BRIDGES | INVESTMENT MANAGEMENT

Think Forward

July 27th , 2018

Total returns for various stock and bond indexes for the second quarter, the first six months of 2018, and the last twelve months are summarized in the following table:

Index	Second Quarter	Trailing 6-Mo	Trailing 12-Mo
S&P 500	3.43%	2.65%	14.36%
S&P 400 Midcap Index	4.29%	3.49%	13.53%
S&P 600 Small Cap Index	8.77%	9.37%	20.41%
MSCI World Index Ex U.S.	-2.32%	-3.49%	7.79%
Barclays U.S. Aggregate Bond Index	-0.16%	-1.62%	-0.40%

Past performance is not a guarantee of future results. Index performance is not illustrative of fund performance. Please call 1.866.934.4700 for fund performance.

U.S. stocks posted moderate gains in the second quarter, leading to positive returns for the first half of 2018, and solid total returns over the last twelve months. International equities, after a strong 2017, struggled in the second quarter and in the first half of 2018. Small cap equities were the best performing asset class during the second quarter, the first half of 2018, and over the past twelve months.

Stock price volatility increased materially during the first half of 2018. The volatility was driven by: 1) continued monetary tightening by the Fed, 2) growing concerns about the effects of trade sanctions implemented by the Trump Administration, and 3) growing concerns regarding the sustainability of the corporate profit growth during the second half of 2018 and into 2019.

Bonds struggled during the second quarter as the Federal Reserve continued to signal a less accommodative policy as the current economic cycle shows ongoing strength. Bond returns were marginally negative during the quarter, and were also slightly negative during the first half of 2018, and over the past twelve months.

Despite increased price volatility, stocks have worked higher on balance in 2018 primarily because of continued solid earnings growth. First quarter earnings results were decidedly positive, both on a year-over-year basis, and relative to consensus expectations. U.S. corporations continue to show solid underlying financial performance, and consensus earnings expectations have moved higher over the past few months as investors consider the positive impact of the corporate tax cuts enacted in late December of 2017.

In our view, the level, quality and trajectory of corporate earnings remain the most important variables in order for the equity market to show continued progress in the second half of 2018, and into 2019. We expect corporate earnings will show solid growth over the next several quarters, although year-over-year earnings comparisons will become more difficult in coming quarters.

Stocks remain somewhat below our estimate of “fair value.” At present, we believe year-end 2018 fair value for the S&P 500 is approximately 3,000, based on a P/E of 18.5x consensus estimated earnings for 2018 of $160 per share. Our fair value estimate implies upside potential of about 10% from the S&P 500’s second quarter ending value of 2,718. We believe fair value for year-end 2019 is approximately 3,250, based on a P/E of 18.5x consensus estimates of $175 per share for 2019.

We believe equities are currently priced to provide mid-to-high single digit returns from current levels over the next several years, albeit with continued elevated levels of volatility. We would not be surprised if U.S. equities traded 15-20% lower, 15-20% higher, or both, over the next 12-18 months. A material decline in stock prices from current levels would create good long-term value in our view and represent an attractive level to commit capital to equities; conversely, we would be inclined to reduce commitments to stocks in the event of a 15-20% increase in stock prices in the short term, which would materially diminish implied forward returns for stocks.

We would use a meaningful correction from current stock price levels to add to or initiate positions in companies that we believe offer compelling long-term returns based on their valuations and prospects for solid long-term business value growth. As the current economic expansion ages, it will be important to own companies that are well-positioned for the next economic slowdown, in terms of the quality, durability, and growth potential of their business franchise.

Bonds remain both absolutely and relatively unattractive in our view, because 1) interest rates remain low relative to historic norms, and 2) we believe the probabilities favor an eventual return to higher interest rates over the next several years, likely driven by gradually higher inflation expectations. We would become more positive on bonds once yield levels increase to the point where they exceed long-term inflation expectations by 1% or more. The yield curve has flattened over the past year (as the spread between the 2- and 5-year Treasuries have narrowed relative to the yield on the 10-year Treasury); we are beginning to see better opportunities in fixed income as rates have drifted higher in the middle segment of the yield curve (two to seven years) on balance over the past several quarters.

Given our continued constructive intermediate to longer-term view toward equities, and our continued defensive approach to bonds, we remain over-weighted in stocks and underweighted in bonds relative to specific target asset allocations in client portfolios.

As always, we also encourage you to contact us if you would like to discuss our outlook for the remainder of 2018, and/or your portfolio in detail.

Sincerely,

Edson L. Bridges III, CFA CEO

Earnings growth is not representative of the fund’s future performance.

The S&P 500 Index is a broad based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general.

The S&P MidCap 400 Index, more commonly known as the S&P 400, is a stock market index from S&P Dow Jones Indices. The index serves as a barometer for the U.S. mid-cap equities sector and is the most widely followed mid-cap Index in existence.

The S&P 600 SmallCap Index measures the small cap segment of the U.S. equity market.

The MSCI World Index – ex U.S. is a stock market index of 1,643 'world' stocks. It is maintained by MSCI Inc., formerly Morgan Stanley Capital International, and is used as a common benchmark for 'world' or 'global' stock funds. The index includes a collection of stocks of all the developed markets in the world, as defined by MSCI.

The Barclays U.S. Aggregate Bond Index is a broad based index maintained by Barclays Capital, and is often used to represent investment grade bonds being traded in the United States.

P/E, price-earnings ratio, is the ratio for valuing a company that measures its current share price relative to its per-share earnings. The price-earnings ratio can be calculated as: Market Value per Share / Earnings per Share.

A yield curve is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates. The most frequently reported yield curve compares the three-month, two-year, five-year and 30-year U.S. Treasury debt. This yield curve is used as a benchmark for other debt in the market, such as mortgage rates or bank lending rates, and it is also used to predict changes in economic output and growth.

The Bridges Investment Fund is distributed by Quasar Distributors, LLC.

It is not possible to invest directly in an index.

Opinions expressed herein are those of Edson L. Bridges III and are subject to change. They are not guarantees and should not be considered investment advice.

Mutual fund investing involves risk. Principal loss is possible. Small and medium capitalization companies tend to have limited liquidity and greater price volatility than large-capitalization companies. Investments in debt securities typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. The Fund invests in foreign securities which involve political, economic and currency risks, greater volatility and differences in accounting methods.

The Fund’s investment objectives, risks, charges, and expenses must be considered carefully before investing. The statutory and summary prospectus contains this and other important information about the investment company; any may be obtained by calling 1.866.934.4700 or by visiting www.bridgesfund.com. Read it carefully before investing.