US Short Duration High Yield Fund

September 30, 2020

SKY HARBOR GLOBAL FUNDS

Monthly Commentary

Market

After five straight months of positive returns, risk assets hit a speedbump and High Yield turned negative in the month of September. Markets reacted negatively with increased concerns around the global economy as virus cases increased throughout the world. Also weighing heavily on the markets is the contention around the upcoming US elections as well as the decreasing likelihood for the US to pass a second stimulus package. After rising for 4 straight months, Oil took a hit in September with WTI Crude closing the month down $2.39/bbl (or 5.61%) to $40.22/bbl bringing the Energy sector down with it. The US dollar was up 1.89% on the month, and the US Treasury curve was relatively unchanged as the 2-yr Treasury remained at .13% and the 10-yr Treasury yield decreased 2 bps to 0.69%.

Technicals were a headwind in September with funds seeing outflows and we continued to have a heavy supply of new issuance. High Yield mutual funds/ETFs saw outflows of $7.7bn, while loan funds experienced outflows of $1.8bn, as tracked by Lipper and reported by Barclays. High yield new issuance was $45.5bn, as tracked by Barclays, while $27.9bn in bonds were redeemed or upgraded, leaving net supply at $17.6bn. The percentage of the high yield bond market trading at distressed levels (below 70% of par) remained at 4.5%; the comparable figure for the loan market (below 80% of par) decreased to 6.6%. The par-weighted twelve-month high yield bond default rate was unchanged at 7.2% at month-end, per BofA Merrill Lynch, and the loan market par-weighted trailing default rate ended May at a five-year-high of 4.26%, per JP Morgan.

The ICE BofA US High Yield Index returned -1.04% in September while the Credit Suisse Leveraged Loan Index returned 0.69%. The yield-to-worst (YTW) for the high yield index increased 35 bps to 5.70% and spreads increased 34 bps to 535 bps. By rating, the BB, B and CCC bond sub-indices returned -1.42%, -0.90% and 0.43%, respectively. Returns were mixed across sectors for the month with Transportation the top performer, returning 0.37%, while Energy was the bottom performer, posting -4.2%. Across risk types (defined by duration and yield to worst), more speculative securities outperformed while longer duration securities lagged. High yield underperformed investment grade corporate bonds, represented by the ICE BofA US Corporate Index's -0.26% return, but outperformed small cap equities, represented by the Russell 2000's -3.47% return, as well as large cap equities, represented by the S&P 500's -3.92% return.

Strategy

SKY Harbor Global Funds US Short Duration High Yield Fund ended the month with a slightly negative return but captured only 30% of the negative return of the broader US high yield market return (as measured by the ICE BofA US High Yield Index) on a gross of fee basis and excluding currency impact. A duration shorter than the broader high yield market helped to dampen volatility throughout the month. By risk type (defined by yield and duration to worst), the most speculative securities (yielding > 9%) which tend to trade on credit specific events, outperformed, generating a positive return while all other risk segments turned negative. By sector, Transportation and Insurance led while Utility and Real Estate lagged. By rating, lower quality led again this month, with Triple-Cs outperforming both Single-Bs and Double-Bs though all ratings segments were slightly negative. Looking forward, we continue to focus on the best risk-adjusted opportunities, which are typically in bonds maturing in 5 years or less and trading with durations of between 2.0 and 3.0.

Investment Objective

To generate a high level of current income while also experiencing lower volatility than the broader high yield market. The Fund principally invests in US below-investment-grade corporate debt securities that are expected to be redeemed through maturity, call or other corporate action within three years. The strategy seeks to capture the current income of the high yield market with substantially less volatility through the consistency of monthly returns and reinvestment.

Benchmark

Active strategy not managed in reference to a benchmark index

Portfolio Management

Lead PM: Anne C. Yobage, CFA
David Kinsley, CFA

Fund Detail

Fund Inception	Apr 05, 2012
Fund AUM	$2,628.0 mn
Order Cut-off	12:00 CET
Settlement	T+3
Dealing Frequency	Daily
Valuation Frequency	Daily

Statistics on performance, risk measures and portfolio characteristics are presented in share class Fund Factsheets available online at: http://skyharborglobalfunds.com/funds/usshortdurationhighyield.shtml

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Strategy (cont.)

The YTW on the Fund rose 52 bps to 4.61% and represented 81% of the broad market yield at month-end. The duration-to-worst increased to 1.9, or 52% of the broad market duration. The average coupon of 6.13% increased slightly from last month and was 7 bps the average coupon in the broad market. Exclusive of cash, Fund holdings (273 issues, representing 197 issuers) comprised 28% bonds with maturities of less than three years and 32% in longer maturities but trading to expected early take-outs inside this three-year period. Overall credit quality decreased slightly in the Fund: at month-end Double-B rated holdings represented 38.1% of the portfolio, Single-Bs were 49.0% and Triple-Cs were 11.4%.

Outlook

Investor surveys suggest that credit investors have been most focused on the upcoming election, having shifted from a focus on the timing and pace of an economic recovery. 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 evolved towards sectors where those risks are either over- or under-discounted.

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 over time. 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 appear ready to resize and evolve on an as-needed basis and development of both a coronavirus treatment protocol and a vaccine appear likely. Spread compression is likely to continue as a result. We believe the market has excess return opportunity associated with credit picking given the high level of dispersion in the market and are managing our portfolios with the expectations of improving earnings over the next 12 months.

About SKY Harbor Capital Management

SKY Harbor Capital Management, LLC ("SKY Harbor"), an independent investment manager registered with the US Securities and Exchange Commission, is the appointed Investment Manager for SKY Harbor Global Funds. SKY Harbor offers a range of US high yield and leveraged loan strategies for global institutional investors and private wealth advisors. Senior leadership and co-founders Hannah Strasser and Anne Yobage have managed high yield investments as a team through multiple market cycles for nearly 30 years. SKY Harbor's process is grounded in fundamental analysis, then refined by quantitative and technical assessment, to identify income potential while effectively managing risk. SKY Harbor is based in Greenwich, CT USA. Visit www.skyhcm.com.

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