



PORTFOLIO UPDATE AND MARKET OUTLOOK

July 31, 2024

“The world ain’t all sunshine and rainbows. It’s a very mean and nasty place and I don’t care how tough you are it will beat you to your knees and keep you there permanently if you let it. You, me, or nobody is gonna hit as hard as life.”

–Sylvester Stallone as Rocky Balboa

We are a little delayed with this month’s Catalyst. There seems to be a new development every day. It feels like we have lived through three market cycles in the last three weeks. We have seen a Federal Reserve pivot, a market rotation, and a market selloff.

The Fed pivot came about as inflation appears to have cooled along with the economy. Most investors believe that the Fed has signaled they are likely to cut interest rates at their next meeting.

We have written extensively how rate cut expectations fuel the non-earning companies in our benchmarks. This time was no different. In July, low/no profit companies, biotechnology stocks, and highly shorted issues were among the best performers. Our lack of exposure to these companies was a headwind to the month’s performance. *(continued on page 2)*

Performance (%)

Representative Accounts

	MTD			QTD			YTD		
	Gross	Net	vs. Benchmark*	Gross	Net	vs. Benchmark*	Gross	Net	vs. Benchmark*
Small Cap Value	9.05	8.96	-3.13	9.05	8.96	-3.13	10.07	9.43	-1.16
Small/Mid Cap Value	7.21	7.14	-0.89	7.21	7.14	-0.89	12.11	11.56	+2.39
Mid Cap Value	5.35	5.28	-0.69	5.35	5.28	-0.69	12.69	12.16	+1.83
Micro Cap Value	11.86	11.76	-0.95	11.86	11.76	-0.95	12.53	11.88	+1.61

Source: SEI

Past performance does not guarantee future results. Representative accounts are those of the Integrity Small Cap Value Equity Strategy, Integrity Small/Mid Cap Value Equity Strategy, Integrity Mid Cap Value Equity Strategy, Integrity Micro Cap Value Equity Strategy. Performance is preliminary and subject to change. Benchmark comparison is versus gross performance.

Market Returns (%)

	MTD	QTD	YTD
S&P 500® Index	1.22	1.22	16.70
Nasdaq 100® Index	-1.59	-1.59	15.60
Russell 2000® Growth Index	8.19	8.19	12.99
Russell 2000® Value Index	12.19	12.19	11.23

Past performance does not guarantee future results. Indices represent different segments of the market and are not correlated to the strategies above, with the exception of the Russell 2000® Value Index, which is the benchmark for Integrity Small Cap Value Equity.



Daniel G. Bandi, CFA is Chief Investment Officer for Integrity’s value equity strategies and lead portfolio manager for the company’s Small-Cap Value Equity strategy and Small/Mid-Cap Value Equity strategy.

We also witnessed a significant rotation away from mega-cap tech stocks into small cap issues. The Russell 2000® Index outperformed the S&P 500® Index by over 10 percentage points in July. The equal-weighted S&P 500 beat the S&P 500 by more than four percentage points. The Philadelphia Semiconductor Index posted a loss of more than four percent for the month as investors fled the AI trade.

Before the talking heads could even debate whether this rotation was real or if the small-cap rally was over, the market experienced its first significant selloff in some time. There is some debate about what caused it. The two most common theories are a weak jobs report signaling recession and the unwind of the Yen carry trade.

We have seen our share of earnings disappointments in our cyclical sectors. This seems to support the recession concern case. We feel the market had been discounting a soft landing, and the weak job numbers changed investor's opinions.

I can't claim to be a Yen carry trade expert. My best explanation is that people borrowed for years in Yen because interest rates in Japan were close to zero. They would invest that money in higher yielding markets. Japan recently raised rates, and their currency strengthened significantly. This forced investors to sell liquid assets (stocks) to meet margin calls.

A third reason for the market drawdown is nobody knows. Markets are volatile, and stuff like this happens. You can decide which is more accurate.

That said, our performance has been challenged by not owning the money losing names in our benchmarks. Over time, we believe this will even out. Companies can't stay in business without cashflow. We don't think rates are going back to zero, and the cost of financing will be prohibitive for these companies to survive longer term. In the near term, we continue to look for solid investments that correlate with the non-earners. We haven't found too many as of yet.

Earnings have, in general, been a little disappointing. As we work our way through earnings season, we are evaluating each miss from the perspective of macro vs. micro. If the economy is slowing, we need to be careful not to sell one disappointment just to buy another. We believe that if the Federal Reserve does cut rates, good, cyclical companies should be solid performers. We want to hold on to those issues. If it is a company-specific problem we will move on. Determining between the two is the grey area of our profession.

To provide the other half of the opening quote:

"But it ain't about how hard ya hit.

It's about how hard you can get hit and keep moving forward.

How much you can take and keep moving forward. That's how winning is done!"

Attribution:

Investors rotated out of technology stocks in July and shifted their focus to value stocks and small caps which could benefit from widely anticipated interest rates cuts. The Russell 2000 Value Index surged, up 12.2%, easily outpacing the S&P 500 (+1.1%) and the tech heavy Nasdaq (-0.8%). Value outperformed growth in all four of our benchmarks for the month of July. On a relative basis, we underperformed all our respective benchmarks for the month.

Composite Performance (%) as of December 31, 2023

	1 Year		5 Year		10 Year	
	Gross	Net	Gross	Net	Gross	Net
Small Cap Value	18.87%	17.69%	13.78%	12.65%	8.72%	7.64%
Small/Mid Cap Value	15.38%	14.23%	14.06%	12.92%	8.90%	7.81%
Mid Cap Value	13.51%	12.55%	13.49%	12.55%	9.40%	8.50%
Micro Cap Value	16.14%	14.99%	11.99%	10.87%	8.95%	7.86%

Returns for periods greater than one year are annualized. Returns reflect the reinvestment of dividends and other earnings and are expressed in U.S. dollars. Gross-of-fees returns for the representative account are presented before management and custodial fees but after all trading expenses.

If you would like more information about our firm and investment strategies, please contact:


Patrick Kennedy
Portfolio Specialist

E: pkennedy@integrityasset.com
T: 216.920.5281



Crystal D. Doyle
Director, Account Management

E: cdoyle@integrityasset.com
T: 216.898.2410

All investments carry a certain degree of risk including the possible loss of principal, and an investment should be made with an understanding of the risks involved with owning a particular security or asset class. Interested parties are strongly encouraged to seek advice from qualified tax and financial experts regarding the best options for your circumstances.

Each representative account serves as the model against which all accounts in each respective strategy are managed. The representative accounts are actual portfolios and the information provided, including performance, will vary for other accounts. The representative accounts are being used solely as tools to help demonstrate how performance can be attributed to the investment policies applied in the management of each strategy.

Net-of fees returns reflect gross performance less investment management fees, which are calculated by deducting 1/12 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 in Part 2A of its Form ADV.

*The Integrity Small-Cap Value Equity Strategy is benchmarked to the Russell 2000® Value Index. The Integrity Small/Mid-Cap Value Equity Strategy is benchmarked to the Russell 2500™ Value Index. The Integrity Mid-Cap Value Equity Strategy is benchmarked to the Russell Midcap® Value Index. The Integrity Micro-Cap Value Equity Strategy is benchmarked to the Russell Microcap® Value Index.

Index returns reflect the reinvestment of dividends and other income but do not reflect advisory fees or any other expenses. Indexes are unmanaged and one cannot invest directly in an index.

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