

Victory Trivalent Emerging Markets Small-Cap Fund Quarterly Commentary



As of September 30, 2020

Market Environment

Despite the ongoing pandemic, emerging markets small-cap equities posted another quarter of double-digit positive returns as investors' appetite for riskier assets remained in good health. For the quarter, the MSCI Emerging Markets Small Cap Index (Net) rose 11.9%. The Victory Trivalent Emerging Markets Small-Cap Fund (Class A, without load) had a strong quarter, outperforming the index by a solid margin. Regionally, Asia (+14.0%) outperformed Europe, Middle East and Africa (+9.2%) and Latin America (+1.5%). Not surprisingly, there was a wide dispersion among country returns. Malaysia returned 28.2% and was the best performing country. Malaysia is home to several of the world's largest latex glove manufacturers, which have seen their share prices soar on an exponential increase in demand due to the Covid-19 outbreak. India rose 21.7% as lockdown restrictions were eased in June and an economic stimulus plan to support small businesses was implemented. Korea small-caps returned 24.2% as President Moon more than doubled his "New Deal" spending plan designed to create over 2 million jobs. Argentina fell 14.0% and was the worst performing country, as government officials work to restructure sovereign debt and elevated infection rates in Buenos Aires have resulted in extreme lockdown measures that have impeded economic activity. China returned 10.8%, slightly below the overall market, as investors balanced a gradual economic recovery with geopolitical tensions with the U.S. over technology, trade, and national security.

Ten of the eleven economic sectors posted positive returns. Health Care rose 30.4% and was the best performing sector, as equipment and services providers that have seen a significant increase in demand for Covid-19 related products continued to outperform. Communication Services stocks rose 13.0% on higher demand for bandwidth and cloud services that support remote working environments. The traditionally defensive Real Estate and Utility stocks were relative underperformers, up 0.2% and down 0.5%, respectively.

Portfolio Review

Overall security selection was positive and accounted for most of the Fund's outperformance. The Fund also benefited from a slight overweight to Health Care and underweight to Real Estate. Excess returns were generated in two of three regions and five of the eleven economic sectors. Stock selection was particularly strong in Health Care, Financials, and Information Technology. Within Health Care, Korean diagnostic and screening product manufacturer Seegene returned 137.4% and was the top contributor for the quarter. Demand for Seegene's Covid-19 test kits continues to exceed expectations, and investors anticipate a second wave of infections. Another strong performer in Health Care was Malaysian latex glove manufacturer Supermax, which rose 117.1% as global demand for latex and nitrile gloves surged and average selling prices rose. Within Information Technology, V.S. Industry, a Malaysian provider of electronic manufacturing services, rose 141.3% on the resumption of activity after the country's Movement Control Order was lifted. In addition to securing two new clients during the quarter, the company is also seen as an alternative Asian manufacturing site given soured U.S.-China relations. Unimicron, a Taiwanese manufacturer of printed circuit boards, rose 53.8% on strong demand and pricing for its circuit-insulating film substrate called ABF. Performance in Financials got a boost from Multi Commodity Exchange of India, which advanced 39.9% following a surge in gold and silver bullion trading.

On the downside, the Fund trailed the benchmark in Communication Services and Industrials. Communication Services holding NetDragon Websoft declined 21.7%. The online gaming and education provider suffered larger than expected losses in its education segment due to higher staff salaries and hosting costs, while active users soared due to school closures. Performance in Consumer Discretionary was dragged down by Turkish industrial conglomerate Tekfen. Tekfen's share price dipped 20.6% as second quarter results reflected a challenging environment for their engineering and fertilizer businesses.

From a style perspective, the Fund's exposure to high-quality companies with improving business momentum trading at attractive valuations contributed to relative performance. Business momentum was the strongest factor, while value remains challenged in the current environment as the winners continue to trade at lofty valuations.

Market Outlook

A sustained economic recovery will remain challenging until a vaccine becomes widely accessible. Infection rates will continue to be closely monitored, and signs of a significant second wave of infections that could reinstate restrictions could bring market volatility with it. Economies and sectors with a higher dependence on travel and tourism will likely remain laggards in the near term. While uncertainty about the pandemic remains, central banks have eased rates aggressively, and domestic and regional trade has increased. In several emerging markets, manufacturers have increased output as restrictive measures have been alleviated and demand has rebounded. Export-dependent economies have seen an increase in trade following several months of contraction and business confidence has improved. Growth in employment has been measured as companies adhere to social distancing guidelines. When a vaccine becomes available, a more substantial increase in employment is likely to follow and potentially provide upside to markets. Flexible companies focused on digital strategies will have advantages over companies with more ingrained traditional business practices. Opportunities for relative outperformance remain, particularly among the diverse and broad segment of emerging market small-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.

Top 5 Contributors* (%)	Return	Contribution to Relative Return
Seegene, Inc.	137.4	2.5
Supermax Corp. Bhd.	117.1	2.3
Granules India Limited	94.1	1.2
V.S. Industry Bhd.	141.3	0.7
NHN KCP Corp.	42.8	0.5

Top 5 Detractors* (%)	Return	Contribution to Relative Return
Taidoc Technology Corporation	-23.8	-0.4
MRV Engenharia e Participacoes S.A.	-16.1	-0.1
YiChang HEC ChangJiang Pharmaceutical Co. Ltd. Class H	-27.0	-0.1
Asmedia Technology Inc.	-20.2	-0.1
NetDragon Websoft Holdings Limited	-21.7	-0.1

Source: FactSet.

Top 10 Holdings	Country	Sector
Seegene, Inc.	Korea	Health Care
Granules India Limited	India	Health Care
Supermax Corp. Bhd.	Malaysia	Health Care
NHN KCP Corp.	Korea	Information Technology
Ipca Laboratories Limited	India	Health Care
SINBON Electronics Co., Ltd.	Taiwan	Information Technology
ELAN Microelectronics Corp.	Taiwan	Information Technology
Unimicron Technology Corp.	Taiwan	Information Technology
Merida Industry Co., Ltd.	Taiwan	Consumer Discretionary
V.S. Industry Bhd.	Malaysia	Information Technology
Total % of Portfolio		15.47%

Investment Performance (%)	QTR	YTD	1-YR	ANNUALIZED RETURNS				EXPENSE RATIO	
				3-YR	5-YR	10-YR	Since Inception 7.2.13	Gross	Net
Class A, without load	12.78	10.70	21.14	3.11	9.03	—	5.99	2.74%	1.75%
Class A, with max. sales load (5.75%)	6.26	4.33	14.19	1.08	7.74	—	5.12	2.74%	1.75%
Class Y	12.94	10.86	21.46	3.37	9.31	—	6.25	2.24%	1.50%
MSCI Emerging Markets Small Cap Index (Net)	11.85	-2.40	6.89	-1.09	4.60	1.03	—		

Source: Zephyr StyleADVISOR.

Past performance does not guarantee future results. The performance data quoted represents past performance, and current returns may be lower or higher. The investment return and principal will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. To obtain performance information current to the most recent month end, please visit www.vcm.com. Fee waivers were in place for all or some of the periods shown, without which performance would have been lower.

Net expense ratios reflect the waiver, reimbursement or recoupment, as applicable, contractually agreed to through October 31, 2020.

Returns include reinvestment of dividends and capital gains. Not all share classes are available to all investors. Please read the prospectus for details.

Risks Associated with Investing in the Fund: All investing involves risk, including potential loss of principal. Investors should note that investments in foreign securities involve additional risks due to currency fluctuations, economic and political conditions, and differences in financial reporting standards. There are greater risks involved in investing in emerging market countries than those associated with investment in developed foreign markets. Smaller company stocks are more volatile and less liquid than larger, more established company securities. A substantial portion of the Fund's assets may be invested in securities issued in a small number of countries; therefore, adverse market conditions impacting those countries may have a more pronounced effect on the Fund.

Index Defined: The MSCI Emerging Markets Small Cap Index is a free float-adjusted, market-capitalization-weighted index that measures the performance of small-cap stocks in 26 emerging markets. A fund's portfolio differs significantly from the securities held in an index. An index is unmanaged and not available for direct investment.

Fund holdings are as of the most recent quarter end, 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. Top holdings do not reflect cash, money market instruments, or options/futures contracts holdings. The most current 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. Percentages shown are for the most recent quarter.

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An investor should consider the Fund's investment objectives, risks, and charges and expenses carefully before investing or sending money. This and other important information about the investment company can be found in the Fund's prospectus. To obtain a prospectus, please call 1-800-539-FUND or visit www.victoryfunds.com. Please read the prospectus carefully before investing.

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