

## SMALL-CAP OPPORTUNITIES STRATEGY

3Q 2018

### The Quarter in Review

The Oberweis Small-Cap Opportunities Composite returned 9.12% (8.95% net of fees) during the third quarter versus a 5.52% return for the benchmark Russell 2000 Growth Index, an outperformance of 360 bps (343 basis points net of fees). Year-to-date, the Composite returned 19.22% (18.60% net of fees) versus 15.76% for the Russell 2000 Growth Index, a positive differential of 346 basis points (284 basis points net of fees).

Both absolute and relative returns were solidly positive despite numerous undercurrents that have required careful navigation so far this year. Growth stocks continued to perform better than value stocks during the quarter and have now outperformed by 862 basis points year-to-date<sup>1</sup>. Valuation just hasn't mattered much this year, and this theme has infiltrated the growth universe as well, with the Russell 2000 Growth Index return driven by the highest P/E quintile and companies without earnings (such as biotech and software stocks). This is also reflected in ROE data; benchmark returns have been driven by the lower two ROE quintiles in 2018. In a portfolio populated with attractively valued (based on our above-consensus estimates) companies growing earnings beyond expectations, it's a backdrop that hasn't been particularly favorable, although one we were able to overcome through positive stock selection. From a capitalization perspective, small-cap stocks significantly outperformed large caps over the first half of 2018 but gave back nearly all of those gains in the third quarter<sup>2</sup>.

We believe concerns in the marketplace over a "trade war" influenced returns as investors have generally discounted an escalating situation by emphasizing investment in sectors and industries relatively less exposed to global trade. The year-to-date benchmark return was driven by the technology and healthcare sectors, while energy, materials, and producer durables were the clear losers. More interesting, technology and healthcare performance was acutely bolstered by industries perceived to be unscathed by tariffs, threatened or actual. Within tech, for example, software stocks returned nearly 39% so far in 2018 and 12% during the September quarter. Medical equipment stocks returned 61% and 24%, respectively, and biotechs, while not a huge driver in the quarter, returned 16% this year.

To us it seems like a relatively crowded trade at this point, with a consensus opinion that tensions will ratchet higher from here. Witness the following comment from JP Morgan in early October: "A full-blown trade war becomes our new base case scenario for 2019." Meanwhile, the Trump administration just completed a revamped trade agreement with Mexico and Canada, dubbed USMCA, suggesting to us the possibility that trade tensions may have actually peaked.

The elephant in the room now is clearly China. While we don't know when a deal will get done, we believe President Trump views himself first and foremost as a skilled deal-maker and ultimately – after all the bluster and rhetoric and threats – a deal we shall get. We think most underestimate Trump's desire to do a deal and overestimate the concessions necessary by China to reach an agreement. Look no further than the USMCA for supporting evidence, which The Brookings Institution labeled as "a new trade deal that looks remarkably similar to the old NAFTA." Trump's big win with Canada? Greater access to Canada's market for U.S. dairy products. If Trump can hold up a piece of paper with President Xi's signature it's a win for Trump with his support base – details be damned. The defensive posturing by investors could quickly and painfully unwind when it happens.

Despite trade fears, equity returns have been supported by continued economic strength in the U.S., and current economic data appear to support persistence into 2019. Corporate America, benefitting from tax reform and an accelerating economy, has posted record profits this year. The U.S. manufacturing Purchasing Managers' Index has remained solidly above 50 (suggesting expansion), and developed markets readings in Europe and Asia ex-China are similarly robust, although emerging markets readings have not been as solid and are flashing a warning signal. U.S. unemployment declined to 3.7% in September, and while wages are inflating as a result, the rate of wage increases remains muted relative to historical standards. The consumer has benefited, with incrementally more disposable income, record household net worth and historically low debt-service ratios.

The Federal Reserve's response is tighter monetary policy, executed through rate increases and a contracting balance sheet. The Fed's target is inflation; price spikes in emerging economies and a 21% increase in oil this year are warning signs, but overall inflation remains under control in the U.S. and throughout the developed world. A more rapid rise in rates and prices likely represents the biggest risk to equity markets as we enter 2019.

While macro factors can drive correlations toward one and influence stocks as a group in shorter time periods, we believe that investing in companies growing earnings beyond expectations results in superior investment performance over the long-term. Rather than ruminate about macro-economic indicators or geopolitical events, we focus on investing in individual businesses where we believe something fundamentally misunderstood or under-estimated is likely to drive earnings growth in excess of consensus expectations. While the multiple paid for such companies may oscillate in the short-run, we believe building portfolios populated with such companies leads to portfolio performance in excess of the benchmark over the long-term.

<sup>1</sup> During the quarter, the Russell 2000 Growth Index returned 5.52% versus 1.60% for the Russell 2000 Value Index, a differential of 392 basis points. Year-to-date, the Russell 2000 Growth Index returned 15.76% versus 7.14% for the Russell 2000 Value Index, a differential of 862 basis points

<sup>2</sup> During the quarter, the Russell 2000 Growth Index underperformed the Russell 1000 Growth Index by 365 basis points.

## Portfolio Highlights

As of September 30, 2018, the portfolio was 95.8% invested in 81 different positions. The portfolio had its largest over-weightings in producer durables (18.5% average weighting during the quarter versus 15.5% for the Russell 2000 Growth Index), consumer discretionary (20.2% versus 17.8%), and materials (9.5% versus 8.1%); these collective over-weights during the quarter cost the portfolio 20 basis points in performance. The portfolio was under-weight health care (21.8% versus 25.7%), consumer staples (0.3% versus 2.5%), and energy (0.4% versus 2.3%). Year-to-date, allocation effect detracted 148 basis points from portfolio performance, led by our under-weighting in health care and our over-weighting in producer durables.

Performance in the third quarter was driven entirely by stock selection (allocation effect was neutral), with notable picks in health care (where our holdings returned 26.06% versus an 8.05% return for the benchmark's health care holdings), consumer discretionary (11.57% versus 5.50%), and materials (5.67% versus 0.57%). Performance was negatively impacted by stock selection in technology (-2.21% versus 8.97%) and financials (-2.29% versus 2.06%).

Some of the top performers during the third quarter included: Amedisys (AMED), which returned +46% and contributed 72 basis points to portfolio return; STAAR Surgical (STAA), which returned +55% and contributed 70 basis points to portfolio return; and BioTelemetry (BEAT), which returned +43% and contributed 69 basis points to portfolio return. In contrast, some of the leading detractors for the quarter included: Enova Intl (ENVA), which returned -21% and detracted 36 basis points from portfolio return; Intersect ENT (XENT), which returned -30% and detracted 31 basis points from portfolio return; and Asure Software (ASUR), which returned -21% and detracted 27 basis points from portfolio return.

### PORTFOLIO CHARACTERISTICS

(AS OF SEPTEMBER 30, 2018)

Number of Stocks	81
Weighted Market Capitalization (in millions)	\$2,635
Median Market Capitalization (in millions)	\$2,429
P/E Forward 4 Quarters (estimated)	18.9x
Long-Term Future EPS Group Rate (estimated)	10%
Long-Term Debt to Total Equity	14%
Return on Equity	8%
Cash Position	4.2%
Portfolio Turnover (2017)	137.1%

Source: Thomson Reuters Eikon

## Key Benefits

The Small-Cap Opportunities strategy seeks to capitalize on the exceptional growth potential of smaller companies that are often misunderstood by traditional Wall Street research analysts. The Small-Cap Opportunities strategy generally invests in companies (with market capitalizations under \$5.0 billion at the time of purchase) where our expectations for earnings growth differ from consensus expectations. These companies often boast exciting products and/or services, a strong and sustainable competitive position, and the potential for upward revisions in earnings expectations in the future. Our fundamental research process is specifically designed to efficiently identify such opportunities.

The key benefits of the Small-Cap Opportunities strategy are:

- Potential for significant alpha over a full market cycle
- Combines empirically-proven Behavioral Finance principles with the very best of fundamental bottom-up research
- Disciplined and repeatable investment process managed by a passionate and experienced investment team
- Fundamental research process specifically designed to efficiently discover smaller cap companies that are misunderstood by traditional Wall Street research analysts
- Exposure to smaller cap companies offering the potential for earnings growth that differs from consensus expectations
- Diversified portfolio with a focus on risk management

**Minimum Account Size: \$5 million for Institutional Account Management**

For more information please contact:

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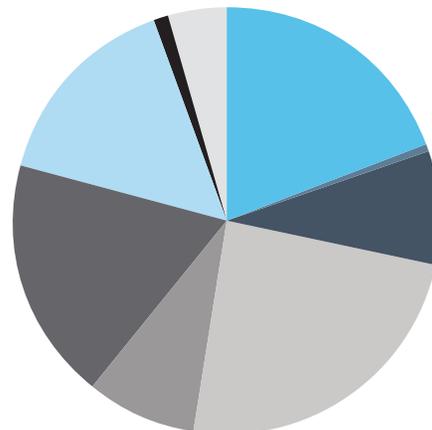
**TOP TEN HOLDINGS (as of September 30, 2018)**

Company		Line of Business
1	LHC Group, Inc.	2.4% Provides home healthcare services
2	Skywest, Inc.	2.2% Operates a regional airline
3	Skyline Champion Corp.	2.2% Designs and manufactures modular homes and RVs
4	Atricure, Inc.	2.2% Develops treatments for atrial fibrillation
5	Biotelemetry, Inc.	2.2% Provides cardiac monitoring services and products
6	Green Dot Corp.	2.1% Offers personal banking products and services
7	Amedisys, Inc.	2.1% Provides home healthcare services
8	Carbonite, Inc.	2.0% Provides cloud data protection services to consumers and businesses
9	Control 4 Corp.	2.0% Provides smart solutions for home entertainment, lighting, and security
10	Cavco Industries, Inc.	2.0% Designs and manufactures modular homes and RVs

Top 10 holdings as a percentage of Total Net Assets. Portfolio Holdings are subject to change at any time. References to specific securities should not be construed as a recommendation to buy or sell and should not be assumed profitable. Source: Thomson Reuters Eikon

**SECTOR WEIGHTINGS (as of September 30, 2018)**

Consumer Discretionary	19.4%
Consumer Staples	0.0%
Energy	0.5%
Financial Services	8.5%
Health Care	24.1%
Materials & Processing	8.4%
Producer Durables	18.4%
Technology	15.3%
Utilities	1.2%
Cash	4.2%
<b>Total</b>	<b>100.0%</b>



Sector weightings as a percentage of Total Net Assets. Source: Thomson Reuters Eikon

**AVERAGE ANNUAL TOTAL RETURNS (as of September 30 2018)**

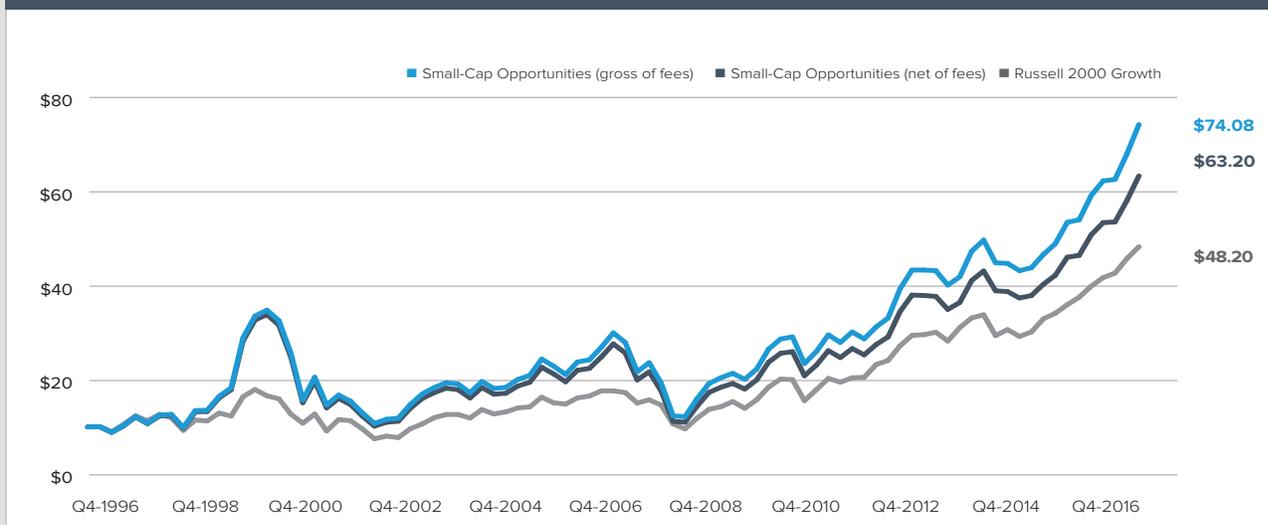
	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Inception (9/15/1996)
<b>Small-Cap Opportunities (gross of fees)</b>	<b>9.12%</b>	<b>19.22%</b>	<b>25.49%</b>	<b>18.28%</b>	<b>13.56%</b>	<b>14.40%</b>	<b>9.62%</b>
<b>Small-Cap Opportunities (net of fees)</b>	<b>8.95%</b>	<b>18.60%</b>	<b>24.67%</b>	<b>17.61%</b>	<b>12.90%</b>	<b>13.61%</b>	<b>8.83%</b>
Russell 2000 Growth Index	5.52%	15.76%	21.06%	17.98%	12.14%	12.65%	7.53%

Oberweis Asset Management, Inc. ("OAM") is an independent investment management firm that is not affiliated with any parent organization. The composite returns are comprised of all fully discretionary accounts with a minimum value of \$2.5 million. Performance results, from 1-1-97 to 12-31-03 and from 7-1-08 to present, are derived solely from the performance of the Oberweis Small-Cap Opportunities Fund (formerly known as the Oberweis Mid-Cap Fund), a registered open-end mutual fund, for which OAM serves as investment adviser. Accounts are dollar-weighted within the composite and reported in U.S. dollars.

The Russell 2000 Growth Index measures the performance of those Russell 2000 companies with higher price-to-book ratios and higher forecasted earnings growth rates. The index is an unmanaged group of stocks, whose performance does not reflect the deduction of fees, expenses or taxes.

Advisory fees are disclosed in Part II of Form ADV. Performance is historical and includes the reinvestment of dividends and other income. Past performance is not necessarily indicative of future results.

Before investing, consider the fund's investment objectives, risks, charges, and expenses. To obtain a copy of the prospectus or summary prospectus containing this and other information, please visit our website at [oberweisfunds.com](http://oberweisfunds.com) or call 800-323-6166. Read it carefully before investing. The Oberweis Funds invest in rapidly growing smaller and medium sized companies which may offer greater return potential. However, these investments often involve greater risks and volatility. There is no guarantee that the portfolios can achieve their objectives. The Oberweis Funds are distributed by Oberweis Securities, Inc. Member: FINRA & SIPC.

**GROWTH OF \$10,000 — WITH INCOME INVESTED (September 15, 1996 – September 30, 2018)**


The Russell Microcap Growth Index began on 7/3/00, and the line graph for the Index begins at the same value as the Fund on that date.

**Oberweis Asset Management, Inc.**

Recognized as a leading small-cap stock specialist, Oberweis has been helping institutional investors manage their assets prudently and effectively for many years.

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