

OBERWEIS MICRO-CAP FUND INSTITUTIONAL CLASS: (OMCIX) MARKET COMMENTARY

1Q 2023

The Quarter in Review

The Oberweis Micro-Cap Fund returned +9.13% versus +0.76% for the Russell Microcap Growth Index during the first quarter, an outperformance of 837 basis points.

Style and capitalization influences were particularly distinct during the period, with small-cap stocks significantly lagging large-caps and growth stocks outperforming value stocks by a solid margin¹. Micro-cap stocks fared even worse, with the smallest quintile in the Russell 2000 Growth Index and stocks with market caps under \$500 million underperforming. The lowest quintile of return-on-equity (ROE) companies and unprofitable “non-earners” in the Russell 2000 Growth Index, where we historically have had minimal exposure, again lagged². This cohort – which includes shares in biotech, software, and cloud computing companies – demonstrated irrational bubble characteristics during the zero-interest-rate policy environment and are crashing back to earth as monetary policy normalizes. We warned repeatedly about the “ZIRP bubble” and compared it to the Internet bubble we experienced early in our careers. This unwind should continue as a new generation of investors – even growth investors – realizes the importance of valuation when making investment decisions. As a result, our portfolio of higher quality micro-cap growth companies with real earnings, cash flows, and strong balance sheets has markedly outperformed.

All of this is unfolding against a backdrop that is really “A Tale of Two Markets.” While the widely-followed and top-heavy³ S&P 500 Index (the top five companies make up 21% of the index) is up nearly 18% from its low, micro-cap stocks remain in bear territory. The Russell Microcap Growth Index, for example, has been stuck in a sideways range since last June and is still down nearly 49% from its peak in early February 2021.

We contend there’s a reasonable probability the broader market – one that excludes the capitalization behemoths Apple, Microsoft, Alphabet, Amazon, and NVIDIA – is largely discounting the most anticipated economic recession in market history. Whether that recession materializes or not remains to be seen, as does the Federal Reserve’s ability to drive inflation back to its 2% long-term target. Inflation has cooled somewhat as supply chain issues moderated and transportation costs fell. Commodity prices, as broadly measured by the CRB Index, are down nearly 15% from their peak. Housing prices have started to decline in many areas. On the flip side, wage inflation isn’t offering much relief as job openings remain near all-time highs. Underlying economic activity, albeit slow, is by no means disastrous. While the ISM Manufacturing Purchasing Managers’ Index has dipped sluggishly below 50, the Services PMI remains above that watermark. The Atlanta Fed’s GDP forecast for first quarter is +1.7%, and The Conference Board is still projecting positive (although tepid) GDP growth for the full year. Furthermore, current consensus analyst estimates are projecting growth in S&P 500 operating earnings in 2023. All of this, of course, may change quickly, but it has us wondering if Fed Chairman Powell might keep rates higher for longer than anticipated as he tries to normalize the interest rate regime off zero-bound and shut the spigot of free money.

¹ The Russell 2000 Growth Index underperformed the large-cap Russell 1000 Growth Index by 830 basis points during the quarter. The Russell 2000 Growth Index outperformed the Russell 2000 Value Index by 673 basis points during the quarter.

² The lowest ROE quintile in the Russell 2000 Growth Index returned only 2.99%, the lowest-performing quintile during the quarter. “Non-earners” in the Russell 2000 Growth Index returned only 2.45% during the quarter.

³ The Top 5 names in the S&P 500 Index – Apple, Microsoft, Alphabet, Amazon, and NVIDIA – currently represent 21.3% of the Index.

AVERAGE ANNUAL TOTAL RETURNS (as of March 31, 2023)

	QTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Inception 1/1/1996	Gross/Net Expense Ratio*
Oberweis Micro-Cap Fund Institutional Class (OMCIX)**	9.13%	6.76%	42.53%	16.32%	17.00%	11.68%	1.28%/1.27%
Oberweis Micro-Cap Fund Investor Class (OBMCX)	9.07%	6.53%	42.19%	16.04%	16.72%	11.40%	1.53%/1.52%
Russell Microcap Growth Index	0.76%	-17.98%	10.87%	0.95%	5.82%	N/A	

Performance data shown represents past performance and is no guarantee of future results. Investment return and principal value will fluctuate, so that you may have gain or loss when shares are sold. Current performance may be higher or lower than quoted. Unusually high returns may not be sustainable. Visit us online at oberweisfunds.com for most recent month end performance.

The Oberweis Funds invest in rapidly growing smaller and medium-sized companies that may offer greater return potential. However, these investments often involve greater risks and volatility. Foreign investments involve greater risks than U.S. investments, including political and economic risks and the risk of currency fluctuations. There is no guarantee that the Funds can achieve their objectives.

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.

*Audited data as of December 31, 2022. Oberweis Asset Management, Inc. (OAM), the Fund’s investment advisor is contractually obligated through April 30, 2024 to reduce its management fees or reimburse OBMCX to the extent that total ordinary operating expenses, as defined, exceed in any one year the following amounts expressed as a percentage of each Fund’s average daily net assets: 1.8% of the first \$50 million; plus 1.6% of average daily net assets in excess of \$50 million and for OMCIX 1.55% of the first \$50 million; plus 1.35% of average daily net assets in excess of \$50 million.

**Institutional Class shares OMCIX performance information was calculated using the historical performance of Investor Class shares for periods prior to May 1, 2017.

The Oberweis Funds are distributed by Oberweis Securities, Inc. Member: FINRA & SIPC.

The Russell Microcap Growth Index measures the performance of those Russell Micro Cap companies with higher price-to-book ratios and higher forecasted growth values. The performance data includes reinvested dividends.

The Russell Microcap Index is represented by the smallest 1,000 securities in the small cap Russell 2000 Index plus the next 1,000 securities. Each index is an unmanaged group of stocks, whose performance does not reflect the deduction of fees, expenses or taxes.

The Quarter in Review (continued)

If that's the case, we believe it's an environment that favors fundamental stock pickers, and are confident our differentiated approach focusing on companies generating better-than-expected earnings growth driven by transformational fundamental change can yield above-market performance. When the economic outlook eventually brightens (and we don't profess to know when, just that it will), we also believe the Fund is particularly well-positioned for a few very important reasons. First, within the small-cap universe (of which micro-cap is a subset), valuations of our preferred higher quality companies remain relatively attractive. According to research by Jefferies, the highest ROE small-cap names trade for just 1.2x sales, while the lowest ROE companies trade for 4.5x, still well above their bottom of 2x in 2003 (the portfolio is nearly 25% invested in the highest ROE quintile and 81% in the top 3 quintiles). We think it makes sense to invest in higher ROE companies to begin with, and the valuation spread makes the proposition even more compelling. Second, small-cap stocks trade at the largest discount relative to large-caps we've seen since 2000, as some investors appear to be "hiding" defensively in the market's biggest names. Historically, top-heavy concentration in the S&P 500 Index has reversed, and we expect this time will be no different, providing a relative tailwind to small-caps and micro-caps as mega-cap darlings and other large caps flounder. Finally, periods of heightened uncertainty often represent the best times to invest in this strategy as forward expectations are abnormally low. This provides a natural tailwind to our "relative-to-expectations" growth strategy. Again, while making macroeconomic projections is not part of our investment process, we are pretty confident that – based on our experience – an economic inflection will be a boon for our portfolio holdings.

Fund Highlights

As of March 31, 2023, the Fund was 96.1% invested in 78 different positions. The Fund had its largest over-weightings in technology (32.6% average weighting during the quarter versus 16.3% for the Russell Microcap Growth Index) and consumer discretionary (11.8% versus 9.1%). The Fund was most underweight healthcare (13.1% versus 27.6%), producer durables (18.3% versus 24.7%) and financial services (6.3% versus 8.0%).

Performance in the first quarter was positively impacted by stock selection in technology (where our holdings returned 20.36% versus 7.89% for the benchmark's technology holdings), healthcare (17.75% versus -2.44%), producer durables (7.45% versus 1.51%), and consumer discretionary (11.73% versus 6.04%). Our stock selections in energy slightly detracted from performance during the quarter.

Organization Update

There was no change to the team during the quarter.

Oberweis Asset Management Investment Philosophy

We believe that investing in smaller companies driving revenue and earnings growth in excess of expectations results in superior investment performance over long periods of time. We believe that innovation is the key to economic growth and wealth creation and are committed to investing in companies at the forefront of innovation – smaller company stocks that offer the potential for extraordinary revenue and earnings growth.

The entrepreneurial spirit is alive and well at these companies. Many are nimble and uniquely address the needs of their customers with patented new products and services. Successful investing, however, demands more than finding companies with good growth prospects. We must also buy these stocks for our clients at prices that make sense. By paying careful attention to companies' valuations in relation to expected earnings growth rates, we seek to purchase stocks when they still have considerable appreciation potential.

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