



Quarterly Commentary

*And all that is now
And all that is gone
And all that's to come
And everything under the sun is in tune
But the sun is eclipsed by the moon*

– Pink Floyd

We had to have an “eclipse” reference this month. It was either Pink Floyd or Bonnie Tyler (“Total Eclipse of the Heart”). Classic rock won out.

Anticipation of Federal Reserve interest rate policy seems to eclipse everything else in the market. The first quarter of 2024 witnessed a reversal of some of the rate-cut euphoria of Q4 2023. The Q4 2023 expectations for significant rate reductions weighed on Q4 portfolio performance. The portfolios benefitted in Q1 from some lessening of those expectations.

We are not sure when or by how much the Federal Reserve will cut interest rates. Furthermore, while not the most likely, we don't completely discount the possibility of zero cuts this year or further increases down the road. We were happy to hear Federal Reserve Chairman Powell state something we have been harping on for some time. Interest rates are not going back to pre-pandemic levels. The post-2008 interest rate environment was unique, not normal. Powell does not think it is likely that we would return to long-run rates that are in the 2% range. He also doesn't see long-term rates around the world returning to levels at or below zero.

Money-losing, long-duration equities have been a big beneficiary of ultra-low interest rates. We've written in the past about the high concentration of these companies in our value benchmarks and our significant underexposure to them. These stocks react favorably to rate reduction expectations. We continue to look for companies that meet our investment criteria and respond favorably to lower rates. We have found some investments, but not enough to completely offset our underexposure.

The upcoming Russell rebalance holds a sliver of good news. Some of the value indexes will likely see the weight of non-earners slightly decrease. Our lead risk analyst, Mike Wayton, projects that non-earners would decrease by approximately 1.6 percentage points in the Russell 2000® Value Index, by almost 1% in the Russell Midcap® Value Index benchmark, and remain roughly the same in the Russell 2500™ Value Index. The exposure will still be significant, but we will take any relief we can find.

Mike also estimates the rebalanced benchmarks will have slightly lower betas, smaller growth rates, and lower valuations. In short, they will be more value-like. The Russell rebalance is scheduled for Friday, June 28. The first official, preliminary index membership lists are expected to be released on Friday, May 24. We will have more certainty around these characteristics as well as sector weights at that time.

Here in Cleveland, we are within the path of totality of the April 8, 2024 eclipse. The last time this happened was 1806. The next occurrence will be 2444. That's about as rare as seeing near-zero to negative interest rates. We don't know if it will be 400 years before zero rates happen again, but we don't think it will be soon. As we have stated before, we believe “normal” rates could provide the catalyst to reverse the significant underperformance of small-caps vs. large-caps and value vs. growth. Time will tell. In the meantime, we will continue to apply our flexible value strategy, searching for undervalued stocks with a catalyst, keeping a close eye on the risk in our portfolios, and striving for consistent, long-term performance for our clients.

Quarterly Commentary

The best performing sectors of the market were energy and industrials. Communication services was the worst performing sector in the benchmark. Small/mid cap value underperformed small/mid cap growth.

The Victory Integrity Small/Mid Cap Value Fund (A shares without sales charge) outperformed the Russell 2500™ Value Index benchmark for the period. Solid security selection resulted in outperformance led by financials, real estate, utilities, and health care. Stock selection in consumer discretionary limited performance. Sector weights were positive as our underweight to real estate helped.

Strong stock selection in insurance was the top contributor within financials. Kinsale Capital Group, Inc. (KNSL), up 57%, was the main highlight as earnings and sales growth reaccelerated from a rare third quarter slowdown. Banks were another positive as our average holding outperformed the benchmark. We benefitted from avoiding some of the worst performing banks, such as New York Community Bancorp (NYCB), which was down 68%. In general, banks underperformed after a strong rally and reduced expectations for near-term interest rate cuts. Our largest detractor within banks, Veritex Holdings, Inc. (VBTX), was down 11%.

In addition to our underweight in real estate, stock selection was helpful as our average holding outperformed the benchmark (+2% versus -2%).

Vistra Corp. (VST), up 81%, benefitted from higher power prices as supply continues to shrink and strong demand growth from data centers.

Tenet Healthcare Corp. (THC) and Select Medical Holdings Corp. (SEM) led the way within health care. Favorable trends as contract labor utilization continues to decline as well as improving revenue and cost expectations aided Tenet Healthcare Corp. (THC). The company also announced the sale of two hospitals at favorable terms. Select Medical Holdings Corp. (SEM) announced it will spin off its Concentra business segment to unlock its value.

Victoria's Secret & Company (VSCO) and Caesars Entertainment Inc. (CZR) hampered performance within consumer discretionary. Victoria's Secret & Company (VSCO) issued disappointing guidance resulting from intimates category weakness. Caesars Entertainment Inc. (CZR) preannounced results that trailed expectations as their business was impacted by construction, lower player profitability, and finalized union labor negotiations. Marriott Vacations Worldwide Corp. (VAC) and Ralph Lauren Corporation Class A (RL) were bright spots. Marriott Vacations Worldwide Corp. (VAC) rebounded after delivering better-than-feared earnings and guidance. Ralph Lauren Corporation Class A (RL) delivered solid earnings as the brand continues to benefit from initiatives to keep inventory clean and elevate AURs (average unit retail).

Communication services helped performance, largely due to Cinemark Holdings, Inc. (CNK). Shares rallied on better-than-expected results as well as commentary that leverage is back to within its target range, increasing the prospects for future capital return.

Positive stock selection in industrials was paced by Core & Main, Inc. Class A (CNM); Saia, Inc. (SAIA); and Carlisle Companies Inc. (CSL). Core & Main, Inc. Class A (CNM) benefitted as it beat fourth quarter estimates and provided better-than-expected 2024 guidance on sales and margins. Strong earnings that demonstrated better operating leverage and cost controls lifted shares of Saia, Inc. (SAIA). A strong fourth quarter earnings report and the bottoming of commercial roofing orders helped drive strong performance in Carlisle Companies Inc. (CSL). A couple of companies limited performance. Shares of GXO Logistics Inc. (GXO) declined as slower European growth has investors more cautious on their outlook. We sold the position. Vestis Corp. (VSTS) struggled as the company provided disappointing 2024 guidance after losing a customer contract.

Juniper Networks, Inc. (JNPR) and MKS Instruments, Inc. (MKSI) were the top highlights in technology. Juniper Networks, Inc. (JNPR) announced they would be acquired for a premium by Hewlett Packard (HPE). Better-than-feared guidance as well as progress on de-leveraging the balance sheet boosted shares of MKS Instruments, Inc. (MKSI). Performance in semiconductors was a source of weakness. Diodes Incorporated (DIOD) lagged going into earnings on inventory and end-market demand concerns. Synaptics Incorporated (SYNA) issued disappointing guidance on weakness in enterprise and automotive end markets. An unexpected resignation of their CFO for a lateral move to a competitor also pressured shares. Kulicke & Soffa Industries, Inc. (KLIC) reported an in-line quarter, but guidance trailed estimates as auto and power semiconductor weakness impacted demand.



Quarterly Commentary

Overall selection in energy generated a small positive. Permian Resources Corporation Class A (PR) was the top contributor as the company outperformed on the back of a strong fourth quarter and successful synergy realization after they acquired Earthstone Energy (ESTE) in the fourth quarter of 2023. CONSOL Energy (CEIX) limited performance in the aftermath of the Francis Scott Key Bridge collapse. A significant portion of coal transport will be blocked for an indeterminant time until the wreckage is cleared. We sold the position.

Overall performance in materials was flat. Berry Global Group Inc. (BERY) and Chemours Co. (CC) underperformed. Concurrent with fourth quarter results, Berry Global Group Inc. (BERY) announced the spin-off of its healthcare business, which negatively surprised investors who expected a full sale. Chemours Co. (CC) announced a delay to its fourth quarter earnings call and material weaknesses to its internal controls. We exited the position ahead of the CEO and CFO being fired.



Quarterly Commentary

Past performance does not guarantee future results. For standardized performance, please visit www.vcm.com.

Carefully consider a fund's investment objectives, risks, charges and expenses before investing. To obtain a prospectus or summary prospectus containing this and other important information, visit www.vcm.com/prospectus. Read it carefully before investing.

All investing involves risk, including the potential loss of principal. In addition to the normal risks associated with investing, investments in small- and mid-cap companies typically exhibit higher volatility. Investments concentrated in an industry or group of industries may face more risks and exhibit higher volatility than investments that are more broadly diversified over industries or sectors. Investments in companies in the industrials sector may be adversely affected by changes in supply and demand for products and services, governmental regulation and changes spending policies, world events and economic conditions. International investments may involve risk of capital loss from unfavorable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations. The value of your investment is also subject to geopolitical risks such as wars, terrorism, environmental disasters, and public health crises; the risk of technology malfunctions or disruptions; and the responses to such events by governments and/or individual companies.

The Russell 2500™ Value Index is a market-capitalization-weighted index that measures the performance of those companies in the Russell 2500™ Index with higher composite value scores.

Fund holdings mentioned in the Quarterly Commentary are as of 3/31/2024 and the percentages shown are based on net assets as of that date. Fund holdings are subject to change and should not be considered purchase recommendations. There is no assurance that the securities mentioned remain in the Fund's portfolio or that securities sold have not been repurchased. The Fund's top ten holdings as of 3/31/2024 were Carlisle Companies Inc (1.5%), ITT, Inc (1.3%), Cleveland-Cliffs Inc (1.3%), Pentair plc (1.2%), Textron Inc (1.3%), Saia, Inc (1.2%), First Industrial Realty Trust, Inc (1.2%), Reliance, Inc (1.2%), Commercial Metals Company (1.1%), and Gaming and Leisure Properties, Inc (1.1%). Top holdings do not reflect cash, money market instruments, or options/futures contracts holdings. The most currently available data regarding portfolio holdings can be found on our website, www.vcm.com.

Contributors and Detractors Source: FactSet. The contributors and detractors mentioned are presented to illustrate examples of the Fund's investments and may not be representative of the Fund's current or future investments.

The information in this article is based on data obtained from recognized services and sources and is believed to be reliable. Any opinions, projections or recommendations in this report are subject to change without notice and are not intended as individual investment advice. The securities highlighted, if any, were not intended as individual investment advice.

Distributed by Victory Capital Services, Inc., an affiliate of Victory Capital Management Inc., the Fund's investment adviser.

V17.054 // 1Q 2024 INTGY SMID Cap Val Fund COM

