Oberweis
Asset Management

# EMERGING MARKETS MARKET COMMENTARY

4Q 2023

## The Quarter in Review

The Oberweis Emerging Markets strategy climbed 6.96% (6.73% net of fees) during the fourth quarter of 2023 and 16.78% (15.53% net of fees) for the full year. The MSCI Emerging Markets Small-Cap Index, which serves as our benchmark, returned 8.95% and 23.92% for the quarter and year, respectively. Looking at a much longer time horizon, we have generated a 7.72% (6.45% net of fees) annualized return since the strategy's June 2018 inception, which compares favorably to the benchmark's 5.29% annualized return over that same time period.

Emerging markets small-caps had a weak start to the quarter before moving decisively upward at the beginning of November when U.S. Federal Reserve Chairman Jerome Powell suggested interest rates were at their peak. After falling nearly 5% during September, the MSCI Emerging Markets Small-Cap Index climbed 14.4% over the last two months of the year. Even so, emerging markets small-cap stocks relatively underperformed most other major global indexes in the fourth quarter, including the S&P 500, Russell 2000 and the MSCI All-Country World Index. For the full year, however, only the S&P 500 outperformed the MSCI Emerging Markets Small-Cap Index, and that outperformance was driven by a small group of companies. Excluding the so-called Magnificent Seven (Tesla, Meta, Nvidia, Amazon, Alphabet, Microsoft and Apple) from the S&P 500, the small-cap emerging markets index had twice the return of the remaining 493 S&P stocks. The bottom line is that emerging markets small-cap stocks had a good year in both absolute and relative terms.

We think the strong performance of small-cap emerging markets stocks deserves wider recognition. The typical market narrative is that rising interest rates and a strong U.S. Dollar are generally disastrous for emerging markets. There was certainly no shortage of articles and investment-strategy pieces predicting EM carnage as the current interest rate hiking cycle got started two years ago. Once upon a time, the doomsayers would probably have been correct. This time around, however, emerging markets have handled rising interest rates and U.S. Dollar strength with remarkable resiliency. Over the past quarter century, developing countries have cleaned up their balance sheets, reduced foreign currency exposure and strengthened their banking systems, improving their economic resiliency. Even so, the MSCI Emerging Markets Small-Cap Index is trading at Bloomberg-compiled forward P/E multiples that are lower than its 15-year historical average while the S&P 500 and the globe-spanning MSCI All-Country World Index are trading at substantial premiums to their historical averages. We think the market will eventually reward the developing world's improved durability. In the meantime, we have the opportunity to invest in excellent businesses at valuations we believe are unreasonably cheap.

Turning to the portfolio, country allocation added 11 basis points to relative performance, while stock selection subtracted 85 basis points. China was the biggest drag, reducing relative performance by 124 basis points almost equally divided between allocation—an overweight position in underperforming China—and stock selection. Looking at the portfolio from a sector perspective, stock selection subtracted 114 basis points from relative performance. Sector allocation added 39 basis points. Information Technology added the most to relative performance. The Industrials sector was the biggest detractor from relative performance.

**AVERAGE ANNUAL TOTAL RETURNS *(as of December 31, 2023)***

| | QTD | 1 YR | 3 YR | 5 YR | Since Inception 6/1/2018 |
|---|---|---|---|---|---|
| **Emerging Markets (gross of fees)** | **6.96%** | **16.78%** | **1.30%** | **13.34%** | **7.72%** |
| **Emerging Markets (net of fees)** | **6.73%** | **15.53%** | **0.03%** | **12.06%** | **6.45%** |
| MSCI Emerging Markets Small-Cap Index | 8.95% | 23.92% | 6.45% | 9.92% | 5.29% |

**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 6-1-18 to present, are derived solely from the performance of the Oberweis Emerging Markets 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 Emerging Markets Small Cap Index is a free float-adjusted, market capitalization-weighted index that measures the performance of small-cap stocks in 24 emerging markets. It is not possible to invest directly in an index.*

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## Outlook

We remain excited about the investment potential in emerging markets. We believe the drive of people who live in the developing world to live better, healthier, and more productive lives is inexorable. Moreover, we continue to believe that drive will fuel structural growth in spending on consumer goods and healthcare, as well as investments in infrastructure and automation. Our strategy to invest in prudently managed and competitively advantaged companies that are positioned to benefit from that long-term structural growth remains unchanged.

We also continue to believe that emerging markets equities are attractively valued. According to data compiled by Bloomberg, the MSCI Emerging Markets Small-Cap Index traded at a forward price-to-earnings multiple of 14.7 times at the end of the quarter, which is slightly lower than the average forward multiple over the past 15 years and compares favorably to other indexes. Bloomberg reports that the globe spanning MSCI All Country World Index (ACWI) trades at 18.6 times forward earnings while the S&P 500 trades at 22.1 times, which are material premiums to those indexes' 15-year historical averages. Given the comparatively attractive long-term growth opportunities we see for smaller companies in developing markets, we think the lower valuation multiple is attractive.

## Portfolio Highlights

At quarter-end, the portfolio was invested in 69 stocks domiciled in 20 countries. Our top five country weightings (portfolio versus the MSCI Emerging Markets Small-Cap Index) were India (21.7% vs. 25.6%), Taiwan (14.2% vs. 22.4%), South Korea (13.3% vs. 13.4%), Brazil (8.9% vs. 5.3%), and China (8.7% vs. 7.1%). The strategy's largest overweight sectors were Information Technology (31.9% vs. 17.6%), Consumer Staples (12.0% vs. 6.5%), and Consumer Discretionary (16.7% vs. 11.6%). The largest underweight sectors were Materials (0.8% vs. 12.4%), Industrials (10.9% vs. 16.8%) and Real Estate (1.8% vs. 6.2%).

## Organization Update

There were no organizational changes during the quarter.

## Oberweis Asset Management's Investment Phillosophy

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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