

High Yield Market Update

The third quarter of 2017 was the seventh straight quarter of positive returns for High Yield. Despite rising tensions with North Korea, widespread devastation inflicted by back-to-back hurricanes and continued legislative gridlock in Washington, the markets rallied during the quarter on the strength of the US economy and the potential for continued growth through tax reform and reduced regulation across key industries. During the quarter all sectors were positive, led by Energy as oil rallied with WTI Crude oil prices up 12.23%, closing Q3 at \$51.67 per barrel. Treasuries ended the quarter with the 2-year up 11 basis points (bps) to 1.49% and the 10-year up by 2 bps to 2.33% as the yield curve flattened.

High yield technicals were mixed in Q3 as high yield funds saw outflows but net supply was negative. High yield funds saw outflows of \$3.2bn, slightly offset by \$136mn of inflows for loan funds, as tracked by Lipper. For the quarter \$67.5bn of new issuance was offset by \$69.9bn of bond redemptions, leaving net supply at -\$2.46bn. The percentage of the market trading at

distressed levels (below 70% of par) ended Q3 at 2.7%, per JP Morgan. The par-weighted twelve-month default rate ticked lower to 1.7% at quarter-end, per BofA Merrill Lynch. Excluding commodities, the default rate was 1.5%.

The BofA Merrill Lynch US High Yield Index returned 2.04% in Q3, ending the period with an average price of 101.75, a 0.39 point increase from the prior quarter. Credit spreads tightened by 20 bps to 353 bps and the yield-to-worst was lower by 0.21% to 5.41%. High Yield outperformed investment grade corporates, as represented by the BofA Merrill Lynch US Corporate Index's 1.37% return, but underperformed small cap equities, as represented by the Russell 2000's 5.76%, and large cap equities, as represented by the S&P 500's 4.48% quarterly return. In High Yield, performance was positive across all credit qualities with the Double-B, Single-B and Triple-C sub-indices returning 2.03%, 1.80% and 2.65%, respectively. By sector, Energy was the top performer with a 4.48% return, while Retail was the bottom-performing sector, posting 0.22%.

Portfolio Performance

Portfolios managed by SKY Harbor according to our Unconstrained **Broad High Yield Market Strategy (BHYM)** performed in line with the benchmark in the third quarter of 2017. By risk type (defined by duration and yield to worst) overall security selection was a positive contributor to relative performance while allocation was a drag on performance. Security selection within the better quality, more rate sensitive and shortest duration, most defensive parts of the market were sources of outperformance. These were partially offset by weak selection in the most speculative part of the market. By sector, strong selection in Services and an underweight to the bottom-performing Retail sector were drivers of outperformance offset by weak selection in speculative Energy and an underweight to Energy during the rally in oil.

On a representative basis, the largest positive contributor to portfolio returns was Ahern Rentals Inc. (AHEREN) 7.375% notes due 2023, which traded up during the quarter on Q2 results and guidance that was appreciably ahead of Street expectations, reflecting much improved operating metrics amid a favorable industry backdrop. Last quarter's top contributor,

Approach Resources Inc. (AREX) was this quarter's largest bottom contributor, trading down during the quarter on technical pressure.

Broad High Yield Market Strategy: Performance

	SKY Harbor BHYM Strategy Performance			
	Gross of Fees	Net of Fees	BofA ML US HY Index	Alpha
Q1 2017	2.66	2.59	2.71	-0.04
Q2 2017	2.07	2.00	2.14	-0.07
July 2017	1.07	1.05	1.15	-0.08
August 2017	0.07	0.04	-0.03	0.09
September 2017	0.88	0.86	0.90	-0.02
Q3 2017	2.04	1.96	2.04	0.00
Year to Date 2017	6.92	6.68	7.05	-0.12
Last 12 Months	9.54	9.21	9.06	0.48
Three Years (annl)	5.24	4.92	5.87	-0.63
SI Return (annl)	8.37	8.03	8.38	-0.01

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.

Unconstrained **Short Duration High Yield Strategy (SDHY)** portfolios generated returns that approximated the current income for the quarter, capturing approximately 60% of the broader US high yield market return (as measured by the BofA Merrill Lynch US High Yield Index). A duration shorter than the broad market limited our ability to capture the full upward price move. The portfolios nevertheless posted returns which were in line with the historical capture rate of the SDHY strategy.

On a representative basis, at quarter-end our SDHY portfolios had a yield-to-worst of 4.08% (75% of the broad market yield). Exclusive of cash, the average coupon was 6.65% (vs. the

market average of 6.45%) and the duration-to-worst was 1.5 (or 43% of the broad market). Holdings (379 issues, representing 271 issuers) comprised 35% bonds with maturities of less than three years and 65% in longer maturities but trading to expected early take-outs inside this three-year period. We continue to believe that companies will proactively refinance debt ahead of stated maturities and capture the favorable interest rate environment that the new issue market still offers. Overall credit quality in SDHY portfolios was largely unchanged during the quarter: at quarter-end Double-B rated holdings represented 38.1% of the portfolio, Single-Bs were 48.6% and Triple-Cs were 10.0%.

Short Duration High Yield Strategy: Performance

	SKY Harbor SDHY Strategy Performance				Annualized Daily Volatility		
	Gross of Fees	Net of Fees	High Yield Market ¹	Market Capture	SKY SDHY Strategy	High Yield Market ¹	Relative Volatility
Q1 2017	1.59	1.50	2.71	59%	1.5	2.9	52%
Q2 2017	1.36	1.27	2.14	63%	0.9	1.6	54%
July 2017	0.68	0.65	1.15	59%	0.8	1.7	46%
August 2017	0.07	0.04	-0.03	NM	1.1	2.1	50%
September 2017	0.54	0.51	0.90	60%	0.5	0.8	59%
Q3 2017	1.29	1.21	2.04	64%	0.8	1.7	49%
Year to Date 2017	4.30	4.03	7.05	61%	1.1	2.1	52%
Last 12 Months	5.70	5.34	9.06	63%	1.3	2.5	53%
Three Years (annl)	3.46	3.09	5.87	59%	2.3	4.3	54%
Since Inception (annl)	4.65	4.26	8.38	62%	1.9	3.6	53%

1. The Short Duration High Yield strategy is not a benchmarked strategy. The HY Market index shown (BofA ML 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

While a variety of geopolitical risks remain, markets are benefiting from the strongest corporate earnings growth in the last five years. The overall high yield market has not reached cycle tight spreads, yet parts of the market have or are approaching cycle tightness. We continue to believe further spread compression is possible absent a general spike in risk premiums. Interest rate expectations seem to be rising, though not meaningfully enough yet to derail the most rate and spread sensitive parts of the market. Our conviction that fundamentals will continue to improve and HY defaults have peaked remains high and the strongest driver of portfolio positioning. However, we continue to believe we are generally not being paid to take "equity-like" risk at current market levels due to the underlying secular and/or cyclical changes that much of the remaining higher-yielding part of the market faces. We still expect high yield issuance to remain tilted towards better quality and refinancing, but generally be demand driven and sensitive to fund flows, which we expect to be more volatile. Based on our view of risks and valuations across the market, we continue to

believe Single-B rated credit offers the best opportunity for attractive returns through credit picking.

We believe our Broad High Yield Market portfolios continue to be well positioned for the current market environment. We have moderated our underweight to the better quality, more spread sensitive segment of the market such that we have reached our target positioning. We continue to look for opportunities to benefit from credit picking among the higher-yielding segments of the market although remain underweight this segment.

In our Short Duration High Yield Strategy, we continue to believe the portfolios are well positioned to take advantage of any potential volatility associated with changing geopolitical risks considering the large amount of front-end maturities and expected near-term calls held in the portfolio. Additionally, we continue to moderate our underweight to the more spread sensitive segment of the market and will use market volatility to opportunistically add attractively priced positions to the fund.

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	6.3	6.2	Basic Industry	18.8%	12.0%	156%	
Yield to Worst	5.44%	5.41%	Energy	11.9%	13.9%	85%	
Current Yield	6.64%	6.34%	Media	9.5%	11.4%	83%	
Duration to Worst	3.3	3.5	Healthcare	8.5%	9.7%	88%	
OAS	350	353	Technology & Electronics	8.5%	6.0%	142%	
Avg Coupon	6.88%	6.45%	Capital Goods	7.8%	5.4%	144%	
Number of Issuers	320	865	Services	6.9%	5.2%	132%	
Number of Issues	404	1877	Telecommunications	6.7%	10.1%	66%	
Average ML Rating	B2	B1	Leisure	4.5%	4.4%	101%	
Average Price	103.6	101.8	Financial Services	4.1%	3.7%	110%	
			Automotive	3.2%	2.2%	143%	
			Consumer Goods	2.5%	2.6%	94%	
			Banking	1.8%	3.3%	55%	
			Real Estate	1.5%	0.7%	228%	
			Transportation	1.1%	0.9%	116%	
			Retail	1.0%	4.9%	20%	
			Insurance	1.0%	0.9%	107%	
			Utility	0.8%	2.5%	30%	
Distribution by ML Rating	Portfolio ¹	HY Market					
A Holdings	0.0%	0.0%					
BBB Holdings	1.7%	0.0%					
BB Holdings	31.4%	47.9%					
B Holdings	47.6%	37.8%					
CCC or Under	19.4%	14.3%					
Distribution by Issue Size	Portfolio ¹	HY Market					
0 - 250M	6.7%	1.8%					
250 - 500M	36.8%	27.7%					
500 - 750M	19.5%	21.3%					
750 - 1000M	11.3%	15.7%					
1000+M	25.6%	33.5%					
Top 5 Holdings by Weight	BofA ML Rating	Issue Size (\$mil)	Current Price	BofA ML Industry	Duration to Worst	Yield to Worst (%)	% of Portfolio
Sprint Corporati 7.875% 15-Sep-2023	B2	4,248.9	116.00	Telecommunications	4.83	4.76	0.90
QUAD/GRAPHICS 7.000% 01-May-2022	B2	300.0	102.13	Media	3.78	6.45	0.81
Ahern Rentals In 7.375% 15-May-2023	B3	550.0	91.63	Services	4.32	9.35	0.79
Prince Mineral H 11.500% 15-Dec-2019	CCC1	285.0	104.00	Basic Industry	0.21	5.68	0.79
Mastec Inc. 4.875% 15-Mar-2023	BB3	400.0	102.00	Services	3.15	4.17	0.78

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	3.5	6.2	3.4	Basic Industry	17.0%	12.0%	12.9%
Yield to Worst	4.08%	5.41%	3.98%	Energy	11.7%	13.9%	13.6%
Current Yield	6.37%	6.34%	5.94%	Media	9.2%	11.4%	10.7%
Duration to Worst	1.5	3.5	1.9	Healthcare	8.9%	9.7%	7.6%
OAS	258	353	244	Telecommunications	8.1%	10.1%	10.2%
Avg Coupon	6.65%	6.45%	6.17%	Technology & Electronics	7.3%	6.0%	4.2%
Number of Issuers	271	865	369	Capital Goods	7.2%	5.4%	6.1%
Number of Issues	379	1877	579	Financial Services	6.9%	3.7%	8.3%
Average ML Rating	B1	B1	BB3	Leisure	4.5%	4.4%	5.2%
Average Price	104.40	101.76	103.93	Services	4.1%	5.2%	4.0%
				Transportation	3.5%	0.9%	1.7%
				Automotive	2.7%	2.2%	1.9%
				Consumer Goods	2.3%	2.6%	2.1%
				Retail	2.0%	4.9%	4.4%
				Real Estate	1.7%	0.7%	1.2%
				Utility	1.4%	2.5%	1.9%
				Banking	1.1%	3.3%	3.3%
				Insurance	0.3%	0.9%	0.8%
Distribution by Issue Size	Portfolio ¹	HY Market ²	SD Universe ³				
0 - 250M	6.7%	1.7%	0.0%				
250 - 500M	36.8%	27.5%	23.6%				
500 - 750M	20.6%	21.2%	25.4%				
750 - 1000M	12.6%	15.6%	14.3%				
1000+M	23.3%	33.9%	36.7%				
Top 5 Holdings by Weight	BofA ML Rating	Issue Size (\$mil)	Current Price	BofA ML Industry	Duration to Worst	Yield to Worst (%)	% of Portfolio
Sprint Nextel Co 7.000% 15-Aug-2020	B2	1,500.0	109.25	Telecommunications	2.60	3.58	0.72
Scientific Games 7.000% 01-Jan-2022	B1	2,100.0	106.00	Leisure	0.25	3.24	0.71
Sprint Corporati 7.250% 15-Sep-2021	B2	2,250.0	110.75	Telecommunications	3.45	4.17	0.68
HCA Inc. 6.500% 15-Feb-2020	BB1	3,000.0	108.88	Healthcare	2.20	2.62	0.65
DISH DBS Corpora 5.125% 01-May-2020	BB3	1,099.6	104.50	Media	2.37	3.16	0.62

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 September 30, 2017 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, BofA Merrill Lynch US High Yield indexes H0A0 and JVC4.

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