US Short Duration Sustainable High Yield Fund

May 31, 2021

SKY HARBOR GLOBAL FUNDS

Monthly Commentary

Market

US High Yield generated less than coupon income returns in May. Earnings beats and relaxation of pandemic restrictions boosted sentiment for lower-quality credit and sectors levered to a re-opening outperformed for the month. Fed commentary about tapering and general concern surrounding inflationary pressures weighed on the more rate-sensitive portions of the market. The rally in Oil continued in May with WTI Crude closing the month up $2.74/bbl (or 4.31%) to $66.32/bbl causing the Energy sector to be one of the top performers for the month, returning 0.84%. The US dollar was down 1.59% on the month, and the US Treasury curve was relatively unchanged as the 2-yr Treasury decreased to 0.15% and the 10-yr Treasury yield decreased to 1.60%.

Technicals were a headwind in May with a return of investor outflows and continued positive net supply for the month. High Yield mutual funds/ETFs saw outflows of $4.0bn, while loan funds experienced inflows of $4.2bn, as tracked by Lipper and reported by Barclays. High yield new issuance remained elevated in May at $48.8bn, as tracked by Barclays, while $25.0bn in bonds were redeemed or upgraded, leaving net supply at $23.8bn for the month. The percentage of the high yield bond market trading at distressed levels (below 70% of par) increased to 0.6%; the comparable figure for the loan market (below 80% of par) decreased to 1.8% for the month. The par-weighted twelve-month high yield bond default rate was down to 3.1% at month-end, per BofA Merrill Lynch, and the loan market par-weighted trailing default rate ended May at 1.96%, per JP Morgan.

The ICE BofA US High Yield Index returned 0.29% in May while the Credit Suisse Leveraged Loan Index returned 0.52%. The yield-to-worst (YTW) for the high yield index increased 4 basis points (bps) to 4.06% and spreads increased 8 bps to 329. By rating, the BB, B and CCC bond sub-indices returned 0.25%, 0.17% and 0.80% for the month, respectively. Returns were mixed across sectors for the month with Banking the top performer, returning 0.94%, while Healthcare was the bottom performer, posting -0.43%. Across risk types (defined by duration and yield to worst), more speculative securities continue to outperform shorter duration, more defensive securities. High yield underperformed investment grade corporate bonds, represented by the ICE BofA US Corporate Index's 0.70% as well as large cap equities, represented by the S&P 500's 0.55% return, but outperformed small cap equities, represented by the Russell 2000's 0.11% return.

Strategy

SKY Harbor Global Funds US Short Duration Sustainable High Yield Fund posted a positive return in May, outperforming the broader US high yield market (as measured by the ICE BofA US High Yield Index) on a gross of fee basis and excluding currency impact. By risk type, the shortest duration, most defensive securities outperformed longer duration (within the context of short duration). All sectors generated positive returns for the month with the exception of Healthcare which was very slightly negative. By rating, lower quality led, with Triple-Cs outperforming Double-Bs and Single-Bs. Looking forward, we continue to focus on maintaining a relatively high current income by selling when valuations are too tight or negative convexity limits further upside and rotating into issuers that align with our FASST positioning.

The YTW on the Fund tightened another 6 bps to 3.69% but still capturing over 90% of the broad market yield at month-end. The duration-to-worst was unchanged at 1.5, or 42% of the broad market duration. The average coupon of 6.87% increased slightly from last month and was 96 bps the average coupon in the broad market. Exclusive of cash, Fund holdings (204 issues, representing 151 issuers) comprised 21% bonds with maturities of less than three years and 79% in longer maturities but trading to expected early take-outs inside this three-year period. Overall credit quality was essentially unchanged in the Fund: at month-end double-B rated holdings represented 23.8% of the portfolio, Single-Bs were 57.1% and Triple-Cs were 17.2%.

Investment Objective

ESG socially responsible active investment strategy seeking to generate a high level of current income with lover volatility by diversified investments in US dollar-denominated high yield corporate bonds expected to mature, be call or otherwise be redeemed within three years.

Benchmark

Active strategy not managed in reference to a benchmark index.

Portfolio Management Group

Anne C. Yobage, CFA
David Kinsley, CFA
Mike Salice, CFA
Ryan Carrington, CFA

Fund Detail

Fund Inception	Apr 05, 2012
Fund AUM	$2,644.5 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

Outlook

Risk assets have benefited from resolution of various key identified risks – the US election, vaccine roll-out, and COVID-19. The sharp rise in interest rates suggests investors have shifted towards focusing on rising inflationary pressures and the path to higher rates. Valuations across risk assets are also top of mind for credit investors.

Investor perception of risks around fundamentals has benefited from a strong recovery in earnings and generally strong aggregate economic data that is supportive of tighter credit spreads over time. Default risk is rapidly normalizing, and the credit ratings cycle is swinging to the positive after a pandemic-induced downgrade cycle. We continue to believe that there remains an opportunity around spread compression based upon lower defaults and strong economic and market conditions.

We believe the market has excess return opportunity associated with sector allocation and credit picking and are mindful of tighter valuations across better quality segments of the market. Unlike last year where picking bonds with recovering results and attractive valuations was a key driver of returns, this year we expect returns will be a function of missing companies that stumble and are rerated to higher yields. Our valuation work suggests a bias towards cyclicals versus defensive issuers and smaller issue sizes over larger issues that have been pushed tighter by ETF buying. We are also biased towards the sectors that are better positioned for somewhat higher corporate taxes.

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.

Contact

info@skyhcm.com

+49 69 75938622

+1 203 769 8800

Find all fund documents at:
www.skyharborglobalfunds.com

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