Clark Capital Management Group

Benchmark Review
& Monthly Recap

December Bookends a Tough Year for Stocks and Bonds

Highlights

After gains in October and November, December saw stocks decline again. The S&P 500 and Dow rose for the quarter (the first quarterly gains of 2022), but the Nasdaq recorded its fourth straight quarterly decline to close out the year.

Bonds, which enjoyed gains in November, came under pressure as well in December as rates rose.

Overall, it was the worst year for stocks since 2008 and the Bloomberg U.S. Aggregate Bond Index posted its worst annual decline on record (and by a long shot) since its inception in 1976. As expected, the FOMC raised its policy rate by another 75-basis points in November. The debate in the market is whether the Fed raises rates by a less aggressive amount at its final FOMC meeting in mid-December and into 2023.

The 10-year U.S. Treasury yield ended November at 3.68%, but rates rose to close out 2022 at 3.88%. As a reminder, the 10-year yield ended 2021 at 1.52%.

The FOMC raised rates by "only" 50 basis points in December. This followed four consecutive meetings of rate increases of 75 basis points. The first FOMC meeting of 2023 will conclude on February 1 with another rate increase expected.

The economy continues to grow at a slow pace under the pressure of higher interest rates. Although inflation has improved in recent months, it remains elevated and continues to be the central focus of the Fed moving into 2023.

Equity Markets

Equity index returns for December were as follows: The S&P 500 fell -5.76%, the Dow Jones Industrial Average slid by -4.09%, the Russell 3000 declined -5.86%, the NASDAQ Composite tumbled by -8.67%, and the Russell 2000 Index, a measure of small-cap stocks, slumped -6.49%.

Like the general trend in 2022, large, value-oriented companies fared better during the month compared to growth and smaller-cap stocks. For the fourth quarter, the index results in the same order were as follows: 7.56%, 16.01%, 7.18%, -0.79% and 6.23%, respectively.

Despite gains in the fourth quarter (with the exception of the NASDAQ), for all of 2022, the declines for these equity indices in the same order were as follows: -18.11%, -6.86%, -19.21%, -32.54%, and -20.44%, respectively.

The VIX Index went below 20 in early December, but it rose from that point to end the year at 21.67 as stocks slumped. Although higher for the month, the VIX Index was lower for the quarter after being above 30 for much of the first half of October.

Equity weakness was widespread in December, but following the trend of 2022, large-cap growth stocks came under pressure during the month. The large-cap focused Russell 1000 Growth Index declined -7.66% for the month and it was off -29.14% for 2022. In contrast, the Russell 1000 Value Index fell by -4.03% in December and was down a more modest -7.54% for the year.

In relative performance terms, the value index was more than 2,100 basis points better than its growth counterpart in 2022. Growth stocks are sensitive to interest rate moves and higher interest rates in 2022 led to the significant underperformance of growth stocks. The same trend held true for small-caps for all of 2022, but not to the same degree as large-caps.

The Russell 2000 Growth Index fell -6.42% in December, just modestly better relative results than the Russell 2000 Value Index, which declined -6.56%. However, year to date, those indices have declined -26.36% and -14.48%, respectively. At Clark Capital, we continue to use our disciplined approach of seeking out what we believe to be high-quality companies with improving business conditions at what we believe are good prices and those companies can be found in both the value and growth universe.

After rebounding sharply in November, international stocks continued to have better relative results than U.S. stocks in December, although they were modestly lower. As we often discussed in 2022, the US Dollar Index

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(DXY) broadly strengthened during most of the year, but it was relatively flat in December after declining sharply in November.

The removal of that significant headwind of dollar strength in November contributed to the rally in international stocks and a flat December for the dollar helped international stocks in relative terms. The MSCI ACWI ex USA Index, a broad measure of international equities, fell by a modest -0.75% in December, while the MSCI Emerging Markets Index slipped by -1.41%. For the quarter, those two indices were up 14.28% and 9.70%, respectively, but for all of 2022, these indices were down -16.00% and -20.09%, respectively.

Fixed Income

Fixed income returns were as follows for December: the Bloomberg U.S. Aggregate Bond Index fell -0.45%, the Bloomberg U.S. Credit Index declined -0.43%, the Bloomberg U.S. Corporate High Yield Index slipped -0.62% and the Bloomberg Municipal Index inched higher by 0.29%. As would be expected, the 30-year U.S. Treasury Index had some of the worst results, falling -2.49% for the month as rates rose, while the general U.S. Treasury Index slid -0.52%.

For the quarter, the returns for these indices in the same order were as follows: 1.87%, 3.44%. 4.17%, 4.10%, -2.63% and 0.72%. For the year, the returns for these indices in the same order were as follows: -13.01%. -15.26%, -11.19%, -8.53%, -33.29% and -12.46%, respectively.

It was a dramatic year of interest rate increases, which led to one of the worst years for bond returns on record. The 10-year U.S. Treasury yield ended 2021 at 1.52% and it rose dramatically to end 2022 at 3.88%. It closed on 10/24 at a more than 10-year high of 4.25% - a level not seen since the credit crisis.

The overall increase in interest rates this year put significant pressure on the bond market and returns suffered. While short-term returns are negatively impacted by the Fed raising rates, we believe future potential returns for bonds have become more attractive with the higher yields available, making bonds a more attractive asset class.

As we have previously stated, we believe the move higher in rates in 2022 has run its course at the longer end of the yield curve and we expect the 10-year yield to move lower from this point. Since that high mark on the 10-year yield in late October, longer rates have come down and created a better backdrop for bond returns, which resulted in gains for the quarter. However, it's still worth acknowledging that negative returns overall in 2022 were challenging to say the least.

Bonds struggled in 2022 as there was a repricing of interest rates across the yield curve and across bond sectors under this Fed rate tightening cycle. We maintain our long-standing position favoring credit versus pure rate exposure in this interest rate environment. We also believe that the role bonds play in a portfolio, to provide stable cash flows and to help offset the volatility of stocks in the long run, has not changed.

Economic Data and Outlook

Job market strength continued in November. Non-farm payrolls increased by 263,000 in November when expectations called for only 200,000. The unemployment rate remained at 3.7% as expected. As payrolls continued to climb, so did wages as year-over-year earnings rose by 5.1% when expectations were only for an increase of 4.6%. Fed action is expected to raise unemployment, but Fed rate increases so far have not resulted in significant weakness in the job market and is likely a point of frustration for the Fed as strong wage increases can be inflationary.

Typically, the unemployment rate starts to rise heading into a recession, but there continues to be millions more job openings than job seekers – a key driver of ongoing wage increases. However, based on the JOLTS reading of job openings, the number of openings has been moving lower. The openings in October stood at just over 10.3 million and this compares with the September level of just under 10.7 million. This might reflect businesses starting to slow hiring activity. Ultimately, the job market is important to track with about 70% of U.S. economic activity driven by consumer spending, which remained resilient during most of 2022.

Housing continues to be impacted by higher mortgage rates and the data reflected this general theme. Building permits, considered a leading indicator for housing, declined in November by more than -11% compared to October and missed expectations by almost 140,000 (on an annualized basis). However, new home sales surged in November to 640,000 (on an annualized basis) when expectations were at 600,000 and the prior month was at 605,000. Housing starts beat expectations, but existing home sales missed estimates and both readings were lower than the prior month.

The housing market has been a source of strength in the economy and has historically been a good leading indicator as well. The rise in mortgage rates in 2022 and high home prices have taken some steam out of the housing market. The housing market is sensitive to interest rate moves, so on a month-to-month basis, data might reflect what is happening with rates in the near term, but overall, housing appears to be slowing as the broader economy slows down.

Recently, we have seen some monthly drops in home prices for the first time in years, but on an annual basis, values are still higher. Based on the year-over-year reading of the S&P CoreLogic CS 20-City Index, home prices rose by 8.64% in October, but this continues the trend of slower price gains as the September increase had been 10.41% compared to the prior year.

The steady move lower in the ISM Manufacturing Index continued in November as it dropped to 49.0 – its first sub-50 reading since May 2020. The new orders component dropped further to 47.2 and prices paid dropped as well to 43.0, but that could bode well for inflation data continuing to moderate. The ISM Non-Manufacturing Index, which covers the much larger service industries in the U.S. economy, showed strength as it rose to 56.5 in November compared to expectations of 53.5 and the prior reading of 54.4.

Recall that ISM readings above 50 indicate expansion and below 50 signal contraction, so manufacturing has slipped into contractionary territory while services are still exhibiting growth.

Retail sales (ex. auto and gas) fell unexpectedly in November by -0.2% when a flat reading was expected. The preliminary University of Michigan Sentiment reading for December was better than expected and improved from November, which is not too surprising with stock market strength in October and November and ongoing moderation in inflation.

The Conference Board's Leading Index continued to decline and fell by -1.0% in November, which was double the expected decline of -0.5%. The third reading of Q3 2022 GDP was revised higher to a 3.2% annualized growth rate compared to expectations of 2.9%, which was the second estimate as well. Economic growth weakened in 2022, but we do not believe we are currently in a recession and the third quarter GDP number supports that opinion.

However, we acknowledge the risk of a mild recession, most likely in the mid to latter part of next year, has increased, especially as the 3-month T-Bill and the 10-year U.S. Treasury inverted in late October. Historically, this has been an indicator that the economy might be headed toward a recession, and this inversion is now coupled with an ISM Manufacturing reading below 50.

We believe that we are in the later innings of this Fed rate hike cycle as the Fed at long last slowed rate increases to "only" 50 basis points at its December FOMC meeting. Despite this step-down in rate increases, Chairman Powell remains focused on inflation and has kept his hawkish tone. Furthermore, the Fed continues to tell the market to expect rates to stay higher for longer, which continues to put pressure on the market.

Inflation remains elevated, but progress on the inflation front has also become more of a trend in recent months. The headline Consumer Price Index dropped from 7.7% in October to 7.1% in November, well off its high of 9.1%. The core CPI reading dropped from 6.3% to 6.0%. The Producer Price Index, while higher than expected in November at 7.4%, still improved from the prior reading of 8.1%. The Fed appears to have enough improvement occurring on the inflation front to at least throttle down the pace of rate hikes as it did in December. The course of Fed action in 2023 will still be of critical importance to the market.

The shift in the Fed's stance to more restrictive monetary policy in 2022 as it battles inflation has impacted markets and the economy during the year. The Fed is focused on bringing inflation under control, but its primary tool in achieving that goal is raising interest rates, which is a headwind to general economic activity. Markets reset valuations in 2022 based on higher interest rates and lower corporate earnings expectations in this rate-tightening cycle.

Growth has slowed and the chances of the Fed pushing us into a mild recession in 2023 have risen. However, the job market has remained resilient, which is a critical component of our overall economy. As a result, we believe that any economic slowdown would be modest.

Importantly, stocks and bonds have historically hit their lows early in the rate hike cycle, well before the Fed has made its final rate hikes. Also, the headwind of a mid-term election year has passed, and we move into a more favorable part of the 4-year presidential cycle for the first half of 2023. As always, we believe it is imperative for investors to stay focused on their long-term goals and not let short-term swings in the market derail them from their longer-term objectives.

Investment Implications

Clark Capital's Top-Down, Quantitative Strategies

December did not prove to provide the normal seasonal rally into year-end, known as the Santa Claus Rally. Markets struggled under the weight of an additional Fed rate hike and hawkish speech coming from Fed officials. In addition, tax-loss selling likely contributed to the losses across both the bond and equity markets into year end.

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A silver lining to the recent weakness is that credit proved to be resilient in the face of selling pressure. Our tactical strategies, including Fixed Income Total Return and Global Tactical remain risk-on, invested in high yield and global equity, respectively. The credit-based risk management models that drive those allocations remained favorably positioned on risk as the year ended.

Clark Capital's Bottom-Up, Fundamental Strategies

Across our bottom-up equity strategies, we continue to balance portfolio holdings between the dominant large-cap growth companies and those anti-fragile large, small, and mid-cap companies that we believe will continue to see strong business momentum despite rising inflation and tight labor market conditions.

We believe our focus on higher quality and more antifragile companies has helped the portfolios mitigate exposure to the extreme declines associated with expensive or low-quality company indices.

In the Tax-Free Fixed Income portfolio, we have been aggressively managing duration and extension risk; taking advantage of illiquidity to purchase what we believe are attractive names at wider than usual spreads and percentages of Treasuries. In the Taxable Fixed Income portfolio, we continued to focus on improving the overall credit quality of the portfolio while increasing the overall coupon and current yield. The portfolio also continued to add newer higher-quality names in the 10-year part of the curve while selling those same names that were shorter, lower yielding and had lower coupons.

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Economic Data

Event	Period	Estimate	Actual	Prior	Revised
ISM Manufacturing	Nov	49.7	49.0	50.2	—
ISM Services Index	Nov	53.5	56.5	54.4	—
Change in Nonfarm Payrolls	Nov	200k	263k	261k	284k
Unemployment Rate	Nov	3.7%	3.7%	3.7%	—
Average Hourly Earnings YoY	Nov	4.6%	5.1%	4.7%	4.9%
JOLTS Job Openings	Oct	10250k	10334k	10717k	10687k
PPI Final Demand MoM	Nov	0.2%	0.3%	0.2%	0.3%
PPI Final Demand YoY	Nov	7.2%	7.4%	8.0%	8.1%
PPI Ex Food and Energy MoM	Nov	0.2%	0.4%	0.0%	0.1%
PPI Ex Food and Energy YoY	Nov	5.9%	6.2%	6.7%	6.8%
CPI MoM	Nov	0.3%	0.1%	0.4%	—
CPI YoY	Nov	7.3%	7.1%	7.7%	—
CPI Ex Food and Energy MoM	Nov	0.3%	0.2%	0.3%	—
CPI Ex Food and Energy YoY	Nov	6.1%	6.0%	6.3%	—

Event	Period	Estimate	Actual	Prior	Revised
Retail Sales Ex Auto and Gas	Nov	0.0%	-0.2%	0.9%	0.8%
Industrial Production MoM	Nov	0.0%	-0.2%	-0.1%	—
Building Permits	Nov	1480k	1342k	1526k	1512k
Housing Starts	Nov	1400k	1427k	1425k	1434k
New Home Sales	Nov	600k	640k	632k	605k
Existing Home Sales	Nov	4.20m	4.09m	4.43m	—
Leading Index	Nov	-0.5%	-1.0%	-0.8%	-0.9%
Durable Goods Orders	Nov P	-1.0%	-2.1%	1.1%	0.7%
GDP Annualized QoQ	3Q T	2.9%	3.2%	2.9%	—
U. of Mich. Sentiment	Dec P	57.0	59.1	56.8	—
Personal Income	Nov	0.3%	0.4%	0.7%	—
Personal Spending	Nov	0.2%	0.1%	0.8%	0.9%
S&P CoreLogic CS 20-City YoY NSA	Oct	8.00%	8.64%	10.43%	10.41%

Source: Bloomberg: P=Preliminary, T=Third Reading

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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).

Clark Capital utilizes a proprietary investment model to assist with the construction of the strategy and to assist 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.

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 value of investments, and the income from them, can go down as well as up and you may get back less than the amount invested.

Equity securities are subject to price fluctuation and possible loss of principal. Stock markets tend to move in cycles, with periods of rising prices and periods of falling prices. Certain investment strategies tend to increase the total risk of an investment (relative to the broader market). Strategies that concentrate their investments in limited sectors are more vulnerable to adverse market, economic, regulatory, political, or other developments affecting those sectors.

A Treasury Bill (T-Bill) is a short-term debt obligation backed by the U.S. Treasury Department with a maturity of one year or less.

The Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services.

References to market or composite indices, benchmarks or other measures of relative market performance over a specified period of time (each, an "index") are provided for your information only. Reference to an index does not imply that the portfolio will achieve returns, volatility or other results similar to that index. The composition of the index may not reflect the manner in which a portfolio is constructed in relation to expected or achieved returns, portfolio guidelines, restrictions, sectors, correlations, concentrations, volatility or tracking error targets, all of which are subject to change. Investors cannot invest directly in an index.

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 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.

DXY is the symbol for the US dollar index, which tracks the price of the US dollar against six foreign currencies, aiming to give an indication of the value of USD in global markets. The index rises when USD gains strength against the other currencies and falls when the dollar weakens.

The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 80% of U.S. equities.

The University of Michigan Consumer Sentiment Index rates the relative level of current and future economic conditions. There are two versions of this data released two weeks apart, preliminary and revised. The preliminary data tends to have a greater impact. The reading is compiled from a survey of around 500 consumers.

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.

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 2000 Value Index measures the performance of the small-cap value segment of the U.S. equity universe. It includes those Russell 2000 companies with lower price-to-book ratios and lower expected and historical growth values.

The Russell 2000 Growth Index measures the performance of the small-cap growth segment of the U.S. equity universe.

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 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 Bloomberg Aggregate Bond Index or "the Agg" is a broad-based fixed-income index used by bond traders and the managers of mutual funds and exchange-traded funds (ETFs) as a benchmark to measure their relative performance.

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.

The MSCI Emerging Markets Index captures large and mid cap representation across 27 Emerging Markets (EM) countries.

The MSCI ACWI ex USA Index captures large and mid cap representation across 22 of 23 Developed Markets (DM) countries (excluding the US) and 27 Emerging Markets (EM) countries*. With 2,359 constituents, the index covers approximately 85% of the global equity opportunity set outside the US.

The S&P CoreLogic Case-Shiller 20-City Composite Home Price NSA Index seeks to measures the value of residential real estate in 20 major U.S. metropolitan areas

The U.S. Treasury index is based on the recent auctions of U.S. Treasury bills. Occasionally it is based on the U.S. Treasury's daily yield curve.

The New Orders Index shows if businesses in the sector are growing with new customers or orders. An index value above 50 percent indicates a positive development in the service sector new orders, whereas a value below 50 percent indicates a negative situation.

The Consumer Price Index (CPI) measures the change in prices paid by consumers for goods and services. The CPI reflects spending patterns for each of two population groups: all urban consumers and urban wage earners and clerical workers.

The "core" PCE price index is defined as personal consumption expenditures (PCE) prices excluding food and energy prices. The core PCE price index measures the prices paid by consumers for goods and services without the volatility caused by movements in food and energy prices to reveal underlying inflation trends.

The VIX Index is a calculation designed to produce a measure of constant, 30-day expected volatility of the U.S. stock market, derived from real-time, mid-quote prices of S&P 500® Index (SPX℠) call and put options. On a global basis, it is one of the most recognized measures of volatility -- widely reported by financial media and closely followed by a variety of market participants as a daily market indicator.

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.

Gross domestic product (GDP) is the standard measure of the value added created through the production of goods and services in a country during a certain period.

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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