Oberweis
Asset Management

INTERNATIONAL OPPORTUNITIES MARKET COMMENTARY

3Q 2023

Portfolio Performance

During the third quarter, the International Opportunities Strategy returned -5.71% (-5.93% net of fees) vs. -5.93% for the benchmark, the MSCI World Ex USA Small Cap Growth Index. Year-to-date, the strategy has returned -1.56% (-2.22% net of fees) vs. -0.55% for the benchmark. While any strategy may out- or underperform in the short-term, the International Opportunities Strategy has delivered strong medium- and long-term results. For example, it has outperformed since the beginning of Covid, as measured as of 12/31/2019, with a positive return of +7.60% (+4.03% net of fees) vs a negative return of -2.90% for the benchmark.

The strategy's long-term alpha generation is high. Since inception, the strategy has significantly outperformed its benchmark and has returned a strong cumulative +288.48% (+234.57% net of fees) vs. only +76.74% for the benchmark.

All that said, we recognize the recent short-term underperformance after extremely strong outperformance during the early days of Covid. Our team and process have not changed. However, the rapid rate of interest rate increases has been a significant headwind for our investment style that, after all, identifies misunderstood future earnings, which then get discounted more regardless of the strength of the underlying company fundamentals. As a result, we have seen considerable multiple compression among our portfolio holdings. This has hurt performance over the trailing two years.

While performance hence has been style-consistent, this multiple compression has also historically set the stage for some of our all-time best buying opportunities. It would not surprise us if the present yet again turns out to be one of those times. Valuations are among the cheapest we have ever seen. At some point, we expect that economic growth expectations will become less pessimistic and the rise in interest rates will slow down. When investors begin to discount such events, depressed valuation multiples will normalize, and that pivot point tends to be extremely favorable for our investment style. This shift can occur rapidly. While we cannot control yearly economic gyrations, we can and do focus on the underlying cash generation strength of our portfolio companies. While that means performance may vary in the short-term, our strong long-term track record demonstrates our ability to generate high alpha over a full market cycle.

Market Environment Review

After a positive start in July, developed markets weakened over the subsequent two months to finish lower for the quarter. The biggest concern for investors has been the consistent increase in U.S. Treasury yields, with the increase most pronounced at the long end of the curve (maturities longer than five years out), a dynamic also reflected in the UK and Euro area. In the last six months, 10-year U.S. Treasury yields have increased by approximately 150bps and closed the quarter near 16-year highs. Inflation expectations have not been increasing, so real rates, which is to say yields less inflation expectations, have also appreciated materially.

Federal Reserve Chairman Jerome Powell at the September U.S. Fed meeting clearly indicated a bias towards a more restrictive policy and a "higher-for-longer" approach to interest rates. The rise in real rates seems in part a reaction to the resilience of the economy and labor market, along with the magnitude of the Federal government's financing needs. Perhaps counter-intuitively, the increase in rates has occurred while the inflation trend has become more benign.

Supply chain pressures have reversed, and supply has caught up with demand in the U.S. apartment rental market, boding well for the shelter component of CPI. The tightness of the labor market remains a risk to the disinflation narrative; however, wage pressures appear to be moderating. In particular, the increase in immigration has impacted on the low end of the labor market, and wage growth premia enjoyed by job switchers vs stayers has been coming down. The core PCE price index, a measure watched very closely by the Fed, rose 0.14% in August from July. The three month annualized core inflation rate was +2.2%.

AVERAGE ANNUAL TOTAL RETURNS ***(as of September 30, 2023)***

	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Since Inception 2/1/2007
International Opportunities (gross of fees)	**-5.71%**	**-1.56%**	**11.30%**	**-6.94%**	**1.01%**	**6.17%**	**8.48%**
International Opportunities (net of fees)	**-5.93%**	**-2.22%**	**10.31%**	**-7.78%**	**0.10%**	**5.22%**	**7.52%**
MSCI World ex-US Small-Cap Growth Index	-5.93%	-0.55%	12.96%	-3.15%	0.51%	4.31%	3.48%

Past performance is not necessarily indicative of future results. Performance is historical and includes the reinvestment of dividends and other income. Unusually high returns may not be sustainable. The strategy invests 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. Net-of-fee composite returns are calculated using the highest model investment advisory fees applicable to portfolios within the composite. Advisory fees are disclosed in Part II of Form ADV.

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 $5 million. Performance results from 2-1-07 until 7-31-08, were derived solely from the performance of the Oberweis International Opportunities 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 MSCI World ex-US Small-Cap Growth Index (Net) is a free float-adjusted market capitalization weighted index that is designed to measure the performance of small cap growth developed markets excluding the U.S. with minimum dividends reinvested net of withholding tax. It is not possible to invest directly in an index.

Market Environment Review (continued)

Internationally, the softening inflation trends in the U.S. have been mirrored. Euro area core inflation fell to +4.5% year-on-year in the September report, below consensus. However, the macro data has indicated a widening performance gap between the U.S. and Euro Area economies, especially Germany and Italy where manufacturing data has been disappointing. With U.S. rates still elevated vs German rates, and with expectations that the ECB will not hike further beyond the next meeting, the dollar has been strong and European assets broadly underperformed.

Earnings in the Euro Area have remained resilient, even though higher interest rates have proven more effective at slowing economic activity than in the U.S. In fact, Europe has been the region with the best earnings revisions over the last year with net margins holding up well. That is a good combination for our investment strategy: low investor expectations followed by data that is not as bad as feared. It is much easier to find companies with the potential to beat expectations when expectations are much lower-than-normal. Stock valuations are a reflection of future expectations and for our universe of Euro Area small-caps, valuations remain far below historical averages, which we believe increases the odds of strong future returns.

In Japan, a series of corporate governance reforms announced at the beginning of the year by the Tokyo Stock Exchange encourages listed companies to improve capital efficiency. This appears to have been highly impactful, with companies increasing efforts to address some of the long-standing issues that have plagued them in the past. These government reforms likely represent a marked turning point, and are part of a coordinated approach by policy makers to get both foreign investors and Japanese households to increase their exposure to Japanese equities. If successful, the impact on supply and demand would be material.

Outlook

The outlook for the change in the second derivative in real interest rate changes is currently, in our opinion, the most critical factor impacting capital markets. After 22 months of monetary tightening and positive economic surprises, it looks like markets have accepted that the economy is in fact far less rate sensitive than was initially presumed. Thus, the steepening yield curve reflects a belief that the economy is not going to crack under the weight of tighter policy. The increased discount rate has already contributed to near-historically low valuations for non-U.S. equities:

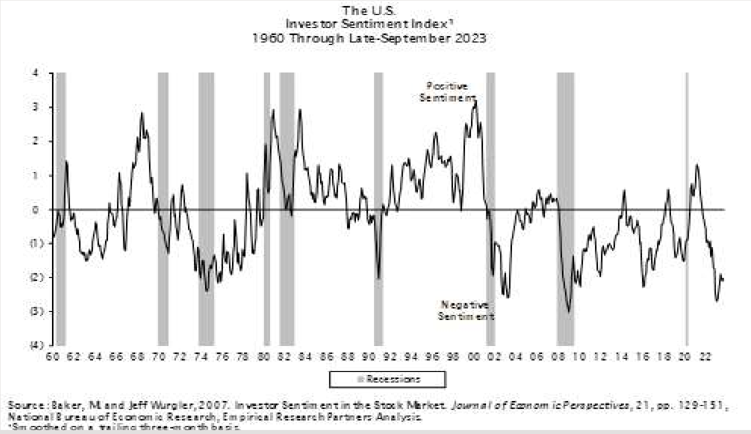
However, this is backward-looking. What matters to forward equity returns is whether rates will increase substantially from here or not relative to investor expectations. Should the rate of change in interest rates changes (i.e. the second derivative) slow down from here, this would, in our experience, have a positive effect on forward equity returns. Similar to the attractive earnings-based valuation across our investible universe, free cash flow yields in ex-U.S. developed markets remain near historical highs:

INTERNATIONAL OPPORTUNITIES MARKET COMMENTARY

3Q 2023

Outlook (continued)

Further, investor sentiment and expectations for forward returns remain among the lowest they have ever been. Counter to common investor behavior, which tends to shy away from deploying new capital when consensus opinion becomes fearful, our experience has shown that attractive valuations and near-trough expectations have generally made a favorable set-up for forward-looking long-term returns.



Our primary focus continues to be investing in strong companies with great underlying fundamentals, balance sheets and cash flows. Our holdings tend to be niche-oriented firms operating in disruptive markets. GDP matters, but it generally is not the main driver of long-term earnings growth for our holdings. In that regard, our portfolio companies had, in aggregate, a solid set of earnings reports with strong underlying fundamentals. We are confident that whether the market goes up or down from here in the short-term, on a relative basis, the underlying fundamentals of our companies will continue to do well.

Portfolio Highlights

At quarter-end, the portfolio was invested in 65 stocks in 14 countries. Our top five country weightings (portfolio weighting vs. the MSCI World Ex USA Small Cap Growth Index) at quarter end were United Kingdom (21.6% vs. 14.0%), Japan (20.3% vs. 29.6%), Canada (14.2% vs. 9.4%), France (10.2% vs. 3.6%), and Germany (7.5% vs. 4.3%). On a sector basis, the portfolio was overweight industrials (26.5% vs. 22.6%) and underweight real estate (0.0% vs. 4.5%).

Organization Update

There are no changes to the International team or strategy.

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.

For more information please contact:
Brian K. Lee, Director of Marketing & Client Service
(800) 323-6166 | (630) 577-2321 |
brian.lee@oberweis.net

Marc Carlson, Director Marketing & Client Service
(800) 323-6166 | (630) 577-2364 |
marc.carlson@oberweis.net

Oberweis Asset Management, Inc.
3333 Warrenville Rd., Suite 500, Lisle, IL 60532