Oberweis
Asset Management

EMERGING MARKETS MARKET COMMENTARY

2Q 2024

The Quarter in Review

The Oberweis Emerging Markets strategy climbed 1.07% (0.77% net of fees) during the second quarter of 2024. The MSCI Emerging Markets Small Cap Index, which serves as our benchmark, climbed 5.93%. Looking at a much longer time horizon, we have generated a cumulative total return of 54.7% (43.89% net of fees) since the strategy's June 2018 inception, compared to the benchmark's 42.7% return over that same time period.

India and Taiwan drove the index's strong performance during the quarter. Stocks from those two countries make up nearly half of the total index. Indian small caps, which constitute almost 27% of the benchmark, climbed nearly 20% during the quarter, largely thanks to a strong rally after the national election in early June. Prime Minister Narendra Modi and his party fell short of an outright majority, but still held onto power much to the market's relief. Taiwan small caps were weak during the first three weeks of the quarter before turning sharply higher after Nvidia reported strong earnings. Much of the global semiconductor supply chain calls Taiwan home and a rally in that sector helped boost that country's small caps by more than 6% for the quarter.

We failed to keep pace with the index because of our relative country weights. Parsing our returns by country, stock selection added 92 basis points, but country allocation subtracted 601 basis points. As we mentioned, India and Taiwan are by far the largest country weights in the index and were clear outperformers. We were underweight both countries. At the same time, we were overweight Mexico and Brazil, which were amongst the worst performing countries in the benchmark. In Mexico, the left-wing Morena party's electoral success spooked investors, while Brazilian equities continued to struggle with persistently high interest rates.

While stock selection helped us in country-attribution terms, it was the main driver of underperformance if we analyze returns by sector, reducing relative performance by 420 basis points. Even there, however, the performance shortfall was largely a country-allocation phenomenon. The negative contribution from stock selection was almost entirely from Industrials, Financials, Consumer Discretionary, Energy, Communication Services and Information Technology. In each case, our sector underperformance was driven by what we owned in Mexico or Brazil, the poorly performing countries, or what we didn't own in India or Taiwan.

We are fundamental, bottom-up investors. We don't buy or sell shares based on top-down, country- or sector-level opinions. We focus exclusively on companies that we believe have durable balance sheets, reliable growth opportunities, sustainable competitive advantages and clean corporate governance. We try to buy those companies when they trade for less than they are worth. That last point is key. Company-specific valuation opportunities are often found in out-of-favor countries. When countries are well loved by investors, valuations tend to be less attractive. For us, that is the source of many opportunities. We are happy to invest in outstanding businesses in temporarily unloved countries.

Sometimes, however, the lovefest can go on and on, which can be a performance headwind for us. That has definitely been the case with India, which has been a relative-performance thorn in our side for many quarters. The topic of India warrants a longer discussion. It is our single largest country weight, making up 16.2% of the portfolio on average during the second quarter, but we have not found enough attractive opportunities in that country to get close to the benchmark's almost 27% weighting. It is not for lack of trying. We have scoured India looking for firms that have all the quality and durability attributes we look for, and that also trade at a fair price. We have found plenty of great businesses, but precious few that trade at attractive valuations.

To be frank, until something changes in India, we expect to be structurally underweight that country. We are simply not going to buy shares that are overpriced in hopes that someone comes along tomorrow and pays an even bigger premium to their fair value. However, we do expect something to change in India. The MSCI India Small Cap Index trades at 29.4 times forward earnings estimates as compiled by Bloomberg. For comparison purposes, The MSCI Emerging Markets Small Cap Index trades at 15.4 times forward earnings and, again, more than a quarter of that index is invested in comparatively high-multiple Indian equities. According to ICRA, Moody's Indian subsidiary, the total amount of margin debt for stock purchases hit an all-time high in January of 2024 and was four times larger than it was in January 2020, growing twice as fast as the overall stock market. We don't have hard numbers for the amount of shares that have been pledged by individual investors as collateral for personal loans, but India's central bank, the Reserve Bank of India (RBI), expressed concern in April about the amount of "loans against shares" that banks have made and barred one bank, JM Financial, from extending any more debt collateralized with stocks. The Indian equity options market is now larger than the U.S.'s options market, and according to India's National Stock Exchange, retail investors make up 35% of the options volume. The notional volume of equity derivatives traded in India reached $6 trillion dollars earlier this year, six times higher than it was at the beginning of 2022. From our perspective, all of this helps explain why it is hard for us to find opportunities in that market and also why that market could hit some turbulence. The leverage built up in the Indian market could quickly turn a slip into a fall. We will be ready to scoop up bargains if they appear.

AVERAGE ANNUAL TOTAL RETURNS ***(as of June 30, 2024)***

	QTD	YTD	1 YR	3 YR	5 YR	Since Inception 6/1/2018
Emerging Markets (gross of fees)	**1.07%**	**2.14%**	**6.72%**	**-3.18%**	**10.51%**	**7.43%**
Emerging Markets (net of fees)	**0.77%**	**1.52%**	**5.52%**	**-4.43%**	**9.25%**	**6.16%**
MSCI Emerging Markets Small-Cap Index	5.93%	7.04%	20.04%	2.54%	9.99%	6.02%

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.

The Quarter in Review (continued)

Outside of India and, to a lesser extent, Taiwan, we are finding opportunities galore. Those two countries constitute half the index and trade at 29.4 times and 20.3 times forward earnings, respectively. Almost all of the remaining emerging markets countries trade around 10 times forward earnings or less. They may not have the cache that India and Taiwan currently enjoy, but the rest of the countries in the emerging markets universe hold plenty of excellent businesses trading at incredibly attractive prices. It is a world of opportunity for patient investors.

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 15.4 times at the end of the quarter, which is in line with its 15-year average. The benchmark's forward multiple compares favorably to other indexes. Bloomberg reports that the globe-spanning MSCI ACWI trades at 18.9 times forward earnings while the S&P 500 trades at 22.6 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 59 stocks domiciled in 18 countries. Our top three country weightings (portfolio versus the MSCI Emerging Markets Small Cap Index) were India (16.2% vs. 26.6%), South Korea (14.6% vs. 12.8%), and China (11.7% vs. 9.0%). The strategy's largest overweight sectors were Consumer Staples (14.0% vs. 6.2%) and Consumer Discretionary (15.4% vs. 11.5%). The largest underweight sectors were Materials (0.9% vs. 11.8%) and Real Estate (1.3% vs. 5.9%).

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.

Characteristic Definitions:

Forward Earnings: This is an estimate of a company's earnings for upcoming periods; usually the completion of the current fiscal year and the following fiscal year.

Forward P/E (Price to Earnings) Ratio: This is a measure of valuation. It divides the current share price of a company by the estimated future ("forward") earnings per share (EPS) of that company.

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