

High Yield Market Update

Coming off the worst quarterly performance since Q4 2008, High Yield had its best quarterly performance since Q3 2009. Moderating restrictions on business activity, combined with aggressive monetary policy to keep markets functioning and historic fiscal stimulus to alleviate both consumer and business liquidity pressures, were the primary drivers of strong positive returns for risk assets. Oil prices partially recovered in the second quarter as WTI Crude closed the period up \$18.79/bbl (or 91.75%) to \$39.27/bbl, leading to Energy being the top-performing high yield sector for Q2. For the quarter the US Dollar Index was down 1.67% and Treasuries ended the period with the 2-year down 9 basis points (bps) to 0.16% and the 10-year lower by 1 bp to 0.66% as the yield curve slightly steepened.

Technical were mixed in the second quarter of 2020 as big inflows were met with record new issuance. High yield funds and ETFs had inflows of \$48.6bn while loan funds saw continued outflows of \$40.2bn, as tracked by Lipper and reported by Barclays. Q2 bond new issuance was a record high, pricing \$131.9bn in the quarter, offset by \$55.7bn of bond redemptions, leaving net supply at \$76.2bn for the period, per Barclays. The percentage of the market trading at distressed

levels (below 70% of par) ended the quarter at 6.7%; the comparable figure for the loan market (below 80% of par) was 9.8%, per JP Morgan. The par-weighted twelve-month high yield bond default rate increased to 6.6% by quarter-end, per BofA Merrill Lynch. Excluding commodities, the default rate was 4.2%.

The ICE BofA US High Yield Index returned 9.61% in Q2, ending the period with an average price of 94.38, an 8.35-point increase from the prior quarter. Credit spreads tightened by 211 bps to 648 bps and the yield-to-worst (YTW) was lower by 2.15% to 6.87%. High yield underperformed small cap equities, represented by the Russell 2000's 25.00% return, as well as large cap equities, as represented by the S&P 500's 19.95% return, but outperformed investment grade corporates, as represented by the ICE BofA US Corporate Index's 9.27% quarterly return. In high yield, the Double-B, Single-B and Triple-C sub-indices returned 9.85%, 9.11% and 9.77%, respectively. Returns were positive across all sectors for the quarter: the top performer was Energy, which saw a 33.04% return, while Transportation was the bottom-performing sector with a 3.11% return.

Portfolio Performance

Portfolios managed according to our Unconstrained **Broad High Yield Market Strategy** (BHYM) posted strong absolute returns during the second quarter but lagged the benchmark. Generally, the strategy has weathered volatility with significantly less negative performance on down days and lagged on up days. Q2 relative performance was most negatively impacted by sector allocation decisions which were not fully offset by strong positive security selection. The largest contributor to negative relative returns came from the portfolio's low exposure to the Energy sector, offset only partially by substantially stronger security returns in the sector. Our bias to have low exposure to the Energy sector was a significant contributor to outperformance in Q1. While we added modestly to Energy holdings opportunistically early in the quarter, we remain skeptical of the sector's longer-term ability to support leveraged capital structures due to both cyclical and secular negative trends. Away from sector positioning, portfolios benefited from strong security selection across packaging-related holdings and a number of other Capital Goods-related holdings, and limited exposure to the Bombardier capital structure which did not participate in the market's rally due to concern regarding the company's ability to close on recently announced asset sales. Performance of

several of the portfolios' high conviction Healthcare-related holdings also resulted in above-market performance for that sector. Specifically, Surgery Center and Ardent Health (AHP Health Partners) were significant contributors to overall returns.

Broad High Yield Market Strategy: Performance

	SKY Harbor BHYM Strategy Performance			
	Gross of Fees	ICE BofA US HY Index	Alpha ¹	Net of Fees
April 2020	3.36	3.80	-0.44	3.33
May 2020	3.75	4.57	-0.82	3.72
June 2020	1.37	0.97	0.40	1.35
Q2 2020	8.71	9.61	-0.90	8.63
Year to Date 2020	-4.44	-4.78	0.34	-4.58
Last 12 Months	-0.25	-1.10	0.85	-0.55
Three Years (annl)	3.11	2.94	0.17	2.81
SI Return (annl)	6.54	6.48	0.05	6.21

Performance includes reinvestment of dividends and other earnings. Gross performance does not reflect the deduction of management fees. Fees disclosed in SKY Harbor's Form ADV, Part 2A or applicable offering documents. Past performance is not indicative of future results.
SI=Since Inception. Broad High Yield Market Composite inception date: 9/30/11.

SKY Harbor's Unconstrained **Short Duration High Yield Strategy** (SDHY) portfolios posted strong absolute returns during the recovery in Q2, capturing around 50% of the return of the broader US high yield market (as measured by the ICE BofA US High Yield Index) on a gross-of-fee basis. By risk type, generally more speculative securities and longer duration (within the context of short duration) rallied more than shorter duration, more defensive securities during the quarter. By sector, Energy was the highest performer, but we have minimal exposure and do not expect this to change due to our longer-term concerns about the sustainability of the

sector. SDHY portfolios did benefit from exposure to the bounceback in the hard-hit Real Estate sector. On the negative side, Transportation, though a small weight, logged a negative return even as we reduced exposure to airlines. By rating, the lowest-rated part of the portfolios showed some of the strongest returns, as has been the case with the overall market. Our CCC rated holdings are biased towards the bonds of companies that we believe do not have near-term default or restructuring risk. Our underweight to the recovering Energy sector has negatively impacted our relative security selection within the BB and B rated parts of the portfolio.

Short Duration High Yield Strategy: Performance

	SKY Harbor SDHY Strategy Performance				Annualized Daily Volatility ²		
	Gross of Fees	High Yield Market ¹	Market Capture	Net of Fees	SKY SDHY Strategy	High Yield Market ¹	Relative Volatility
April 2020	2.04	3.80	54%	2.01	10.7	15.7	68%
May 2020	2.63	4.57	57%	2.60	4.2	6.9	60%
June 2020	0.73	0.97	75%	0.70	6.0	9.9	61%
Q2 2020	5.49	9.61	57%	5.40	7.3	11.2	65%
Year to Date 2020	-3.04	-4.78	64%	-3.19	10.1	15.3	66%
Last 12 Months	-0.52	-1.10	47%	-0.84	7.2	10.9	66%
Three Years (annl)	2.84	2.94	96%	2.50	4.3	6.7	64%
Since Inception (annl)	4.00	5.84	68%	3.63	3.0	4.9	61%

1. The Short Duration High Yield strategy is not a benchmarked strategy. The HY Market index shown (ICE BofA US HY Index) is used solely as a relative market indicator. Short Duration High Yield Composite Inception date: 10/31/11
Performance includes reinvestment of dividends and other earnings. Gross performance does not reflect the deduction of management fees. Fees disclosed in SKY Harbor's Form ADV, Part 2A or applicable offering documents. Past performance is not indicative of future results.

Outlook

We believe investors have been focused on the timing and pace of an economic recovery and have been willing to ignore potential risks around trade relations with China, large US deficits and the potential for a changing political landscape. Investor surveys now suggest that concerns regarding the US election are increasing. Market volatility around election outcome probabilities will increase and risks are likely to reprice themselves according to how well they are expected to fare with different election outcomes. Our positioning is evolving towards sectors where those risks are either over-discounted or present less of a headwind.

Our central scenario has not changed. We expect rising default risk in the Energy, Retail, Leisure and potentially Transportation sectors despite an eventual stabilization of coronavirus-related impact to demand in the second half of the year. Defaults away from these key sectors appear to be rapidly declining as markets are willing to bridge many stressed capital structures to the time

when end-market demand is sufficiently robust. Fiscal and monetary stimulus around the globe appears ready to resize and evolve on an as-needed basis and development of both a treatment protocol and a vaccine appears likely. Spread compression is likely to continue as a result. We are managing our portfolios to rebuild returns back into positive territory and believe the market has excess return opportunity associated with credit picking given the high level of dispersion in the market.

To support our risk-taking, we are focused on consumer and business behavior as restrictions are lifted around the globe. We believe current positioning suggests good potential market capture to the upside so long as Energy is not the driver of the upside but are mindful that low-dollar bonds are likely to gap higher in the absence of further selling pressure. Given the secular and cyclical demand destruction, and historically low oil prices, we do not see speculative Energy being a driver of sustained upside returns.

SKY HARBOR CAPITAL MANAGEMENT

Portfolio Characteristics

Representative Broad High Yield Market Portfolio

Characteristics	Portfolio ¹	HY Market	Distribution by Sector	Portfolio ¹	HY Market	SKY as % of HY Market
Avg Years to Maturity	5.9	6.2	Basic Industry	13.5%	10.2%	132%
Yield to Worst	7.36%	6.86%	Services	12.3%	5.4%	229%
Current Yield	7.01%	6.45%	Capital Goods	11.8%	6.0%	195%
Duration to Worst	3.9	4.0	Healthcare	8.7%	9.7%	90%
OAS	723	648	Media	8.5%	9.8%	87%
Avg Coupon	6.83%	6.08%	Technology & Electronics	7.9%	4.7%	169%
Number of Issuers	151	823	Consumer Goods	7.5%	5.4%	139%
Number of Issues	190	1935	Automotive	7.0%	5.4%	130%
Average ML Rating	B2	B1	Retail	6.4%	4.8%	134%
Average Price	97.4	94.4	Leisure	4.1%	5.2%	78%
			Transportation	3.1%	1.1%	275%
			Real Estate	3.0%	2.0%	155%
			Telecommunications	1.9%	8.3%	23%
			Energy	1.7%	12.7%	14%
			Insurance	1.7%	1.1%	156%
			Financial Services	0.8%	4.0%	20%
			Banking	0.0%	1.7%	0%
			Utility	0.0%	2.5%	0%

Distribution by Rating	Portfolio ¹	HY Market
A Holdings	0.0%	0.0%
BBB Holdings	1.4%	0.0%
BB Holdings	22.6%	55.4%
B Holdings	48.4%	32.7%
CCC or Under	27.7%	11.9%

Distribution by Issue Size	Portfolio ¹	HY Market
0 - 250M	7.7%	1.0%
250 - 500M	41.4%	24.9%
500 - 750M	17.2%	21.9%
750 - 1000M	12.3%	15.8%
1000+M	21.5%	36.3%

Top 5 Holdings by Weight	BofA Rating	Issue Size (\$mil)	Current Price	BofA Industry	Duration to Worst	Yield to Worst (%)	% of Portfolio
Townsquare Media Inc. 6.500% 01-Apr-2023	B3	280.1	86.75	Media	2.35	12.68	2.16
Great Lakes Dredge & Dock Corp. 8% 15-May-2022	B3	325.0	103.00	Transportation	0.83	5.02	2.02
Vizient Inc. 6.250% 15-May-2027	B2	300.0	104.50	Healthcare	3.40	5.13	1.67
WW International Inc 8.625% 01-Dec-2025	B2	300.0	104.75	Retail	2.14	7.24	1.42
Kronos Acquisition Holdings Inc 9% 15-Aug-2023	CCC3	890.0	95.25	Consumer Goods	2.55	10.82	1.36

Representative Short Duration High Yield Portfolio

Characteristics	Portfolio ¹	HY Market ²	SD Universe ³	Distribution by Sector	Portfolio ¹	HY Market ²	SD Universe ³
Avg Years to Maturity	3.9	6.2	3.4	Media	11.2%	9.8%	8.7%
Yield to Worst	5.54%	6.86%	5.96%	Basic Industry	11.1%	10.2%	11.8%
Current Yield	6.06%	6.45%	5.95%	Healthcare	10.0%	9.7%	9.4%
Duration to Worst	2.3	4.0	2.4	Telecommunications	8.9%	8.3%	7.2%
OAS	527	648	597	Financial Services	8.7%	4.0%	5.4%
Avg Coupon	6.07%	6.08%	5.83%	Capital Goods	7.5%	6.0%	5.1%
Number of Issuers	199	823	412	Services	6.6%	5.4%	4.9%
Number of Issues	289	1935	702	Leisure	6.1%	5.2%	5.5%
Average Rating	B1	B1	BB3	Technology & Electronics	5.6%	4.7%	4.4%
Average Price	100.13	94.38	98.00	Automotive	5.6%	5.4%	4.3%
				Retail	5.0%	4.8%	5.0%
				Consumer Goods	4.9%	5.4%	3.9%
				Real Estate	4.2%	2.0%	2.8%
				Transportation	2.1%	1.1%	2.7%
				Utility	1.2%	2.5%	1.7%
				Insurance	0.5%	1.1%	1.2%
				Other	0.4%	0.0%	0.0%
				Banking	0.4%	1.7%	2.2%
				Energy	0.1%	12.7%	13.8%

Distribution by Rating	Portfolio ¹	HY Market ²	SD Universe ³
A Holdings	0.0%	0.0%	0.0%
BBB Holdings	1.8%	0.0%	0.0%
BB Holdings	40.9%	55.4%	59.4%
B Holdings	46.2%	32.7%	40.6%
CCC or Under	11.1%	11.9%	0.0%

Distribution by Issue Size	Portfolio ¹	HY Market ²	SD Universe ³
0 - 250M	4.1%	1.0%	0.0%
250 - 500M	28.5%	24.9%	19.7%
500 - 750M	22.2%	21.8%	27.7%
750 - 1000M	10.6%	15.8%	13.1%
1000+M	34.6%	36.5%	39.4%

Top 5 Holdings by Weight	Average Rating	Issue Size (\$mil)	Current Price	BofA Industry	Duration to Worst	Yield to Worst (%)	% of Portfolio
Bausch Health Companies Inc 6.125% 15-Apr-2025	B2	3,250.0	101.37	Healthcare	2.51	5.56	0.89
Kennedy Wilson Inc 5.875% 01-Apr-2024	BB3	1,150.0	99.50	Real Estate	3.27	6.02	0.88
LPL Holdings Inc. 5.750% 15-Sep-2025	BB3	900.0	101.25	Financial Services	2.44	5.24	0.86
T-Mobile US Inc. 7.250% 15-Sep-2021	BB2	2,250.0	104.63	Telecommunications	1.14	3.13	0.86
HAT Holdings I LLC 5.250% 15-Jul-2024	BB1	500.0	101.50	Real Estate	2.72	4.54	0.80

1 Exclusive of Cash. 2,3 The Short Duration High Yield strategy is not a benchmarked product; the HY Indices shown are provided solely as a relative market indicators.

This comparison of selected characteristics of representative SKY Harbor portfolios on or about June 30, 2020 is provided for illustrative purposes only and is subject to change without notice in accordance with the strategies' stated objectives and the sole discretion of SKY Harbor's portfolio management team.

Source: SKY Harbor, FactSet, ICE BofA US High Yield Index "HOA0" (HY Market) and ICE BofA 1-5 Year BB-B US Cash Pay High Yield Constrained Index "JCV4" (SD Universe).

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