

# Quarterly Commentary

*Cloudy With a Chance of Meatballs*  
(2009)

This past quarter had more twists and turns than a roller-coaster ride at Cedar Point (FUN). Volatility was the word of the quarter. We had a little bit of everything—the bombing of a Saudi Aramco oil field, the opening of the impeachment inquiry into Donald Trump, plunging global interest rates, a violent sell-off in August followed by a deep value micro-cap rally to start September, strains in the repo market, the continued saga of the U.S.-China trade war, and a yield curve that has bounced in and out of inversion.

As we enter this upcoming earnings season with the backdrop of slowing global growth and global manufacturing in a recession, we are expecting a tremendous amount of volatility. We are planning to use this volatility opportunistically to tilt the portfolio a little more cyclically. With global interest rates declining and a solid U.S. jobs market, we feel this could be an interesting time to tactically add a modest amount of exposure to smaller cyclical companies as their valuations become more attractive. While smaller/micro companies have underperformed year to date, we are mindful of the potential tailwind for these companies if we are not going off a cliff. All of this is predicated on our belief that the U.S. will not go into a recession and that global economies, while weak, are bottoming. Historical recession indicators (beyond the inverted yield curve) are not evident, such as surging oil prices, spiking initial unemployment claims, and widening of credit spreads, and there are no obvious bubbles to unwind. The best performing sector of the market was real estate (+8.2%). Utilities and consumer staples also outperformed. Energy was the worst performing sector (-12.5%). Communication services also underperformed. Mid value outperformed mid growth.

The Victory Integrity Mid-Cap Value Fund (A shares without sales charge) outperformed the Russell Midcap<sup>®</sup> Value Index for the quarter. Stock selection in health care, consumer discretionary, and technology led to outperformance. Utilities and real estate were very minor sources of underperformance. These were the two best performing sectors, and our underweights detracted slightly. A larger beta and a lower dividend yield hurt.

Positive performance in health care was driven by Zimmer Biomet Holdings, Inc. (ZBH) and Perrigo Co. Plc (PRGO). Zimmer Biomet Holdings, Inc. (ZBH) exceeded analysts' estimates and raised its 2019 outlook. Organic growth accelerated and gross margins improved to drive the earnings beat. Perrigo Co. Plc (PRGO) acquired rights to market Prevacid 24HR from GlaxoSmithKline, which aligns with the new CEO's strategy to strengthen the brand portfolio.

Aramark (ARMK) and D.R. Horton, Inc. (DHI) led the way in consumer discretionary. News of an activist taking a position and the retirement of the CEO following a spate of mis-executions boosted shares of Aramark (ARMK). Falling mortgage rates aided performance of homebuilders with exposure to entry-level customers such as D.R. Horton, Inc. (DHI). Softness in the North American business and second-half concerns for that segment led to underperformance for Ralph Lauren Corporation Class A (RL).

SYNNEX Corporation (SNX), Western Digital Corporation (WDC), and Symantec Corporation (SYMC) outperformed within technology. Strength in the distribution segment resulted in a beat-and-raise quarter at SYNNEX Corporation (SNX). Western Digital Corporation (WDC) rebounded as memory market fundamentals improved. Shares of Symantec Corporation (SYMC) rallied on the announcement of the sale of their enterprise business to Broadcom and news reports of acquisition interest for their consumer business as well. DXC Technology Co. (DXCM) reported disappointing earnings results as the core business continues to struggle with cannibalization by lower-cost, lower-margin digital solutions.

Energy was a very minor positive, as our average holding outperformed. Materials was a small help thanks to Martin Marietta Materials, Inc. (MLM), which is seeing strong aggregate volumes and pricing. Some of this was offset by Cabot Corporation (CBT), which missed earnings and cut guidance due to weakening demand trends and compressing margins.

Utilities was the second-best performing sector (+7.3%), with real estate the best performing sector (+8.2%). We were underweight both sectors, and this was a slight headwind.

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Industrial performance was a very small negative. Dycom Industries, Inc. (DY) underperformed as the market sold high-beta names in favor of lower volatility. Timken Company (TKR) was down almost 15% as it reduced 2019 guidance for slower sales and earnings growth due to macro concerns.

With visibility very limited, maybe the 2009 movie title *Cloudy With a Chance of Meatballs* describes this market environment perfectly, as we never know what's coming next! However, with an easing global interest rate environment, a solid U.S. consumer, global economies that appear to be bottoming, negative investor sentiment, and the possibility of a China trade deal/truce, this could certainly set up a more positive economic backdrop.

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### Past performance does not guarantee future results.

**Risks Associated with Investing in the Fund:** The Fund invests in smaller and medium-sized company stocks, which are more volatile and less liquid than larger, more established company securities. Value-based investments are subject to the risk that the broad market may not recognize their intrinsic value. A substantial portion of the Fund's assets is invested in the financial sector, whose performance can be significantly negatively impacted by economic downturns and changes in government regulation and interest rates. The Fund may invest up to 25% of its assets in foreign securities, which involve additional risks due to currency fluctuations, economic and political conditions, and differences in financial reporting standards. Performance and after-tax returns can be significantly impacted by the Fund's investments in Initial Public Offerings (IPOs), which may involve short-term trading. We cannot, however, ensure that the Fund will obtain IPOs.

**Indexes Defined** The Russell Midcap<sup>®</sup> Value Index measures the performance of those Russell Midcap<sup>®</sup> companies (approximately 800 of the smallest securities in the Russell 1000<sup>®</sup> Index, which includes the 1,000 largest stocks by market capitalization in the Russell 3000<sup>®</sup> Index, an index of the top 3,000 U.S. stocks by market capitalization covering 98% of the U.S. equity investable universe) with higher composite value scores. The S&P 500<sup>®</sup> Index is a widely recognized capitalization-weighted index that measures the performance of the large-capitalization sector of the U.S. stock market. You cannot invest directly in an index. Although reinvestment of dividend and interest payments is assumed, no expenses are netted against an index's returns.

Fund holdings mentioned in the Quarterly Commentary are as of 9/30/2019 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 9/30/2019 were: SunTrust Banks, Inc (1.6%), Zimmer Biomet Holdings, Inc. (1.5%), HCP, Inc. (1.5%), PPL Corporation (1.5%), Duke Realty Corp (1.5%), Fifth Third Bancorp (1.4%), Camden Property Trust (1.3%), Martin Marietta Materials, Inc (1.3%), Laboratory Corporation of America Holdings (1.3%), and Apartment Investment and Management Co (1.3%). 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](http://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. Fund holdings are as of quarter-end and may change at any time.

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