

THB US Micro Cap Fund

Quarterly Report – Q2 2024

Market commentary

The Russell Microcap® Index (the “Index”) returned -7.5% in AUD in Q2 2024.

Consumer Staples (+6.24%) was the best performing sector, followed by Financials (+0.21%) and Energy (-0.78%). Health Care (-10.95%) performed the worst, followed by Information Technology (-9.16%) and Communication Services (-8.57%).

U.S. equities delivered mixed performance during the quarter as elements of bifurcation and concentration with the indices accelerated. A narrow group of mostly mega cap technology companies delivered outsized relative performance as the ‘Magnificent 7’ was up 16.92% which enabled the S&P 500® to post a positive return of 4.28% for the quarter.

Large caps far outpaced lower capitalisation equities as the Russell Mid Cap® returned -3.35% and Russell 2000® returned -3.28%. Higher-than-anticipated inflation and employment data led market participants to dial back the timing and number of rate cuts expected this year.

In April, bond yields soared higher (reaching the highest levels of the year) due to stronger-than-expected economic data but have since settled back to levels experienced in March. The pivot from the current tightening cycle to a more accommodative monetary policy is widely anticipated, but the timing of such appears to hinge on each economic data point which is creating volatility in equity markets.

Fund details	
Benchmark	Russell Microcap® Index ³
Inception date	5 September 2014
Fund size	A\$83 million

Fund performance ¹			
	Fund ²	Russell Microcap®	Difference
1 month	(3.9%)	(2.7%)	(1.2%)
3 months	(8.0%)	(7.5%)	(0.6%)
1 year	2.7%	5.6%	(2.9%)
2 years p.a.	11.1%	7.9%	3.3%
3 years p.a.	(1.2%)	(4.2%)	3.0%
5 years p.a.	7.9%	6.6%	1.3%
Since inception p.a. ²	10.2%	9.6%	0.6%

1. Performance figures are presented in AUD on a net, pre-tax basis and assume the reinvestment of distributions. Past performance is not an indicator of future performance. Figures in the table may not sum correctly due to rounding.

2. Fund inception date was 5 September 2014 however inception performance is calculated from 1 October 2014.

Composite performance ³			
	Composite (Net)	Russell Microcap ⁴	S&P500
1 month	(3.5%)	(2.3%)	3.6%
3 months	(5.9%)	(5.3%)	4.3%
1 year	3.4%	6.0%	24.6%
3 years p.a.	(4.4%)	(7.8%)	10.0%
5 years p.a.	7.6%	5.5%	15.0%
10 years p.a.	6.6%	5.5%	12.9%
Inception p.a.	11.5%	6.2%	8.4%

3. Returns in USD; the THB Micro Cap Composite contains fully discretionary micro cap equity accounts. THB claims compliance with the Global Investment Performance Standards (GIPS). The minimum account size for this composite is US\$1 million. Performance is shown net of 1.25% p.a. management fees and assumes the reinvestment of income.

4. Since inception return is the Russell 2000 Index from June 1998 to December 2006, and Russell Microcap Index thereafter. The Russell Microcap Index is a capitalisation weighted index of 2,000 stocks that captures the smallest 1,000 companies in the Russell 2000 and 1,000 smaller US based listed stocks.

Portfolio commentary

The THB US Micro Cap Fund returned -8.0% in AUD (net of fees) in Q2 2024.

The portfolio saw positive contribution from stock selection in Health Care (+3.11%) and Information Technology (+0.73%) as well as underallocation to Real Estate (+0.69%). Negative contribution came mainly from stock selection in Consumer Discretionary (-0.99%), Industrials (-0.89%), and Real Estate (-0.84%).

The portfolio's top five performing stocks (from a contribution standpoint) were Vital Farms, Inc. (Consumer Staples, +0.77%), Limbach Holdings, Inc. (Industrials, +0.54%), Immersion Corporation (Information Technology, +0.45%), LeMaitre Vascular, Inc. (Health Care, +0.44%), and Blue Bird Corporation (+0.37%).

The bottom five performing stocks (from a contribution standpoint) were Beyond, Inc. (Consumer Discretionary, -1.19%), Latham Group, Inc. (Consumer Discretionary, -0.45%), RPC, Inc. (Energy, -0.40%), Cerence, Inc. (Information Technology, -0.39%), and Allient, Inc. (Industrials, -0.39%).

During the quarter, THB's portfolio companies announced 17 acquisitions and 7 stock repurchase authorisations.

One portfolio holding to highlight this quarter is Daktronics. Daktronics designs and manufactures electronic scoreboards and large screen video boards for commercial purposes. The company has a leading market share of 50% in LED displays in the United States.

Its ability to provide full-service design, manufacturing and installation solutions later translates in recurring maintenance revenue and long-term customer relationships. Sales of newer optic technologies and backend enhancements as older signage is replaced every 7-10 years is driving organic growth. Demand for its products is also supported by a strong investment cycle in live entertainment and sports as well as the transportation market and shift to electronic billboards.

The business profitability has improved to a new baseline in FY2024 and is expected to continue to increase from current levels driven by improved manufacturing efficiencies, and strong on-time delivery to customer sites resulting in higher gross and operating margins.

Outlook

THB remains positive on equities and the overall U.S. economy but remain watchful of negative elements which could be amplified by the upcoming presidential election. Risks such as inflation, government debt levels, interest rates and geopolitics as well as a change in administration and/or policies could ignite one or more of these preexisting conditions.

Many favorable elements for the U.S. economy exist and support our positive outlook, such as slowing inflation, solid consumer balance sheets, tight labour markets, onshoring, and overall strong financial system conditions. Moderating inflation likely gives the U.S. Federal Reserve enough evidence to begin cutting rates sometime this year. Additionally, artificial intelligence (AI) holds tremendous promise and could lead to sizable productivity gains within the U.S. economy. Beyond productivity, AI has also started broadening out across the economy as implementing this new technology requires sizeable capital spending in multiple industries.

Valuations (beyond the handful of concentrated mega-cap companies driving recent index performance) are reasonable, with small- and mid-caps near multi-decade relative (to large-cap) lows. Even the anointed mega-caps that are driving the indices are profitable. This is a clear point of differentiation versus the technology bubble of the late 1990s. One could debate what multiple is appropriate for these companies, but they are largely profitable and generating positive cash flows.

THB believes the combination of attractive valuations, more accommodative monetary policy, increasing productivity, and possible regulatory reforms provides a positive environment for forward small- and mid-cap returns.

Portfolio statistics⁵

	Fund	Russell Microcap®
Weighted avg market cap	US\$1,298m	US\$941m
Price/sales	1.1x	1.2x
Price/book	2.0x	1.6x
Dividend yield	1.1%	1.4%
Number of securities	93	1,446
Standard deviation	21.8%	21.9%
Sharpe ratio	0.4	0.3
Beta	1.0	
Tracking error	6.5	
Information ratio	0.3	

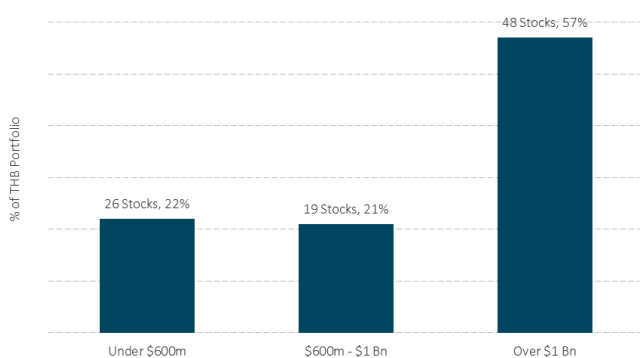
5. Portfolio statistics are reported in USD. Source: THB Asset Management

Top 10 holdings

Stock	Sector	Portfolio weight
UFP Technologies, Inc.	Health Care	2.9%
Transcat, Inc.	Industrials	2.6%
Immersion Corporation	Technology	2.4%
Hawkins, Inc.	Materials	2.4%
ePlus inc.	Technology	2.4%
Limbach Holdings, Inc.	Industrials	2.1%
BrightSphere Investment Group, Inc.	Financials	2.0%
First Busey Corporation	Financials	1.8%
Vericel Corporation	Health Care	1.8%
RPC, Inc.	Energy	1.7%

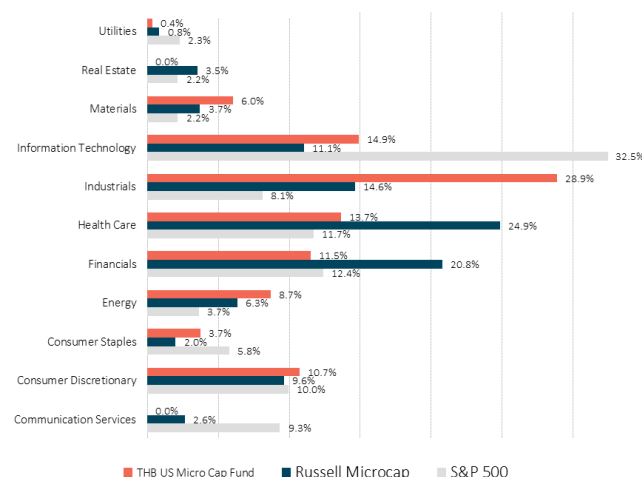
Source: THB Asset Management

Companies by market capitalisation



Source: THB Asset Management

Sector allocation⁶



6. The Russell Microcap Index is a capitalisation weighted index of 2,000 stocks that captures the smallest 1,000 companies in the Russell 2000 and 1,000 smaller US based listed stocks. Portfolio holdings and allocations are subject to change and should not be considered as investment recommendations to trade individual securities. The securities identified and described do not represent all of the securities purchased, sold or recommended for client accounts. The reader should not assume that an investment in the securities identified were or will be profitable. There is no assurance that any securities discussed herein will remain in the portfolio at the time you receive this report, or that securities sold have not been repurchased. There can be no assurance that investment objectives will be achieved. A full list showing every holding's contribution to the overall account's performance during the measurement period and calculation methodology is available upon request.

Investment strategy

THB Asset Management (THB), an investment franchise of Victory Capital Management Inc., is a dedicated micro and small cap specialist investment franchise based in Connecticut, USA. Founded in 1982, THB Asset Management has 40 years' experience investing in micro and small cap companies. THB's US Micro Cap strategy is based on the belief that there are inefficiencies in the micro cap segment of the market due to lack of analyst coverage, difficulty in identifying value and the impact that management skill has on the direction of smaller companies. THB utilises a disciplined, fundamental bottom-up approach that blends both qualitative and quantitative methods to construct a well-diversified portfolio of companies that possess attractive operating metrics, yet with comparable valuation to the Russell Microcap® Index.

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