ex autos and gas), surpassing expectations of a 5% advance. Housing starts, building permits and existing home sales were all improved in June from May, but were all below expectations as well. New home sales at a 776,000 annualized pace easily surpassed expectations of 700,000 and were well ahead of May's rate of 682,000.

Consumer confidence, as measured by the preliminary reading of the University of Michigan consumer sentiment survey for July, slowed to 73.2 and was below expectations of 79.0. This reading likely reflected the resurgence in COVID-19 cases that began in late June and early July. The Conference Board's Leading Index gained 2.0% in June, slightly below the expected 2.1% advance, but May was revised higher to a 3.2% increase from the previous 2.8% mark.

We anticipate a strong bounce back in economic activity in the second half of 2020. Once we move into 2021, we anticipate economic growth will go back to the slower trend type of growth we experienced for most of the post-credit crisis period. We believe it will take until late 2022 or early 2023 to return to the peak levels of economic output we were at pre-pandemic in February.

The Federal Reserve continues to signal an "all-in" attitude and the FOMC meeting that concluded in late July did nothing but confirm this stance. Unfortunately, the focus has now shifted to fiscal stimulus since Congress has yet to agree upon a CARES Act 4.0. The extended Federal benefit of $600 per week for the unemployed expired at the end of the month and a severe drop off in spending could ensue without some sort of replacement. Government officials are trying to determine the right amount of stimulus to help support the unemployed, but at the same time incentivize them to return to work. Clearly, the difference between the two parties on this matter is wide.

As we go through what we know are difficult and challenging times, we remain resolute in our belief that the U.S. economy and corporate America will make it through this pandemic. This stance has not changed since the beginning of the crisis. To be clear, we do expect elevated volatility in the weeks and months ahead and we think it is important that investors brace for this likely bumpy path. However, at this point, we believe the economy and financial markets are heading in the right direction. We believe it is imperative for investors to stay focused on their long-term goals and not let short-term swings derail them from their longer-term objectives.

## Investment Implications

*Clark Capital's Top-Down, Quantitative Strategies*

The markets have been very resilient in the face of higher COVID-19 case counts and risk assets have continued trending higher. The Federal Reserve continues to provide liquidity through asset purchases and another fiscal package appears to be on the horizon. Interest rates have been anchored, with the 10-Year Treasury Note hovering near 60 bps since the end of March.

Credit has remained firm as the economy continues to recover and credit spreads look to trend tighter. The strength in credit turned our tactical models positive near the end of the month, and they now favor a risk-on bias. The Navigator® Fixed Income Total Return and Global Macro portfolios shifted away from U.S. Treasuries and into high yield and global equities, respectively. Growth continues to dominate, and the Navigator® Style Opportunity portfolio is concentrated in large-cap and growth, in tune with the market's relative strength trends. In Alternative Opportunity, precious metals and commodity related equities have been strong performers with the U.S. dollar weakness. Silver, Gold, and commodity related stocks are benefitting from surging money supply growth, the economic recovery, political uncertainty in the U.S., and negative real interest rates acting as a tail wind.

*Clark Capital's Bottom-Up, Fundamental Strategies*

The U.S. economy continues to gradually respond to massive government stimulus resembling a stairstep pattern versus the V or U shape recovery. While the number of COVID-19 cases increased in July, equity averages once again posted solid gains for the fourth month in a row. So far for Q2, S&P 500 revenue and EPS growth are on track to be down -10% and -35% year over year which is better than original estimates, and analysts are cautiously increasing estimates for the balance of the year. The Navigator® High Dividend Equity portfolio invests in companies paying a dividend and normally carries an overweight of dividend growers in the Technology sector. The Navigator® All Cap portfolio remains fully invested with approximately 64.4% in large-cap stocks and the remainder in mid-/small-cap stocks and cash. Technology and its large-cap components continue to dominate both the performance and weight of the portfolio.

The trade weighted U.S. dollar index has declined by almost 10% from its pandemic peak and looks set continue lower over the intermediate-term due to political uncertainty, surging money supply growth, and negative real interest rates. The weak dollar will likely be a tailwind for corporate earnings and international market performance. The Navigator® ADR/ International Equity Strategy has begun to increase its emerging market weight to 17.8% from May's

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11.5% low as prospects for global economic growth begin to stabilize. Similarly, our weight in Japan is down to 15% from 20% at the height of the pandemic.

The fixed income portfolios posted solid gains in July, with the Fed intent on keeping rates pinned lower for longer. The 2-year Treasury yield closed the month at 0.10%, 5-year Treasury note at 0.20%, and the 10 year at 0.53%. As a result, we are in the process of extending duration towards the 5-year range in the portfolios

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## Economic Data

| Event | Period | Estimate | Actual | Prior | Revised |
|---|---|---|---|---|---|
| ISM Manufacturing | June | 49.8 | 52.6 | 43.1 | — |
| ISM Services Index | June | 50.2 | 57.1 | 45.4 | — |
| Change in Nonfarm Payrolls | June | 3.230m | 4.800m | 2.509m | 2.699m |
| Unemployment Rate | June | 12.5% | 11.1% | 13.3% | — |
| Average Hourly Earnings YoY | June | 5.3% | 5.0% | 6.7% | 6.6% |
| JOLTS Job Openings | May | 4500k | 5397k | 5046k | 4996k |
| PPI Final Demand MoM | June | 0.4% | -0.2% | 0.4% | — |
| PPI Final Demand YoY | June | -0.2% | -0.8% | -0.8% | — |
| PPI Ex Food and Energy MoM | June | 0.1% | -0.3% | -0.1% | — |
| PPI Ex Food and Energy YoY | June | 0.4% | 0.1% | 0.3% | — |
| CPI MoM | June | 0.5% | 0.6% | -0.1% | — |
| CPI YoY | June | 0.6% | 0.6% | 0.1% | — |
| CPI Ex Food and Energy MoM | June | 0.1% | 0.2% | -0.1% | — |
| CPI Ex Food and Energy YoY | June | 1.1% | 1.2% | 1.2% | — |
| Retail Sales Ex Auto and Gas | June | 5.0% | 6.7% | 12.4% | 12.1% |
| Industrial Production MoM | June | 4.3% | 5.4% | 1.4% | — |

| Event | Period | Estimate | Actual | Prior | Revised |
|---|---|---|---|---|---|
| Building Permits | June | 1293k | 1241k | 1220k | 1216k |
| Housing Starts | June | 1190k | 1186k | 974k | 1011k |
| New Home Sales | June | 700k | 776k | 676k | 682k |
| Existing Home Sales | May | 4.09m | 3.91m | 4.33m | — |
| Leading Index | June | 2.1% | 2.0% | 2.8% | 3.2% |
| Durable Goods Orders | June P | 6.9% | 7.3% | 15.7% | 15.1% |
| GDP Annualized QoQ | 2Q A | 6.9% | 7.3% | 15.7% | 15.1% |
| U. of Mich. Sentiment | July P | 79.0 | 73.2 | 78.1 | — |
| Personal Income | June | -0.6% | -1.1% | -4.2% | -4.4% |
| Personal Spending | June | 5.2% | 5.6% | 8.2% | 8.5% |
| S&P CoreLogic CS 20-City YoY NSA | May | 4.0% | 3.69% | 3.98% | 3.91% |

Source: Bloomberg

P=Preliminary

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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 market countries.

The S&P 500® Equal Weight Index (EWI) is the equal-weight version of the widely-used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance.

The Bloomberg Barclays U.S. Municipal Index covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prerefunded bonds.

The 30 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 30 years. The 30 year treasury yield is included on the longer end of the yield curve and is important when looking at the overall US economy

The 1 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 1 year.

The 7Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 7 years.

The Dow Jones Industrial Average indicates the value of 30 large, publicly owned companies based in the United States.

The NASDAQ Composite is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market.

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 Russell 1000 Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values.

Russell 1000 Index measures the performance of the 1,000 largest companies in the Russell 3000 Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.

The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 Index companies with lower price-to-book ratios and lower forecasted growth values.

The Russell 2000 Index is a small-cap stock market index that represents the bottom 2,000 stocks in the Russell 3000.

The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

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 MSCI Emerging Markets Index is used to measure large and mid-cap equity market performance in the global emerging markets.

The MSCI ACWI ex USA Index captures large and mid-cap representation across 22 of 23 developed market countries and 24 emerging market countries, covering approximately 85% of the global equity opportunity set outside of the U.S.

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.

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.

The Bloomberg Barclays U.S. Credit Index measures the investment grade, U.S. dollar denominated, fixed-rate taxable corporate and government related bond markets.

The ISM Non-Manufacturing Index is an index based on surveys of more than 400 non-manufacturing firms' purchasing and supply executives, within 60 sectors across the nation, by the Institute of Supply Management (ISM). The ISM Non-Manufacturing Index tracks economic data, like the ISM Non-Manufacturing Business Activity Index. A composite diffusion index is created based on the data from these surveys, that monitors economic conditions of the nation.

ISM Manufacturing Index measures manufacturing activity based on a monthly survey, conducted by Institute for Supply Management (ISM), of purchasing managers at more than 300 manufacturing firms.

Personal consumption expenditures price index is the component statistic for consumption in gross domestic product collected by the United States Bureau of Economic Analysis.

The 3 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 3 year.

The 5 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 5 year.

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 Conference Board's Leading Indexes are the key elements in an analytic system designed to signal peaks and troughs in the business cycle. The leading, coincident, and lagging economic indexes are essentially composite averages of several individual leading, coincident, or lagging indicators. They are constructed to summarize and reveal common turning point patterns in economic data in a clearer and more convincing manner than any individual component – primarily because they smooth out some of the volatility of individual components.

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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