

Quarterly Commentary

*“It’s difficult to make predictions,
especially about the future.”*

– Yogi Berra

Over the holiday, I read the book *Same as Ever* by Morgan Housel. It was an excellent read. The overriding theme of the book is that short-term forecasts miss the surprises that move markets. However, there are behaviors and biases that never change and repeat throughout time. Understanding those behaviors can give you an advantage. With that in mind, I would like to share 10 of the book’s key points and relate them to how we think about money management.

1. We are good at predicting the future, except for surprises, and it’s the surprises that matter. No one saw Pearl Harbor, 9/11, or the COVID lockdowns.
2. Some things never change. People will always cycle between fear and greed, pessimism and optimism.
3. Calm plants the seeds of crazy. Economic stability leads to optimism. Optimism leads to taking on debt. Debt leads to instability.
4. The world breaks every 10 years or so. In between, there will always be disasters. In a world of 8 billion people, all connected by technology, something terrible happens every day. If there are over 100 possible once-in-a-hundred-year events that can happen in a year, the odds of one happening are pretty good. Crazy, therefore, is normal.
5. The best story wins. Every market valuation is just a number today multiplied by a story about tomorrow.
6. Good news takes time; bad news occurs instantly. Things are created step-by-step and piece-by-piece but can be broken or destroyed by one event.
7. Compounding is powerful. Don’t ask, “what is the highest return I can achieve?” Ask, “what’s the highest level of return I can sustain for the longest period of time?” Concentration maximizes return. Diversification increases the odds of owning a winner.
8. Everything dies. Competitive advantage doesn’t last forever. Almost 40% of public companies lost ALL their value between 1980 and 2014!
9. It’s better to be approximately right than exactly wrong. There are typically a handful of simple variables that drive most outcomes. Too much focus on precision loses the big picture, where you have a higher chance of being correct.
10. We can say we are in it for the long run. We must remember that the long run is full of short-term disasters.

For the last 20+ years, Integrity has wrestled with a lot of these concepts. We know nothing lasts forever. Our valuation models incorporate competitive advantage decay. We believe diversification at the sector and characteristic level increases our chances of sustaining consistent returns over time. Our Flexible Value philosophy of investing is built on the knowledge that markets cycle between fear and greed, and always will. We believe by being cognizant of that cycle, we can better position the portfolio to benefit from these changes. Our simple goal is to provide consistent returns for our clients, control risk, and take advantage of changes in

Quarterly Commentary

market psychology, where appropriate. So, what will the market do this year: volatility and some surprises along the way. That's the forecast. We will be monitoring, as usual, for what we see as the best risk/reward opportunities for our clients and trying to take advantage of them.

Utilities and financials were the top performing sectors in the benchmark. Energy was the worst performing sector in the benchmark. Micro cap value outperformed micro cap growth.

The Victory Integrity Discovery Fund (A shares without sales charge) outperformed its benchmark, the Russell Microcap[®] Value Index. Stock selection in industrials and consumer discretionary were the key positives driving outperformance. Financials were a minor contributor. Stock selection in energy and technology detracted. Sector weights were a negative due to a large underweight to biotechs, which outperformed. A larger market cap was a style headwind, as the smallest companies outperformed.

Industrial performance was sparked by three acquisitions. Hawaiian Holdings, Inc. (HA) accepted a significant premium to be acquired. SP Plus Corporation (SP) agreed to be taken private for a premium. Eagle Bulk Shipping Inc. (EGLE) also accepted an offer to be acquired. BlueLinx Holdings (BXC), a distributor of building products, outperformed as interest rates declined. Matrix Service Company (MTRX) detracted. Although it had strong backlog and project awards, this was offset by weaker gross margins which drove an operating loss.

A pair of restaurants in BJ's Restaurants, Inc. (BJRI) and Red Robin Gourmet Burgers, Inc. (RRGB) led the way in consumer discretionary. Positive QTD commentary as well as an upbeat analyst day, highlighting the margin and unit growth opportunity, boosted BJ's Restaurants, Inc. (BJRI). Red Robin Gourmet Burgers, Inc. (RRGB) showed signs of progress on their turnaround. Lindblad Expeditions Holdings, Inc. (LIND) and Hibbett Inc. (HIBB) also helped. Better-than-expected earnings as well as an extension and expansion of the strategic relationship with National Geographic lifted Lindblad Expeditions Holdings, Inc. (LIND) shares. Hibbett Inc. (HIBB) posted a beat-and-raise quarter, driven by a strong back-to-school season and a positive response to new products. Inspired Entertainment, Inc. (INSE) was the largest detractor. It reported their auditor had identified accounting errors related to capitalized software development costs and that the Q3 earnings report would also be delayed. We exited the position.

Stock selection in banks and insurance were the main positives in financials. Our average bank holding was up 30%, besting the 26.2% return in the benchmark. Primis Financial Corp. (FRST) rallied 57% thanks to solid results and improved guidance as expense and funding initiatives take hold. Improved profitability and expectations for better growth aided performance at HCI Group (HCI) within insurance. There was some minor underperformance in capital markets and consumer finance as our more defensive holdings lagged.

Energy was the weakest area of performance. ProPetro Holding Corp. (PUMP) expects a sequential decline in 4Q23 fleet utilization and deployment of a new eFleet could be dilutive in the short term. Results at Solaris Oilfield Infrastructure, Inc. Class A (SOI) were below expectations, driven by lower service activity and higher maintenance costs. Vital Energy, Inc. (VTLE) underperformed as oil prices retreated on weaker demand and higher domestic production. Talos Energy, Inc. (TALO) missed production guidance during the third quarter and expects a sequential decline in production in the fourth quarter as well.

Within technology, we missed owning some of the best-performing software companies. SkyWater Technology Inc. (SKYT) was a notable outperformer. It delivered solid results driven by increasing demand and strong execution.

A larger underweight to biotechs, which outperformed, hurt performance in health care. It cost us 107 basis points. Brookdale Senior Living Inc. (BKD) gained 41% due to strong results driven by occupancy improvement, higher rates, and continued improvement in agency labor. It raised guidance for the fourth quarter also. Collegium Pharmaceutical, Inc. (COLL) renegotiated contract pricing for its two pain therapies, which is expected to drive prescription and product sales growth.

Communication services was breakeven. We avoided some of the worst media stocks. This was offset by Marcus Corporation (MCS) and IMAX Corporation (IMAX). They both lagged on concerns about the impact of the writers and actors strikes on 2024's film slate.



Quarterly Commentary

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All investing involves risk, including the potential loss of principal. In addition to the normal risks associated with investing, micro-cap companies may have narrower markets and be difficult to buy and sell. Micro-cap companies may have limited products or resources and may experience higher failure rates than larger, more seasoned companies. 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. The financial services industry is subject to extensive government regulation that affects the scope of their activities, the prices they can charge and capital maintenance. The industry is subject to severe competition and can be significantly affected by market conditions and activity. 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 Microcap® Value Index is a market- capitalization-weighted index that measures the performance of Russell Microcap® Index companies (1,000 smallest stocks in the Russell 2000® Index plus 1,000 smaller U.S.-based listed stocks) with relatively lower price-to-book ratios and lower forecasted growth values. It represents the value-oriented micro-cap segment of the U.S. equity market.

Fund holdings mentioned in the Quarterly Commentary are as of 12/31/2023 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 12/31/2023 were Brookdale Senior Living Inc (1.6%), RadNet, Inc (1.4%), Columbus McKinnon Corp (1.2%), Ichor Holdings, Ltd (1.2%), NETSTREIT Corp (1.2%), Clear Channel Outdoor Holdings Inc (1.1%), Chuy's Holdings, Inc (1.1%), Enviri Corp (1.1%), Dime Community Bancshares, Inc (1.1%), and Modine Manufacturing Co (1.4%). 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.

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