VICTORY ULTRA SHORT-TERM FIXED INCOME STRATEGY QUARTERLY COMMENTARY

VICTORY income investors®
A VICTORY CAPITAL® INVESTMENT FRANCHISE

As of September 30, 2024

Executive Summary

While markets can finally move on from forecasting the first rate cut, the Federal Reserve (Fed) continued to be in the limelight in the third quarter of 2024. Inflation trended lower throughout the quarter, and the Fed placed additional focus on the second arm of its dual mandate, the labor market. Yields dropped as markets priced in anywhere from one to six cuts through the end of 2024. While rate cut expectations persistently shifted, fixed income performance was positive across all major fixed income markets. Against this backdrop, the Victory Ultra Short-Term Fixed Income Strategy outperformed its benchmark, the Bloomberg U.S. Treasury Bellwethers 3-Month Index, for the quarter ended September 30, 2024, on a gross and net basis.

Market Update & Commentary

The third quarter of 2024 can be characterized by markets focused on the Fed, the labor market, and inflation. Throughout the quarter markets were consistently fixated on the timing of the first rate cut, with some expecting a cut in July based on labor market weakening and lower inflation. Market forecasts for a reduction in interest rates drove Treasury yields down throughout the quarter. The highly prophesied rate cut finally arrived in mid-September. The Fed chose to cut by 50 basis points following a steady decline in inflation and a slowing in job gains. This decision was further supported by unemployment numbers increasing somewhat throughout the quarter but ending at 4.2%. While slightly elevated, unemployment remained low on a historical basis.

Election year political developments, uncertainty in monetary policy, and conflicting consumer sentiment raised market volatility. The hesitation many investors felt on the efficacy of bonds as ballast through equity market downturns was alleviated in August as the negative correlation between bonds and equities once again materialized. The Consumer Price Index (CPI), a popular measure of prices paid, and thus, inflation, decreased throughout the quarter but concluded September at 3.3%, the same as Q2 2024 (Core CPI YoY). While the Fed started easing monetary policy in Q3 2024, there was some dissonance in economic reporting. Taking the higher-than-expected September CPI and the stronger-than-expected September jobs report as examples, this indicates to us that the accelerated pace many expect the Fed to take to normalize interest rates may not shake out as forecasted. Regardless, in our view, forecasting interest rates is not a particularly reliable method of generating excess returns.

	Yield (%)	Spreads (bps)			Returns (%)	
		9/30/2024	6/30/2024	Δ (+/-)	3M	1YR
Investment Grade (Moody's Ratings)						
U.S. Treasury	3.8	-	-	-	4.7	9.7
U.S. Aggregate	4.2	36	39	-3	5.2	11.6
U.S. Credit	4.7	84	88	-4	5.7	13.8
Corporate	4.7	88	93	-5	5.8	14.3
Aa	4.4	46	51	-5	6.1	13.0
A	4.6	73	80	-7	5.9	13.7
Baa	4.9	110	113	-3	5.8	15.0
Crossover	5.6	165	154	+11	4.4	14.8
High Yield (Moody's Ratings)						
U.S. Corporate High Yield	7.2	300	311	-11	5.3	15.7
Ba	6.0	180	177	+3	4.3	14.7
B	7.3	281	279	+2	4.5	14.5
Caa	10.7	689	795	-106	10.2	20.3
Ca-D	24.0	1,610	1,757	-147	22.4	52.5
Structured Product						
U.S. MBS	4.5	42	48	-6	5.5	12.3
ABS	4.4	63	56	+7	3.4	8.7
CMBS	4.6	94	97	-3	4.7	11.8

Source: Bloomberg

Investor compensation for adding credit risk remains low – credit spreads tightened throughout the quarter in response to a stable economic backdrop and lower inflation reports. Fixed income yields dropped, which drove positive performance across asset classes, with credit sectors being the top performers YTD. The Bloomberg U.S. Aggregate Bond Index concluded the quarter at +5.2%.

Portfolio Performance & Positioning

During the quarter, we increased our allocation to corporate bonds, asset-backed securities (ABS), and mortgage-backed securities (MBS), while reducing exposure to commercial mortgage-backed securities (CMBS), cash, bank loans, and government-related securities.

Contributors

- Best performers were in CMBS, Treasuries, MBS, and ABS.
- Asset allocation added to performance.
- From a credit rating perspective, BB-rated and A-rated bonds performed the best.
- Duration added to performance.

Detractors

- Sectors that detracted from performance included other ABS, pharmaceuticals, brokerage and asset managers, and office REITs (real estate investment trusts).
- From a credit rating perspective, while AAA-rated bonds performed the worst, they did have a positive return.

Performance

Average Annual Returns (%) as of September 30, 2024

Victory Ultra Short-Term Fixed Income Strategy	QTD	YTD	1-YR	3-YR	5-YR	10-YR	Since Inception (November 2010)
Gross of Fees	2.12	5.59	7.99	4.14	3.66	2.95	2.77
Net of Fees	1.97	5.13	7.37	3.52	3.05	2.34	2.17
Bloomberg U.S. Treasury Bellwethers 3-Month Index	1.38	4.06	5.51	3.57	2.37	1.68	–

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.

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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 Ultra Short-Term Fixed Income Composite includes all institutional and retail portfolios invested primarily in a broad range of debt securities that have a dollar-weighted average portfolio maturity of 18 months or less. The debt securities in which the composite portfolio may invest include, among others, obligations of U.S., state, and local governments, their agencies and instrumentalities; mortgage- and asset-backed securities; corporate debt securities; repurchase agreements; and other securities believed to have debt-like characteristics. The strategy aims to deliver high current income with preservation of principal. Portfolios in the composite will invest primarily in investment-grade securities, but also may invest in below investment-grade securities, which are sometimes referred to as high-yield or “junk” bonds. High yield bonds carry increased levels of credit and default risk and are less liquid than government and investment grade bonds. Beginning September 1st, 2023, the minimum account size for the composite is $25 Million. The composite creation date is July 2019, and the composite inception date is November 2010. The benchmark of the composite is the Bloomberg U.S. Treasury Bellwethers 3 Month Index. Prior to 5/1/2021, the benchmark of this composite was the FTSE 3 Month T Bill Index. Prior to 4/24/2023, the name of this composite was the USAA Ultra Short-Term Bond Fixed Income Composite.

The benchmark of the composite is the **Bloomberg U.S. Treasury Bellwethers: 3 Month Index.** The index measures the performance of Treasury bills with a maturity of less than three months. The benchmark returns are provided to represent the investment environment existing during the time periods shown and are not covered by the report of independent verifiers. For comparison purposes, the index is fully invested, which includes the reinvestment of income. The returns have been taken from a published source and do not include any transaction fees, management fees, or other costs. Prior to 5/1/2021, the benchmark of this composite was the FTSE 3 Month T Bill Index.

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 adviser registered under the Investment Advisers Act of 1940 and comprises multiple investment franchises: Integrity Asset Management, Munder Capital Management, New Energy Capital Partners, NewBridge Asset Management, RS Investments, Sophus Capital, Sycamore Capital, THB Asset Management, Trivalent Investments, Victory Income Investors (formerly USAA Investments, a Victory Capital Investment Franchise), and the VictoryShares & Solutions Platform. Munder Capital Management and Integrity Asset Management became part of the VCM 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 VCM GIPS firm.

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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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