THB INTERNATIONAL OPPORTUNITIES STRATEGY QUARTERLY COMMENTARY

THB Asset Management®

As of March 31, 2022

Executive Summary

The THB International Opportunities Strategy (the "Strategy") seeks long-term capital appreciation over full market cycles through the creation of a focused portfolio of high-quality securities from 22 of the 23 developed markets. Our investable universe contains approximately 4,000 securities, including constituents from the MSCI World ex USA Small Cap and Micro Cap Indices. The Strategy typically holds 130–160 securities and has a high active share.

THB believes that the international small-cap universe is very inefficient, and that a focused portfolio of high-quality securities in the space can offer strong risk-adjusted returns.

THB International Opportunities Strategy underperformed its benchmark, the MSCI World ex USA Small Cap Index, by 6.32% for the recent quarter and was 0.63% behind for the trailing one-year period (net of fees).

Market Review

Global Equities delivered mixed performance this quarter as participants digested persistent levels of higher inflation, tighter monetary policy, and simmering geopolitical tensions that culminated with Russia's invasion of Ukraine on February 24. The invasion of Ukraine had been weighing on the markets throughout February, and most indices have recovered to levels above the invasion day lows as of March 31, 2022. Western countries reacted swiftly to the invasion and unleashed a host of sanctions against Russia and also effectively unplugged Russia from the world banking system by disallowing transactions via the SWIFT system. In addition to mandatory governmental sanctions, a significant number of major brands and corporations voluntarily decided to exit or cease operations in Russia. These sanctions and actions served to amplify preexisting inflationary drivers such as energy prices and supply chain disruptions. The Federal Reserve raised interest rates and struck a more hawkish tone, intending to bring inflation in the US under control. Large-cap companies outperformed this quarter, with the MSCI World ex USA Index returning -4.81% versus the MSCI World ex USA Small Cap Index return of -7.23%.

A new era

We may look back on the invasion of Ukraine as a time marker when a new geopolitical and economic era began. In the short span of a few weeks, seismic geopolitical changes have taken place that we believe will have a sizable impact on global economies, industries, and markets for years to come.

Globalization as we knew it ends

Years of Western countries' appeasement and ignorance regarding the issues surrounding questionable trading partners and practices likely peaked with the invasion of Ukraine. Many of these issues have been clear for decades, but Western leaders turned the other way for a host of reasons. The naive view that economic interdependence would be a panacea for known issues in both China and Russia has ended abruptly. Intertwining Western economies with both China and Russia in large-scale ways has peaked and will likely undergo years of unwinding.

The revanchist tendencies of Mr. Putin set in motion changes that were hard to imagine a month prior. With a single action, he has united NATO and the EU, ended decades of Swiss neutrality, doubled the German defense budget, severely damaged and isolated the Russian economy for years to come, united the US Democrats and Republicans in their common support for Ukraine, and managed to possibly damage his "no limits" friendship with China.

The next era of globalization will likely encompass trading blocs and regions versus full global integration. Countries will value self-sufficiency above other considerations and trade primarily with countries with shared values and politics. Looking inward (versus outward to low-cost manufacturing locations) will likely be a long-term positive shift for domestic workers and industries.

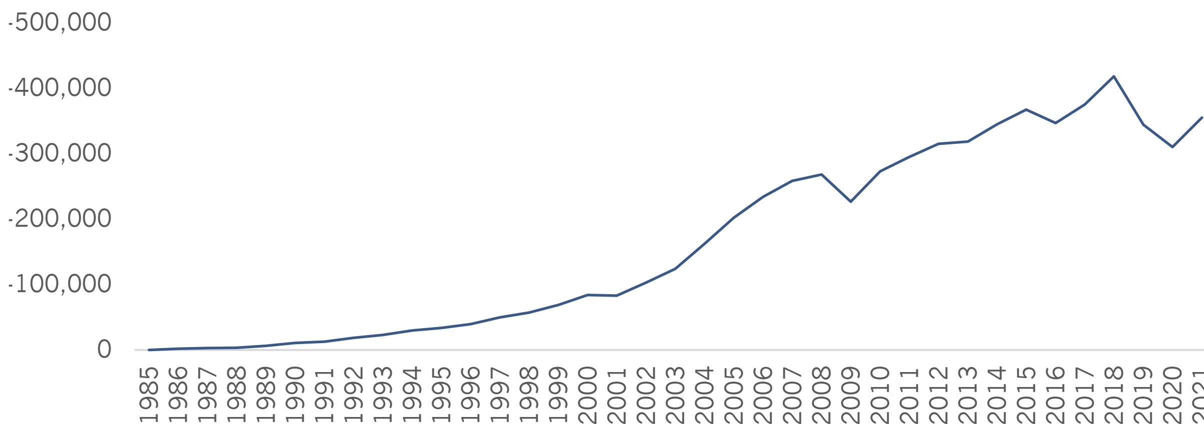
Inflation will not be homogenous

Inflation will not be homogenous across all goods, services, and wages. Unexpected winners and losers will emerge as secondary effects ripple through the economy and difficult-to-predict adaptations occur. Inflation is a point-to-point metric capturing shorter term (12-month to 18-month) directional changes. This is of course important, but sometimes misses the longer-term backdrop. Certain prices and wage groups have experienced a decade-plus of flat to declining movement. The recent "spikes" may be partially caused by current events but are also reflective of the secular declines witnessed during the prior periods. As the new era in geopolitics is ushered in, previous inflation trends may change and not reverse so quickly.

Globalization was a key deflationary factor in the global economy, creating its own set of countries, industries, and companies that experienced significant benefits as globalization roared ahead. One group that did not win during the globalization was factory workers in many developed markets. As jobs were lost to low-cost countries, workers lost any expectation of wage increases. Jobs were scarce and workers were plentiful, allowing corporations to keep wages consistently flat during a fairly strong economic period.

As peak globalization occurs, many companies are aiming to shore up complex supply chains and move production back onshore. Such simultaneous actions by varying groups of industries are increasing the demand for this cohort of workers in an already tight labor market.

Inflationary effects on certain goods, as we have previously stated, will surely recede. The laws of supply and demand still hold true, and producers will move to take advantage of sharply higher prices with increased supply. Additionally, the rate of price change for certain goods will moderate slowing overall inflation. This relationship breaks down when multiple forces inhibit the anticipated supply response, as we are currently experiencing with the global energy markets.



Source: US Census

En-flation

Hydrocarbons impact many aspects of our economy, and rising oil and gas prices will make controlling inflation even more difficult. The breadth of energy's impact on our economy makes taming overall inflation very challenging. Factories run on energy, and hydrocarbons are a key raw material in many products we use each day. Additionally, labor-intensive industries such as farming use vast amounts of energy to plant and harvest the foods we eat. Rising energy prices will be passed along in the form of higher prices for food and services, impacting large parts of our economy.

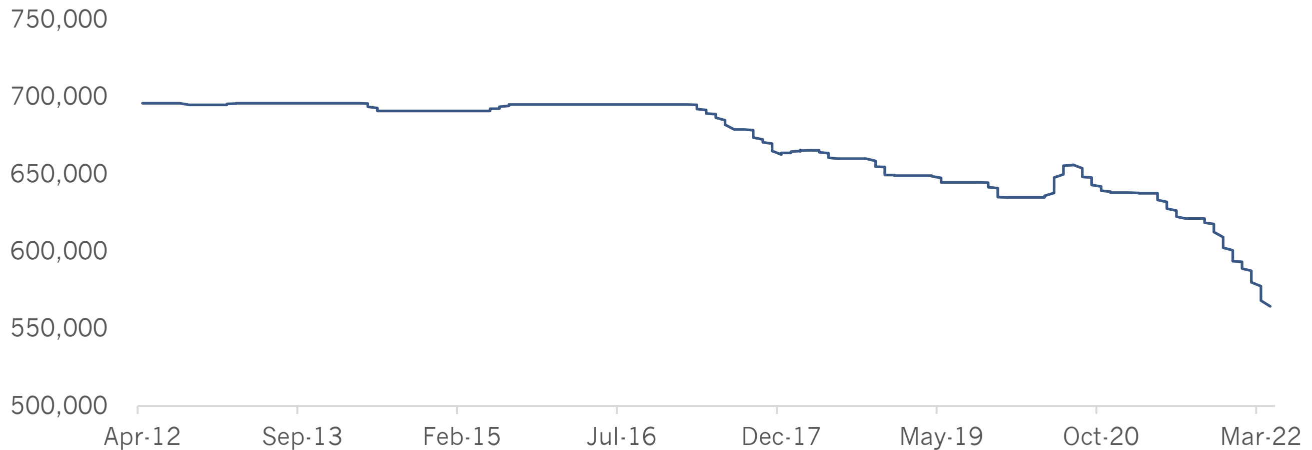
Fossil fuels have generally experienced boom-and-bust cycles largely anchored to the cyclical elements of supply and demand. Societal, governmental, and investment changes, such as ESG considerations and decarbonization, have altered the typical supply response. Investors and banks are reducing exposure to the industry, and the companies themselves are diverting cash flows from exploration (supply growth) to dividends and share repurchases. The supply problem is further complicated by where reserves are located. As Russian oil went under sanctions, the countries with slack capacity (such as Iran, Venezuela, and Saudi Arabia) were talked about as areas from which to source increased supply. Iran and Venezuela already occupy spots on the list of top five most sanctioned countries in the world, and Saudi Arabia's production facilities were recently attacked by Yemen rebels (Houthi). It should be clear that global slack energy capacity is not located in ideal or stable areas, and as certain European countries are quickly learning, this should not be viewed as a long-term supply solution. Fossil fuels, as the world has suddenly witnessed, have not been relegated to the dustbin of history just yet. As expected, the journey to a greener, lower carbon future will require hydrocarbons and not be as linear as some would hope.

Bare cupboard

The Ukraine invasion adds more supply pressures to what was already a tight market, and no quick solutions are apparent. Drilled but uncompleted wells in the US (chart below) have hit a five-year low. These wells would typically come online quickly and provide a supply response. Currently, there is not much excess supply in the system or places that can bring that supply online quickly.

Source: US Department of Energy

On March 31, President Biden announced the largest ever release from the US emergency stockpile of oil (Strategic Petroleum Reserve, or SPR) to combat high energy prices. Starting in May, the US will release 1 million barrels of oil per day from SPR. This will continue for six consecutive months, releasing approximately 180 million barrels in total. This equates to approximately nine days of US oil consumption and two days of global oil consumption. Once released, US stockpiles in the SPR will be approximately 388 million barrels, down more than 40% from the recent high of 695 million in 2017. Releasing supply may not have the desired impact on pricing, as supply could possibly be cut by other (OPEC, Russia) global players. Additionally, those emergency reserves will need to be restocked at some point in the future.



Source: US Deparment of Energy

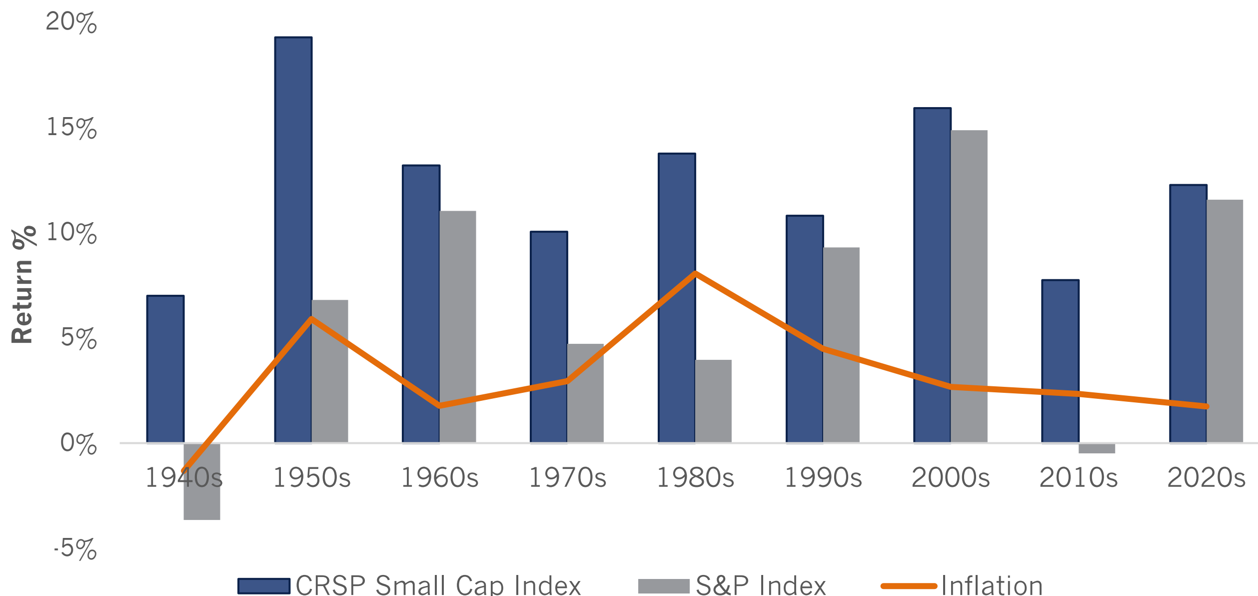
Wars are inflationary

History has shown that wars are generally inflationary, and we are currently experiencing three "wars" across different fronts. We have an actual shooting war in Ukraine, the war against climate change, and the very recent battle against Covid-19. Wars typically require large amounts of "stuff" in a short time frame. Depending on the actual war, food, machinery, ammunition, clothing, fuel, technological solutions, and vehicles are some examples of what is needed. Governments have historically printed money to finance wars, and the same is happening today. Governments across the world are increasing their budgets to fight these three wars, with some examples listed below.

Germany – Annual defense budget increase of $50 billion (since Ukraine invasion)
Finland – One-time defense budget increase of $2 billion (since Ukraine invasion)
Japan – One-time defense increase of $8 billion (host US troops and increase alliance cooperation)
Japan – Aiming to increase annual defense budget from 1% of GDP to 2% (increase of $45 billion annually)
UK – Infrastructure / green energy – $850 billion
US – Covid-19 relief and actions – $3.6 trillion
Japan – Carbon neutrality by 2050 – $10 trillion
Ukraine – Rebuilding cost (TBD; current estimate $600 billion)

Why small companies perform well during inflationary periods

Smaller-cap stocks have historically performed well during inflationary periods.



Source: CRSP

This relative outperformance is likely due to a host of factors. The structure of the underlying businesses, industry representation of the benchmarks, and labor force composition are some of the reasons that contribute to their ability to prosper during higher levels of inflation. Additionally, small- and mid-size companies typically have sizable market shares of lower total addressable market sizes. Put simply, smaller companies sell mission-critical, niche parts or services that go into much larger products or projects. This structure generally affords them pricing power.

- Nimble, flexible operating structures
- Pricing power
- Lower amounts of leverage
- Benchmark composition

Inflation opportunities in today's markets

Every market cycle, even with similar drivers such as inflation, will have differing sets of companies that prosper. Our investment process seeks out companies with traits such as low levels of debt, pricing power, high operating margins, and high returns on capital. Many of these traits are also shared by businesses that we expect may prosper during inflationary periods.

Considering today's economic structure and inflation backdrop, we see a host of attractive opportunities. Some are textbook inflation hedges, and others are more tangential and situational to today's environment.

Commodity producers

Energy, metals, chemicals, wood products, fertilizers, aggregates, and food producers.

Commodity producer ecosystem

Companies that sell to or that service commodity producers should benefit from the higher volumes and increased revenue from their customers. These include oil service companies and machinery producers.

Distributors

Companies that distribute various goods (machinery, food, technology, chemicals) stand to benefit from inflation, assuming they are able to hold margins. They may experience higher gross margin revenue over some element of fixed costs.

People businesses/services

In the current very tight labor market, having an intact team that can provide various services will be in high demand. Customers may not have the ability to find and retain personnel needed to perform certain services. Companies that can provide them in a timely, efficient manner should do well.

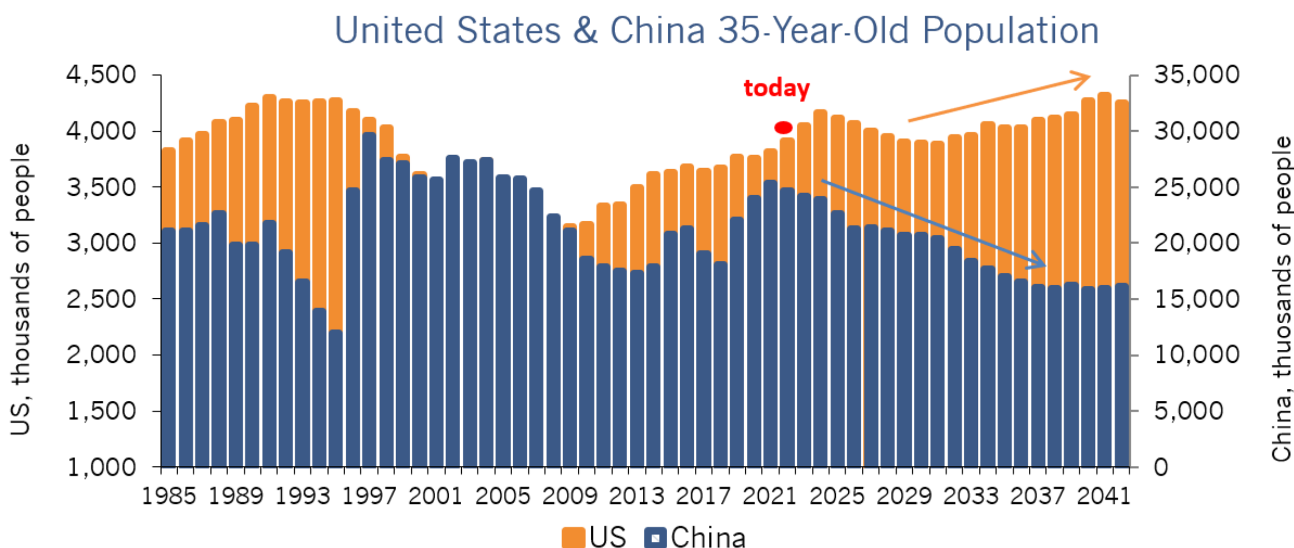
Technology companies

Broad wage and goods inflation that are expected to spur capital investment into projects that increase efficiency and productivity. Software, services, and hardware should all be needed.

The people

Demographics are an important part of a country's economic narrative that are at times overlooked by investors. These are predictable data sets that take a backseat to more prominent economic releases. GDP per capita of a country is one analysis utilized to highlight the economic possibilities of countries such as China as they expand their standards of living and total GDP. The US, however, has one significant demographic advantage over China. The chart below illustrates the historical and estimated native population of 35-year-olds in each country. That age demographic is a key spending milestone attributed to career stability, family formation, and housing needs.

China, due to prior population policies, faces a significant future demographic headwind. In fact, this year marks the start of a multi-decade decline in that key spending cohort of their population. In addition to actual native population birthrates, the US benefits from the 1M+ immigrants who come to this country each year. China has had negative net migration for the past two decades.



Source: National Center for Health Statistics, Statista

Benchmark Performance

The MSCI World ex USA Small Cap Index (the "Index") returned -7.23% (USD) in 1Q 2022.

Energy (+24.66%) was the best performing sector, followed by Materials (+1.94%) and Utilities (+1.00%). Health Care (-17.94%) was the worst performing sector, followed by Consumer Discretionary (-14.83%) and Information Technology (-14.62%).

Canada (+6.47%) was the best performing country, followed by Singapore (+3.00%) and Ireland (+0.54%). Finland (-19.89%), Sweden (-18.21%), and the United Kingdom (-14.31%) were the worst performing countries in the Index.

Portfolio Performance & Positioning

The THB International Opportunities Strategy returned -13.55% (net of fees) in Q1, underperforming the Index by 632 bps.

Contributors to the portfolio's performance were positive stock selection in Canada, underallocation to Singapore, and underallocation to Israel. Detractors from performance included underallocation to Canada as well as stock selection in the United Kingdom and Japan.

From a sector perspective, primary contributors to performance mainly came from underallocation to Financials, stock selection in Real Estate, and underallocation to Consumer Discretionary. Stock selection in Financials and Industrials, as well as overallocation to Health Care, were primary detractors to performance this quarter.

THB's top five performing stocks (from a contribution standpoint) were Karora Resources, Inc. (Australia, Materials, +0.3%); u-blox Holding AG (Switzerland, Information Technology, +0.3%); Wesdome Goldmines Ltd. (Canada, Materials, +0.3%); VERBIO Vereinigte BioEnergie AG (Germany, Energy, +0.2%); and 2G Energy AG (Germany, Industrials, +0.2%).

The bottom five performing stocks (from a contribution standpoint) were Esker SA (France, Information Technology, -0.6%); Kainos Group PLC (United Kingdom, Information Technology, -0.5%); Basler AG (Germany, Information Technology, -0.5%); Eckert & Ziegler Strahlen-und Medizintechnik AG (Germany, Health Care, -0.5%); and Kardex Holding AG (Switzerland, Industrials, -0.4%).

The Strategy's companies continue to deploy capital with the goal of increasing shareholder value. They announced 22 share repurchase authorizations and 28 acquisitions in the first quarter.

During the quarter, we added two new holdings to the strategy that we believe stand to benefit from the transition to electric vehicles (EVs). A significant amount of metals such as nickel, lithium and cobalt will be required to increase the production of these cars and their batteries.

Imdex Ltd. – is a global mining technology company that develops drilling optimization products and cloud-connected sensors. Its solutions provide real-time rock knowledge and data that enables fast, successful and cost-effective operations to drilling contractors and resource companies. Imdex IoG sensors enable creation of a virtual rock model for critical analysis and precision mining, which helps their customers reduce GHG emissions from mining operations.

Imdex has a global presence in all key mining regions of the world and a comprehensive distribution network. It is well positioned to benefit from increasing capital spending due to demand for critical metals used in clean energy such as electric vehicles and batteries. For the world to achieve its net-zero goals, the aluminum, copper and nickel industries need to double in size by the late 2020s, while lithium and cobalt mining would need to increase fivefold.

Karora Resources – is a Canada-listed company with two gold mining operations in Western Australia: Beta Hunt Mine and Higginsville Gold Operations. The company is investing in more exploration projects in the nearby area to leverage their milling process in a hub-and-spoke model. They are also exploring the option to mine nearby nickel. The company has an attractive ESG profile, reaching carbon neutrality in 2021 through both direct GHG reduction initiatives and offset projects in renewables and Australian reforestation under the Australian government's Climate Active Program. New CEO Paul Huet, who joined the company in 2019, brought 30 years of industry experience in the mining industry and a strong operational track record.

Outlook

Many of the challenges and opportunities witnessed and discussed over the past year remain in place. Like Covid-19, the war in Ukraine appears to be another accelerant for preexisting trends. In the short term, higher levels of volatility may be experienced as recalibration to a new geopolitical and inflationary environment takes place. Longer term, we believe there are many positive developments and conditions that will increase the opportunity set for smaller company investors.

We thank you for your continued support.

Sincerely,

THB Asset Management

Top 10 Holdings (%)

as of March 31, 2022

Holding	Rep. Account
Johns Lyng Group Ltd	1.46
El.En. S.p.A.	1.43
Treatt plc	1.37
Judges Scientific plc	1.35
secunet Security Networks AG	1.26
u-blox Holding AG	1.20
Focusrite PLC	1.17
Biotage AB	1.15
PWR Holdings Ltd.	1.15
Kainos Group PLC	1.14

Sector Diversification (%)

as of March 31, 2022

Sector	Rep. Account
Communication Services	4.37
Consumer Discretionary	7.73
Consumer Staples	3.25
Energy	3.29
Financials	0.98
Health Care	15.76
Industrials	33.20
Information Technology	21.90
Materials	8.09
Real Estate	0.57
Utilities	0.00
Cash	0.85

Performance

Average Annual Returns (%) as of March 31, 2022

THB International Opportunities Composite	QTD	YTD	1-YR	3-YR	5-YR	10-YR	Since Inception
Gross of Fees	-13.28	-13.28	-1.09	12.82	12.14	–	14.10
Net of Fees	-13.55	-13.55	-2.32	11.45	10.79	–	12.76
MSCI World ex. U.S. Small Cap Index (Net)	-7.23	-7.23	-1.69	9.55	7.79	–	7.47

Past performance cannot guarantee future results. Performance returns for periods of less than one year are not annualized. Returns include reinvestment of dividends and capital gains. Gross-of-fees returns are presented before management and custodial fees but after all trading expenses. 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 feel). 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 equity 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 II of its Form ADV.

Investing involves risk, including loss of principal.

The information in this article is based on data obtained from recognized services and sources and is believed to be reliable. Any opinions, projections or recommendations in this report are subject to change without notice and are not intended as individual investment advice. The securities highlighted, if any, were not intended as individual investment advice. A complete list of all recommendations of security selection is available by request for the previous 12 months. Furthermore, Victory Capital Management Inc., and its affiliates, as agents for their clients, and any of its officers or employees, may have a beneficial interest or position in any of the securities mentioned, which may be contrary to any opinion or projection expressed in this report.

The holdings and sector diversification are presented to illustrate examples of the portfolio's investments and may not be representative of the portfolio's current or future investments. Holdings are as of a point in time and may change at any time.

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. Holdings are as of quarter end and may change at any time. This material should not be construed as a recommendation to buy or sell securities.

The THB International Opportunities Composite contains fully discretionary international equity accounts and for comparison purposes is measured against the MSCI World ex USA Small Cap Index. The returns for the MSCI World ex USA Small Cap Index presented are net of withholding taxes. As of January 1, 2016, the composite name changed from "International Composite" to "International Opportunities Composite." Prior to January 1, 2016, the benchmark was the MSCI World ex USA Micro Cap Index. This benchmark change was made to more accurately reflect the investment strategy of the composite. The minimum account size for this composite is $100,000. The objective of the composite is to seek long-term capital appreciation over full market cycles by investing primarily in companies that THB feels are undervalued, exhibit lower risk characteristics, and have superior operating metrics. The product typically holds 130–160 securities and has a high active share.

The MSCI World ex USA Small Cap Index captures small-cap representation across 22 of 23 developed markets (DM) countries (excluding the United States). With 2,530 constituents, the index covers approximately 14% of the free-float-adjusted market capitalization in each country.

Index returns reflect the reinvestment of dividends and capital gains but do not include advisory fees, transaction costs, or other expenses. Non-US indices are net of non-reclaimable withholding taxes, if any. One cannot invest directly in an index.

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