Oberweis
Asset Management

SMALL-CAP VALUE STRATEGY 3Q 2019

The Quarter in Review

In the third quarter of 2019, small-cap value stocks, as measured by the Russell 2000 Value Index, returned just -0.57% for the quarter, while the Oberweis Small-Cap Value strategy returned -1.15%. On an absolute basis, the strategy return remains positive at 11.54% yet was still bested by the benchmark return of 12.82%.

Trade tensions with China remained front-and-center, with the market reacting wildly at times to the latest Tweet, rumor, or unnamed source. We believe the uncertainty surrounding trade policy and the magnitude of tariffs now faced by American companies is impacting corporate profits, the economy, and investor risk appetite for small-cap stocks. U.S. real GDP growth is projected to be a lackluster 1.8% in the third quarter, and the September ISM Manufacturing survey reading of 47.8 was the lowest since June of 2009, implying manufacturing contracted for the second consecutive month. Sub-50 readings were also posted in Japan, Korea, Mexico, Russia, and throughout much of Europe, headlined by a distressing 41.7 measure in Germany.

Growth stocks have been in favor for much of the last decade, and many value investors believe a shift is long overdue. While too early to call a change in leadership, the final month of this quarter exhibited a shift in investor preference from growth stocks toward value stocks, with the Russell 2000 Value Index outperforming the Russell 2000 Growth Index by 595 bps. At least in the short-term, it was clear that investors suddenly seemed to be more focused on asset-rich companies with reliable near-term cash flow versus companies with long-term earnings growth potential. Should this trend continue, it would likely prove favorable for our value-focused investment strategy. Generally, following periods of rising risk aversion, behavioral signaling becomes even more relevant in the identification of value investment opportunities that may be misunderstood in the short run.

At a sector level, the portfolio faced headwinds in the financials and materials sectors, despite positive gains in producer durables and energy. Our regional banks were hit harder by interest rate decreases despite continued positive loan growth and the benchmark REITs performed well where we are underweight. Iron ore prices collapsed and soft growth messages challenged our Materials holdings. These disappointing returns belie the fact that our holdings generally outperformed their respective industries on an earnings growth and surprise basis according to Bloomberg data[1]. We believe this further suggests the idea that current macro noise is overshadowing positive underlying company fundamentals in many cases. We believe that focusing our efforts on individual less-followed companies is more likely to generate alpha over a full market cycle than trying to predict widely-watched macro data points.

The greatest such constant in 2019 has proven to be a regularly shifting trade narrative. The United States' August decision to introduce "List 4"[2] in the ongoing trade struggle added yet another layer of uncertainty to market concerns with consumer discretionary retail and apparel stocks bearing the brunt as these were the industries most affected by List 4. The market continues to gyrate heavily when trade related headlines shift. As a recent example, the World Trade Organization's ruling on the EU's illegal Airbus subsidies opened the door for more US ally tariffs. Many stocks in our strategy, both suppliers and manufacturers, conduct a great deal of business within the EU. In many cases the percentage of EU revenues greatly outweighs China contributions. We believe this has put an understandable "show me" ceiling on valuations which, broadly, appear to still be discounting a lot of bad news and remain 13.7% below twenty-year averages[3] even after September's strong positive move to value.

Additionally, the Federal Reserve's rate decisions continue to be viewed with uncertainty regarding what it may or may not portend about the health of the economy and the sustainability of a positive stock market environment. The Fed has twice cut the Federal Funds Rate by a total of 50 bps year to date putting their target rate at 1.75% – 2.00%. While the recent decreases are helping to support market valuations by keeping debt needed for capital investment less expensive, there is still risk as indicated by the recent liquidity issue in the overnight repurchase markets when the Fed injected over $100 billion in the repo market over two days and has stated plans to continue such support operations. Broadly speaking, even if the reason banks are not willing to lend their reserves to shore up the repurchase market is due to stricter post-crisis regulations, it makes the Fed's messaging about economic growth more difficult.

[1] Strategy industry holdings compared to their respective Russell 2000 Value (R2V) benchmark industries: Strategy Financials holdings demonstrated Sales and Earnings growth of 4.35% and 9.56% vs. 7.90% and 2.97% for the benchmark and Materials holdings demonstrated growth of 3.37% and -8.60% vs. -1.75% and -16.32% for the benchmark. Respective Sales and Earnings surprises for the same Strategy vs. R2V industries were 3.09% and 4.94% vs. 1.23% and -5.59% (Financials) and 0.89% and 14.41% vs. -1.53% and 12.97% (Materials).
[2] On August 20, 2019, the United States Trade Representative (USTR) announced tariffs of an additional 10% on certain consumer goods to be implemented in September and December of this year. Source: The National Law Review
[3] As of 9/30/19, Bloomberg forward P/E ratio for the Russell 2000 Value Index was 16.39 vs a 20 year average P/E 19.10

These two factors, geopolitical trade and lending markets, are causing companies to hold back on spending and growth forecasts are being revised. For example, Deloitte's "baseline" forecast calls for GDP growth of less than two percent in 2020 Individual companies from small-cap Navistar to large-cap Illinois Tool Works are cutting spending, and broad manufacturer purchasing has dropped to the lowest level since 2017 according to the Census Bureau. The point is that while the economy has generally been strong enough to absorb these uncertainty costs and avoid recession, the longer and more intense global tension continues to grow, what looked like a low risk to recession now appears more likely the longer global growth continues to sour. In Deloitte's words there is reason "to believe that the economy is unusually sensitive to shocks." Such uncertainty and risk aversion should favor a strategy such as ours focused on high-quality balance sheets and corporate signaling of underlying resilience.

As previously noted, valuations in small-cap value appear to reflect a market wary of risks and are subsequently presenting some companies trading at attractive, relative discounts. It has been difficult to see underperformance in a strategy that seeks out companies signaling undervaluation and which carries desirable fundamental metrics such as solid Free Cash Flow (FCF) yields, attractive relative earnings valuations, and better than benchmark historical and future growth estimates[4]. Yet we believe that sometimes the best moments for investment strategies are when they are most out of favor, and we continue to find investment opportunities where behavioral signaling seems to present evidence of mispricing. The stock market is a game of performance relative to expectations, and we look for opportunities where expectations have, due to human nature, been disproportionately beaten down. We believe that focusing our efforts on individual less-followed companies is more likely to generate alpha over a full market cycle than trying to predict widely-watched macro data points.

PORTFOLIO CHARACTERISTICS
(AS OF JUNE 30, 2019)

Number of Stocks	78
Weighted Market Capitalization (in millions)	$2,940
Median Market Capitalization (in millions)	$2,466
P/E Forward 4 Quarters (estimated)	12.8x
Long-Term Future EPS Growth Rate (estimated)	3.6%
Long-Term Debt to Total Equity	17.8%
Return on Equity	7.8%
Cash Position	0.2%

Source: Thomson Reuters Eikon

Portfolio Highlights

As of September 30, 2019, the portfolio was 99.8% invested in 78 different positions. The portfolio had its largest weights in Financial Services (34.9% versus 41.8% for the benchmark), Producer Durables (17.6% versus 12.3%), and Technology (13.4% versus 7.8%). During the quarter, the portfolio experienced positive stock selection in three main sectors Energy (our holdings in this sector returned -20.10% versus -22.37% for those in the benchmark), Producer Durables (1.93% versus -1.59%), and Consumer Discretionary (4.71% versus 3.50%). Return was most adversely impacted in Materials & Processing (-9.67% versus -2.64%), Financial Services (0.01% versus 1.67%), and Utilities (-1.84% versus 3.60%).

Some of the top performers this quarter included: Tower International (TOWR, which returned +58.92% and contributed 87 basis points to the portfolio's return; CyrusOne, Inc (CONE, which returned +37.93% and contributed 45 basis points; and Mastec, Inc (MTZ), which returned +26.00% and contributed 39 bps. Some of the bottom contributors for the quarter included: Gulfport Energy (GPOR), which returned -44.81% and detracted 47 bps; Cars.com Inc (CARS), which returned -47.26% and detracted 39 bps; and Dana, Inc (DAN), which returned -27.00% and detracted 33 bps.

Key Benefits

The Small-Cap Value strategy seeks to achieve it's objective by making intermediate and long-term investments in domestic, publicly-traded equity securities of small capitalization companies. The strategy primarily invests in companies based in the United States with market capitalization of up to $3 billion.

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

- Potential for significant alpha over a full market cycle
- Disciplined and repeatable investment process managed by a passionate and experienced investment team
- Research process specifically designed to efficiently discover smaller cap companies that are undervalued by traditional Wall Street research analysts and market participants
- Exposure to undervalued smaller cap companies offering the potential for upside as a result of the markets misinterpreation or misunderstanding of positive information signals like sock repurchase activity, dividend increases and merger activity
- Diversified portfolio with a focus on risk management

Minimum Account Size: $5 million for Institutional Account Management

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[4] As of 9/30/19 the Oberweis Small-Cap Value strategy has a current FCF Yield of 4.93%, a trailing twelve-month P/E of 12.4 vs. 15.7, a 5 yr historical earnings growth rate of 9.9% vs. 8.9%, and a 5 yr forecasted earnings growth rate of 3.6% vs 2.6%. Source: Thomson Reuters EIKON and Bloomberg

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SMALL-CAP VALUE

3Q 2019

TOP TEN HOLDINGS *(as of September 30, 2019)*			
	Company		**Line of Business**
1	Old National Bancorp	2.9%	Multi-bank holding company operating in Indiana, Illinois, Ohio, Kentucky, and Tennessee
2	Williams-Sonoma, Inc.	2.8%	Retailer of high-end home goods under Williams-Sonoma, West Elm, Pottery Barn and other retail chains
3	Central Pacific Financial Corp.	2.8%	Banking services and products operating in Hawaii
4	Physicians Realty Trust	2.6%	Self managed healthcare real estate company recently organized to acquire, selectively develop, own, and manage healthcare properties that are leased to physicians, hospitals, and healthcare delivery systems
5	Triumph Group, Inc.	2.4%	Designs, engineers, manufactures, and repairs aircraft components and services various original equipment manufacturers such as Boeing and Bombardier
6	Agco Corp.	2.0%	Manufactures and distribues agricultural equipment
7	Ryman Hospitality Properties, Inc.	2.0%	Real Estate Investment Trust that specializes in group-oriented and destination hotel assets in urban resort markets
8	Wolverine World Wide	2.0%	Manufactures and markets branded footwear and performance leathers
9	Oshkosh Corp.	1.9%	Designs and manufactures specialty commercial trucks and parts
10	Triumph Bancorp, Inc.	1.9%	Offers traditional banking products as well as commercial finance products to businesses that require specialized and tailored financial solutions

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, 2019)*	
Consumer Discretionary	10.5%
Consumer Staples	0.0%
Energy	3.8%
Financial Services	35.0%
Health Care	4.9%
Materials & Processing	8.5%
Producer Durables	17.6%
Technology	13.4%
Utilities	6.1%
Cash	0.2%
Total	100.0%

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

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SMALL-CAP VALUE

3Q 2019

AVERAGE ANNUAL TOTAL RETURNS *(as of September 30, 2019)*	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Inception (7/31/2007)
Small-Cap Value (gross of fees)	**-1.15%**	**11.54%**	**-10.10%**	**6.43%**	**5.79%**	**11.14%**	**8.29%**
Small-Cap Value (net of fees)	**-1.38%**	**10.80%**	**-11.06%**	**5.30%**	**4.58%**	**9.86%**	**7.10%**
Russell 2000 Value Index	-0.57%	12.82%	-8.25%	6.54%	7.17%	10.06%	6.07%

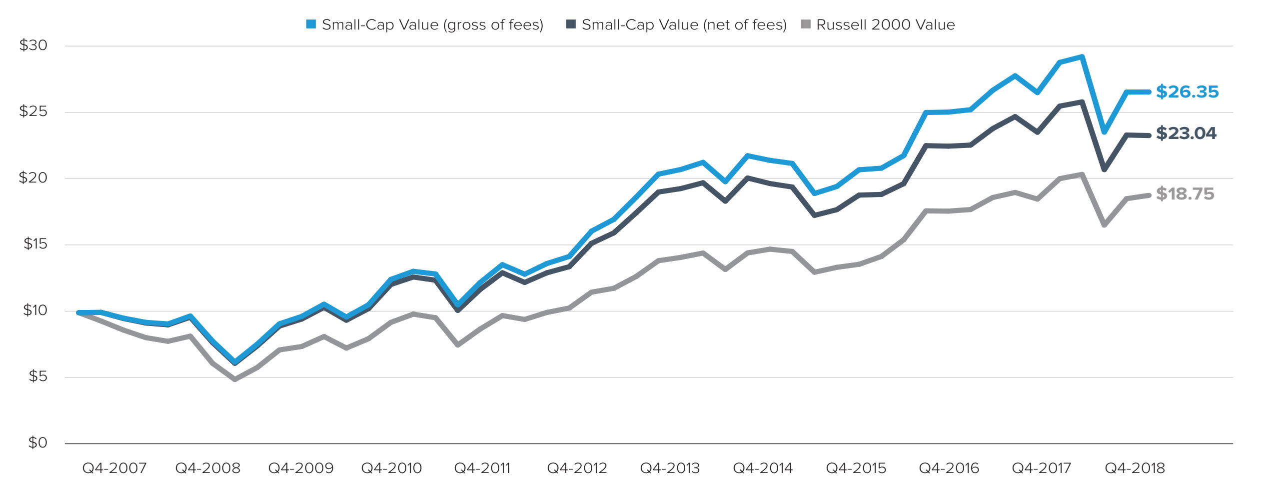
Oberweis Asset Management, Inc. ("OAM") is an independent investment management firm that is not affiliated with any parent organization. The composite returns are comprised of fully discretionary accounts with a minimum value of $5 million. Performance returns prior to October 2, 2017 were derived from another registered investment advisor. Accounts are dollar-weighted within the composite and reported in U.S. dollars.

The Russell 2000 Value Index is an unmanaged market capitalization-weighted index of value-oriented stock of U.S. domiciled companies that are included in the Russell 2000 Index. Value-oriented stocks tend to have lower price-to-book ratios and lower forecasted growth values.

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 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 MILLION — WITH INCOME INVESTED ***(July 31, 2007 – September 30, 2019)***



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.

MEET THE TEAM