Commentary | 3Q23

Voya MidCap Opportunities Strategy

Seeking a More Favorable Risk/Return Trade-off

Strategy overview

Actively managed mid-cap growth strategy that relies on fundamental research and analysis to identify companies with strong and accelerating business momentum, increasing market acceptance and attractive valuations.

Key takeaways

- The bull market run over the first half of the year took a pause as markets pulled back during the third quarter. The specter of a government shutdown was avoided but that has done little to quell market volatility thus far.
- For the quarter, the Strategy outperformed its benchmark, the Russell Midcap Growth Index (the Index), on a net asset value (NAV) basis, due to favorable stock selection, particularly within the financials and consumer staples sectors.
- There remains a great deal of uncertainty ahead regarding the prospect of slowing economic growth and whether or not inflation has truly been tamed by the unprecedented rate cuts over the past year. It appears that the U.S. Federal Reserve is nearing the end of the rate-hike cycle. We are cautiously optimistic that we can achieve the soft-landing scenario.

Portfolio review

U.S. equity markets reversed course during the third quarter, weighed down by fears of interest rates remaining higher for longer. The S&P 500 Index fell by –3.27% for the quarter. Energy and information technology stocks led while utilities and consumer staples lagged. Growth stocks modestly outperformed value stocks during the quarter, and large caps beat small caps.

The U.S. bond market remained choppy during the quarter. The Bloomberg U.S. Aggregate Bond Index lost –3.23%, while a surprisingly resilient U.S. economy pushed the 10-year U.S. Treasury yield from 3.86% at the beginning of the quarter to 4.59% by quarter-end. In July, U.S. Federal Reserve raised rates by 25 basis points, bringing the Fed funds rate to a range of 5.25–5.50%. Rates were held steady at the September meeting, and Fed Chair Powell's remarks maintained a hawkish tone as he reiterated the central bank's strong commitment to returning inflation to its 2% target.

For the quarter, the Strategy outperformed the Index due to stock selection. Stock selection within the financials and consumer staples sectors contributed the most to performance. The information technology and healthcare sectors were the greatest detractors.

Key contributors to the quarter's performance were Reata Pharmaceuticals, Inc., Tradeweb Markets, Inc. and Saia, Inc.

Owning a non-benchmark position in Reata Pharmaceuticals, Inc. (RETA) contributed to performance. The company was acquired by Biogen during the period in a deal that valued the company at $7.3 billion.

An overweight position in Tradeweb Markets, Inc. (TW) contributed to performance. The company reported solid earnings during the period but the larger focus was around management commentary around price increases and increasing volume trends, reporting “mid-double-digit” volume and revenue growth through July.

An overweight position in Saia, Inc. (SAIA) contributed to performance. The company reported a strong quarter which exceeded estimates and showed strong cost execution and opportunity to capture volume due to disruption in the industry.

Key detractors for the quarter were Inspire Medical Systems, Inc., Keysight Technologies Inc. and CONMED Corp.

An overweight position in Inspire Medical Systems, Inc. (INSP) detracted from performance. The company reported a strong quarter but concerns loom over the total addressable market (TAM), as the impact of weight loss drugs could negatively impact Obstructive Sleep Apnea (OSA) volumes.

An overweight position in Keysight Technologies Inc. (KEYS) detracted from performance. The company reported earnings that were in-line with consensus, but weak guidance amidst slowing demand, and the company believes orders could be weaker in some markets for the next few quarters.

Owning a non-benchmark position in CONMED Corp. (CNMD) detracted from performance. The company reported strong earnings during the period but concerns about CNMD losing market share to Novanta — a competitor potentially bringing a new medical device to market - weighed on shares.

Current strategy and outlook

The U.S. economy has remained resilient as have corporate earnings, fueling the debate of a hard versus soft landing. We still believe there may be greater volatility to come given uncertainty over Fed rate policy through the end of the year; mixed business sentiment and slowing economic growth; and whether a recession will actually happen, and if so, the duration and depth. The real story has been the resilience of corporate earnings and rise in equity valuations as interest rates begin to normalize. Using price-to-earnings (P/E) ratio as a proxy, valuations for the S&P 500 Index ended 2022 well below 2019 levels. However, despite elevated rates and tightening financial conditions in the first half of the year, valuations have expanded modestly. P/E ratios are still below 2019 levels, and we believe earnings expectations are reasonable, but this could change as we enter 2024 depending on the state of the U.S. economy.

Holdings detail

Companies mentioned in this report – percentage of portfolio investments, as of 09/30/23: Reata Pharmaceuticals, Inc. 0%, Tradeweb Markets, Inc. 2.45%, Saia, Inc. 2.06%, Inspire Medical Systems, Inc. 1.47%, Keysight Technologies Inc. 0% and CONMED Corp. 1.11%; 0% indicates that the security is no longer in the portfolio. Portfolio holdings are subject to daily change.

The **Russell Midcap Growth Index** is an unmanaged Index that measures the performance of those companies included in the Russell Midcap Index with relatively higher price-to-book ratios and higher forecasted growth values. The Index does not reflect fees, brokerage commissions, taxes or other expenses of investing. Investors cannot invest directly in an Index.

Principal Risks: All investing involves risks of fluctuating prices and the uncertainties of rates of return and yield. **Foreign Investing** poses special risks including currency fluctuation, economic and political risks not found in investments that are solely domestic. Investing in stocks of **Mid-Sized Companies** may entail greater volatility and less liquidity than larger companies. The Portfolio may use **Derivatives**, such as options and futures, which can be illiquid, may disproportionately increase losses and have a potentially large impact on Portfolio performance. Other risks of the Portfolio include but are not limited to: **Growth Investing Risks, Market Trends Risks, Other Investment Companies' Risks, Price Volatility Risks, Liquidity Risks, Securities Lending Risks and Portfolio Turnover Risks. Investors should consult the Portfolio's Prospectus and Statement of Additional Information for a more detailed discussion of the Portfolio's risks. An investment in the Portfolio is not a bank deposit and is not insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board or any other government agency.**

The strategy employs a quantitative model to execute the strategy. Data imprecision, software or other technology malfunctions, programming inaccuracies and similar circumstances may impair the performance of these systems, which may negatively affect performance. Furthermore, there can be no assurance that the quantitative models used in managing the strategy will perform as anticipated or enable the strategy to achieve its objective.

The strategy is available as a mutual fund or variable portfolio. The mutual fund may be available to you as part of your employer sponsored retirement plan. There may be additional plan level fees resulting in personal performance that varies from stated performance. Please call your benefits office for more information.

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