VICTORY HIGH INCOME STRATEGY QUARTERLY COMMENTARY

VICTORY income investors
A VICTORY CAPITAL® INVESTMENT FRANCHISE

As of December 31, 2023

Executive Summary

Fixed income concluded 2023 with a bang! Fourth quarter inflation reports trended lower, and as the Federal Reserve (the Fed) kept rates stable the market regained confidence after a frustrating third quarter. Positive performance was driven by a downward swing in the Treasury curve, pushing yields down. Against this backdrop, the Victory High Income Strategy underperformed its benchmark, the Bloomberg U.S. High Yield 2% Issuer Capped Bond Index, for the quarter ended December 31, 2023.

Market Update & Commentary

Shifts in monetary policy expectations defined the fourth quarter of 2023, leading to a sense of optimism going into 2024. Unemployment slid to 3.7%, and the Consumer Confidence Index rose in December to highs not seen since 2021. All these factors, taken together, fostered greater investor confidence in a soft-landing narrative.

The Consumer Price Index, a popular measure of prices paid (and, thus, inflation), declined to 3.1% from 3.7% during the fourth quarter, indicating that the Fed continues to inch toward its target of 2% inflation. As a result of moderating inflation and a resilient economy, the Fed held rates steady during its meetings during the quarter. These factors led to positive returns within the fixed income market, with November turning out to be the best month for bonds since the 1980s. The remarkable returns can largely be attributed to the downward shift seen in Treasury yields from the 10-year Treasury's peak of 5% in October. This historic rally continued through December and was sufficient to swing fixed income's performance for the full calendar year to the black for the first time since 2020. While the dramatic shifts along the yield curve observed during the fourth quarter might give investors pause when considering fixed income, current yields still present a historically attractive opportunity, even if not at October's high of 5%.

Market expectations for rate cuts in 2024 steadily increased throughout 4Q23 on the Fed's decision to pause and a belief that the hiking cycle has reached completion. Many market participants believe rate cuts are coming soon, and this confidence was an important factor in the positive momentum that drove fixed income and equities higher. At the beginning of the quarter the market priced in two to three 25-bps cuts in 2024, but the quarter ended with interest rate traders pricing federal funds futures for nearly seven cuts. Victory Income Investors, though, believes that the Fed remains data dependent, as it was reiterated at the December Federal Open Market Committee meeting that future monetary policy decisions will hinge on seeing "further evidence to build confidence that inflation is moving down sustainably." Chairman Powell also emphasized the Committee's meeting-by-meeting decision process in his reminder that should economic circumstances change, keeping rates higher for longer is not off the table entirely.

	Yield (%)	Spreads (bps)			Returns (%)	
		12/31/2023	9/30/2023	Δ (+/-)	3M	1YR
Investment Grade (Moody's Ratings)						
U.S. Treasury	4.1	-	-	-	5.7	4.1
U.S. Aggregate	4.5	42	52	-10	6.8	5.5
U.S. Credit	5.0	93	111	-19	8.2	8.2
Corporate	5.1	98	120	-22	8.5	8.5
Aa	4.6	47	57	-10	8.3	7.0
A	4.9	84	105	-20	8.2	7.7
Baa	5.3	121	146	-25	8.8	9.5
Crossover	6.0	183	235	-52	8.0	11.2
High Yield (Moody's Ratings)						
U.S. Corporate High Yield	7.8	323	395	-72	7.2	13.4
Ba	6.4	201	265	-64	7.4	11.6
B	7.7	317	396	-79	7.0	13.8
Caa	12.6	751	846	-94	6.9	19.8
Ca-D	19.5	1,173	1,145	-271	5.1	16.4
Structured Product						
U.S. MBS	4.7	46	66	-20	7.5	5.0
ABS	5.0	68	66	+2	3.5	5.5
CMBS	5.3	126	131	-5	5.2	5.4

Source: Bloomberg

Credit spreads tightened across fixed income asset classes apart from asset-backed securities (ABS) in the fourth quarter. Tighter credit spreads indicate lower compensation for taking on additional risk. Fixed income outperformed in the fourth quarter, driven by a falling yield curve. The decline was sufficient to swing full-year returns in the Bloomberg U.S. Aggregate Bond Index to +5.5% when the index had concluded the first nine months of 2023 at -2.1%.

Portfolio Performance & Positioning

During the quarter, we increased our allocation to cash and decreased our allocation to the following sectors: cable & satellite, technology, leisure, and midstream. At the same time, we increased our holdings in media and some select retailers. We reduced our holdings in lower-rated CCC and low-B credits.

Contributors

- Best-performing sectors were banking, media & entertainment, and wirelines.
- From a credit perspective, our security selection within B-rated credits aided performance.
- Security selection within index-eligible names added the majority to performance.

Detractors

- Sectors that detracted from performance were out-of-index sectors such as senior secured bank loans, CLOs, and short-dated structured products.
- From a credit perspective, BB-rated credits detracted from performance, largely based on changes to the yield curve.
- Our cash holdings detracted from performance.

Performance

Average Annual Returns (%) as of December 31, 2023

Victory High Income Strategy	QTD	YTD	1-YR	3-YR	5-YR	10-YR	Since Inception (September 1999)
Gross of Fees	6.84	13.96	13.96	2.86	5.35	4.56	6.94
Net of Fees	6.62	13.06	13.06	2.07	4.53	3.71	6.01
Bloomberg U.S. High Yield 2% Issuer Capped Bond Index	7.15	13.44	13.44	1.98	5.35	4.59	–

Past performance cannot guarantee future results. Returns for periods greater than one year are annualized. Returns are expressed in U.S. dollars and reflect the reinvestment of dividends and other earnings. Composite and benchmark returns are presented net of non-reclaimable withholding taxes, if any. Gross-of-fees returns are presented before management and custodial fees but after all trading expenses. Net-of-fees returns reflect gross performance less investment management fees. Net-of-fees returns 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 on Part 2A of its Form ADV.

VictoryFunds®

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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.

The Victory High Income Composite includes all institutional and retail portfolios invested in a broad range of U.S. dollar-denominated high-yield securities, including bonds (often referred to as “junk” bonds), convertible securities, leveraged loans, or preferred stocks, with an emphasis on non-investment-grade debt securities. Although the composite will invest primarily in U.S. securities, it may invest without limit in dollar-denominated foreign securities and to a limited extent in non-dollar-denominated foreign securities, including in each case emerging-markets securities. The strategy aims to deliver a total return primarily through a yield-focused portfolio that offers a high level of current income. High yield bonds carry increased levels of credit and default risk and are less liquid than government and investment grade bonds. Portfolios in the composite have a target average maturity of 5-10 years. The composite creation date is July 2019 and the composite inception date is September 1999. The benchmark of the composite is the Bloomberg U.S. High Yield 2% Issuer Capped Bond Index. Prior to 4/24/2023, the name of this composite was the USAA High Income Fixed Income Composite.

The benchmark of the composite is the **Bloomberg U.S. High Yield 2% Issuer Capped Bond Index**. The Bloomberg U.S. High Yield 2% Issuer Capped Bond Index is an index comprised of fixed rate, non-investment-grade debt securities that are dollar denominated and nonconvertible. The index limits the maximum exposure to any one issuer to 2%.

Index returns are provided to represent the investment environment during the periods shown. Index performance does not reflect management fees, transaction costs or expenses that would be incurred with an investment. One cannot invest directly in an index. **Past performance does not guarantee future results.**

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.

Victory Capital Management Inc. (VCM) is a diversified global investment advisor registered under the Investment Advisers Act of 1940 and comprised of multiple investment franchises: Integrity Asset Management, Munder Capital Management, NewBridge Asset Management, RS Investments, Sophus Capital, Sycamore Capital, Trivalent Investments, Victory Income Investors (formerly USAA Investments, a Victory Capital Investment Franchise); the VictoryShares & Solutions Platform, THB Asset Management and New Energy Capital Partners. Munder Capital Management and Integrity Asset Management became part of the Victory Capital GIPS firm effective November 1, 2014; RS Investments and Sophus Capital effective January 1, 2017; Victory Income Investors, effective July 1, 2019; THB Asset Management, effective March 1, 2021, and New Energy Capital effective November 1, 2021. Effective September 1, 2023, INCORE Capital Management is no longer part of the firm definition.

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Victory Capital claims compliance with the Global Investment Performance Standards (GIPS®).

The opinions are as of the date indicated and are subject to change at any time due to changes in market or economic conditions. The comments should not be construed as a recommendation of individual holdings or market sectors, but as an illustration of broader themes.

Advisory services offered by Victory Capital Management Inc., an SEC-registered investment adviser, 15935 La Cantera Parkway, San Antonio, TX 78256.

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