

Trivalent International Small-Capitalization Equity Strategy Quarterly Commentary



As of September 30, 2019

Market Environment

International small-cap equities retreated in the third quarter amid rising trade tensions and weak global economic data. For the quarter, the S&P Developed ex-U.S. SmallCap Index declined 1.6%, while the Trivalent International Small-Capitalization Equity Strategy outperformed the benchmark. Most countries ended in negative territory. South Korea declined 12.5% after it was removed from Japan's favored trade partners list due to worsening diplomatic relations between the two countries. Hong Kong fell 11.1% on growing concerns over mass pro-democracy protests to resist mainland China authority. The United Kingdom was down 1.9% as hard-line Brexit Boris Johnson was elected to succeed Theresa May as Britain's prime minister. On the upside, Israel and Belgium were the top performing countries, advancing 8.1% and 6.6%, respectively. Japan also outperformed, up 2.7% despite an escalating trade dispute with South Korea.

Nine of eleven sectors posted negative returns. Energy stocks were hit the hardest, down 5.4% as the price of Brent Crude fell 8.7%. Health Care stocks were also weak, down 5.2%. The more defensive Real Estate and Utilities sectors were the top performers, up 5.5% and 2.7%, respectively.

Portfolio Review

Overall security selection was positive and accounted for most of the strategy's outperformance. Excess returns were generated in all five regions and ten of the eleven economic sectors. Notable outperformance was generated in the Consumer Discretionary, Health Care, and Information Technology sectors. JD Sports Fashion was among the top contributors. The United Kingdom-listed athleisure retailer rose 24.1% as its JD Sports and Finish Line formats continue to gain market share in their respective markets, backed by strong relationships with Nike and Adidas. A sizable position in Carl Zeiss Meditec boosted performance in the Health Care sector. The German medical technology company rose 15.4% after reporting strong earnings and raising full-year guidance. The company's ophthalmic unit has seen strong demand from Asia for laser consumables and lenses. Within Information Technology, Japanese precision equipment provider Lasertec rose 58.0% after full-year results demonstrated strong demand for its inspection equipment used in cutting-edge lithography.

On the downside, security selection was weakest in the Industrials sector and was most negatively impacted by two holdings. German diesel engine manufacturer Deutz dropped 40.6% as the CEO commented that demand for its motors may have passed the peak in the current cycle and a recent supplier bankruptcy will limit margin improvement in the near-term. Pulp and paper machinery manufacturer Valmet declined 22.2% as demand for its service business saw disappointing progress in the second quarter. Another top detractor was Materials holding Iluka Resources Limited. The Australian mineral sands producer slumped 37.2% as strict environmental regulations in China have led to a decline in zircon demand from the ceramics market.

Market Outlook

Market uncertainty is likely to continue as global trade tensions weigh on economic growth, particularly impacting the export-oriented manufacturing companies. Within the eurozone, manufacturing PMI has remained below the contraction level for the last eight months. In response, the European Central Bank has cut the interest rate on bank reserves by a tenth of a percentage point to -0.5% and has restarted its asset purchase program at €20B per month. The rate cut pushes the ECB's monetary policy further into uncharted territory as investors remain uncertain of the implications and overall effectiveness of negative interest rates. In theory, ultra-accommodative monetary policy should be stimulative. Despite the macroeconomic headwinds facing the eurozone, domestic demand remains resilient as lending to eurozone businesses grew at the fastest pace in a decade. Any positive trade developments between the United States and China would be a meaningful boost to international equities, particularly for Europe and Japan. Within the United Kingdom, Brexit remains key as Parliament voted to prevent Prime Minister Boris Johnson from withdrawing from the European Union on October 31 without a deal in place. The Benn Act requires the prime minister to ask the European Union for an extension to the Brexit negotiation period. From a valuation standpoint, international small-cap earnings multiples remain attractive relative to U.S. equities and historical levels, trading below their five-year average multiples. Opportunities for relative outperformance remain, particularly among the diverse and broad segment of international small- and mid-cap equities. We continue to be guided by our bottom-up analysis and remain focused on stock selection while adhering to our disciplined country and sector risk exposures.

Representative Account		
Top 5 Contributors* (%)	Return	Contribution to Relative Return

Lasertec Corp.	58.0	0.3
JD Sports Fashion Plc	24.1	0.3
Beach Energy Limited	23.0	0.2
Advantest Corp.	61.9	0.2
Entertainment One Ltd.	38.4	0.2

Representative Account		
Top 5 Detractors* (%)	Return	Contribution to Relative Return

DEUTZ AG	-40.6	-0.2
Valmet Corp	-22.2	-0.1
Iluka Resources Limited	-37.2	-0.1
Nexteer Automotive Group Limited	-37.5	-0.1
Dometic Group AB	-21.6	-0.1

Representative Account		
Top 10 Holdings	Country	Sector

Teleperformance SE	France	Industrials
JD Sports Fashion Plc	United Kingdom	Consumer Discretionary
Swiss Life Holding AG	Switzerland	Financials
Charter Hall Group	Australia	Real Estate
Beach Energy Limited	Australia	Energy
Net One Systems Co., Ltd.	Japan	Information Technology
Logitech International S.A.	Switzerland	Information Technology
Carl Zeiss Meditec AG	Germany	Health Care
TIS Inc.	Japan	Information Technology
Eiffage SA	France	Industrials

Total % of Portfolio 11.88%

Source: FactSet.

Information relating to portfolio holdings is based on the representative account in the composite and may vary for other accounts in the strategy due to asset size, client guidelines, and other factors. The representative account is believed to most closely reflect the current portfolio management style.

ANNUALIZED RETURNS

Composite Performance (%)	ANNUALIZED RETURNS						Since Inception 9.1.07
	QTR	YTD	1-YR	3-YR	5-YR	10-YR	
Trivalent International Small-Capitalization Equity (Gross)	0.60	17.25	-4.90	7.97	7.18	11.20	4.76
Trivalent International Small-Capitalization Equity (Net)	0.36	16.42	-5.79	6.95	6.17	10.20	3.87
S&P® Developed ex.-U.S. SmallCap Index (Net)	-1.61	11.11	-7.35	4.85	4.80	6.75	2.95

Source: Zephyr StyleADVISOR.

DISCLOSURES

Investing involves risk and there is no guarantee any investment will be profitable specifically in extreme market conditions. Loss of principal is possible. The value of an investment will fluctuate in response to macro factors such as general economic conditions, interest rates, and the political environment, as well as changes in the prospects of particular companies, including market, liquidity, credit, and management risks.

Past performance cannot guarantee future results. Returns for periods greater than one year are annualized. Returns are expressed in U.S. dollars. Composite returns are net of transaction costs and gross of non-reclaimable withholding taxes, if any, and reflect the reinvestment of dividends and other earnings.

Gross-of-fees returns are presented before management and custodial fees but after all trading expenses. Net-of-fees returns are calculated by deducting one-twelfth of the highest tier of the standard fee schedule in effect for the period noted (the model fee). The composite model fee for each period is either the highest tier of the current fee schedule or a higher value, whichever is required to ensure the model composite net-of-fee return is lower than or equal to the composite net-of-fee return calculated using actual fees. Actual fees may vary depending on, among other things, the applicable fee schedule and portfolio size. The firm's fees are available on request and may be found on Part II of its Form ADV.

The Trivalent International Small-Capitalization Equity strategy focuses on foreign small-cap companies that are characterized by improving business momentum and attractive valuations.

Index returns are provided to represent the investment environment during the periods shown. The index is fully invested, including the reinvestment of dividends and capital gains. Index returns do not include transaction costs, management fees or other costs. Non-U.S. indices are net of non-reclaimable withholding taxes, if any.

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*Contributors and Detractors Source: FactSet. The top contributors and detractors are presented to illustrate examples of the portfolio's investments and may not be representative of the portfolio's current or future investments. The percent displayed in the final column is contribution to return. Holdings are as of quarter end and may change at any time.

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