BRIDGES | INVESTMENT MANAGEMENT

January 4, 2019

Below is our Market Commentary as of the fourth quarter ending December 31, 2018.

Key takeaways include:

1. Global equity markets had their worst quarter since 2008, and the worst December since 1931, as stocks sold off sharply due to a variety of concerns, including slowing corporate earnings growth, recession risk, hawkish Fed policy, and uncertainty around trade negotiations with China.

2. Despite strong corporate earnings growth domestically, U.S. stocks posted their first negative year since 2008 as stock price volatility increased sharply returning to more normal historical levels.

3. Equity valuations contracted materially in the fourth quarter; the S&P 500 currently trades 15% below our estimate of "fair value." While we expect continued volatile capital markets conditions, we believe implied forward total returns for stocks are attractive (7-9% annualized) over the next five years.

4. A down year for stocks was uncharacteristically also a down year for bonds. The yield on the 10-year U.S. Treasury note rose 27.6 basis points, its largest annual rise since 2013. Yields and debt prices move in opposite directions. We believe that stocks remain more attractive than bonds for investors with long-term investment horizons (five to ten years, or longer).

The following table summarizes total returns for a range of asset classes for the fourth quarter of 2018, full year 2018, and since year-end 2008, which marked the approximate bottom of the 2008-09 financial crisis:

Index	Q4	2018	Annualized Since 2008	Cumulative Since 2008
S&P 500	-13.52%	-4.39%	13.10%	242.75%
S&P 400 Midcap Index	-17.28%	-11.10%	13.65%	259.85%
S&P 600 Small Cap Index	-20.12%	-8.52%	13.56%	256.95%
MSCI World Index Ex U.S. Index	-11.45%	-13.80%	7.12%	99.03%
MSCI Emerging Markets Index	-7.85%	-13.32%	8.35%	123.13%
Barclays U.S. Aggregate Bond Index	1.64%	0.01%	3.48%	40.75%

Source: Bloomberg

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.

Volatility returned to the capital markets with a vengeance in 2018, after an uncharacteristically placid 2017. Downside volatility was especially pronounced in late January – early February, when the SP&P 500 declined 12% in eight trading days. Stocks moved steadily higher through the end of the third quarter, propelled by strong corporate earnings growth.

However, equities sold off sharply in early October, initially as a reaction to hawkish comments from new Federal Reserve Chairman Jerome Powell. While Mr. Powell moderated his stance later in the quarter, the market began to discount a more restrictive Fed policy going forward. Investors also focused on a variety of other risks in the quarter, ranging from concerns about the trajectory of future earnings growth (specifically, concerns that third quarter earnings may mark the high-water mark for year-over-year earnings growth in this cycle), the onset of recession, trade and tariff risks, softening global economic data, and continued dysfunction in Washington.

The fourth quarter was the worst quarter for stocks since 2008, and equities posted their worst December since 1931. The S&P 500 declined -20.2% between October 2nd and December 26th which technically qualifies as a “bear market” (equity price decline of at least -20%), with many stocks declining -25% to -30% or more from their 52-week highs. While the SPX rallied +6.5% over the last four trading days of the year, the Index ended the year with a total return of -4.39%, its first negative year since 2008.

In 2018, our companies generally had financial performance that was better than the performance of their stock prices. Consequently, equity valuations contracted to levels that we believe are attractive given a multi-year investment horizon. We will continue to look for opportunities to own excellent business franchises that have a demonstrated ability to grow intrinsic business value for shareholders across a range of economic conditions. The decline in stock prices in the fourth quarter has significantly increased our opportunity set, as valuations have contracted, improving long-term implied returns.

The salient risks that impact the outlook for 2019 are the same as those that contributed to the capital markets volatility in the fourth quarter:

1. Corporate earnings growth is likely to slow in 2019, as the positive impact of the 2017 corporate income tax cut begins to recede. In our view, company management commentary coincident with the release of fourth quarter earnings in January will be more important than usual, given the market’s reaction to third quarter earnings, which were generally in line with expectations, but which in many cases were viewed as “not good enough” and/or were accompanied by tepid forward commentary by management.

2. Economic data showed some softening during the fourth quarter; investors will be keenly attuned to data points that may suggest the onset of the next recession as the first half of 2019 unfolds.

3. The Fed's response to economic data in the first half of 2019 will be critical; a continued hawkish stance, especially in the face of softer economic data, would likely result in periods of material stock price weakness.

4. Trade policy with China will also be an important factor impacting capital markets; further political dysfunction and uncertainty emanating from Washington is also a key risk factor in the first half of 2019.

The critical question for investors at the outset of 2019 is whether the fourth quarter stock decline is signaling the onset of the next recession, or whether the recent stock price action represents a normal correction within the context of a continuation of the current economic expansion.

Although the current economic expansion is the longest on record, its pace has been relatively slow by historic standards. While economic data has shown signs of softening since mid-2018, there are few indications that a recession is imminent, but we do believe that the odds of a recession in the next 12-24 months have increased materially over the past two quarters.

We take a very long view toward asset class valuation and modeling to establish a framework for future implied returns. Modeling future returns for assets is inherently difficult, especially for assets that are volatile, such as equities. A recession in the next 12-24 months would almost certainly lead to disappointing returns for stocks in the near-term but would likely lead to better than average returns during the ensuing economic recovery.

We believe that is important to focus on long-term asset class returns and understand how valuations and normalized asset class price volatility may affect returns over a five-and ten-year investment horizon.

We believe the outlook for bond returns going forward remains relatively unattractive because 1) nominal and real interest rates remain near historic lows, and 2) the Fed appears intent on raising rates for the time being. We expect that interest rates are likely to continue to work higher on balance in 2019; we believe that the ten-year Treasury could end 2019 near 3.50%, with an outside target of 3.75%. If rates do not work higher in 2019, bond returns would likely approximate their coupons.

We remain defensively positioned in fixed income portfolios, but we will look for opportunities to extend bond portfolio durations as interest rates move higher. The current flat shape of the yield curve provides little incentive to take on interest rate risk. We would become more constructive on bonds when nominal and real interest rates rise from current levels, and when credit spreads widen from current levels.

At present, stocks, in the aggregate, appear to be priced roughly 10-20% below our estimate of "fair value." We expect that total returns for our portfolio holdings should approximate the future growth in business value generated by our companies from current levels over the next several years, with additional potential return coming from a normalization of equity valuations toward "fair value," plus dividends.

Our primary focus remains on identifying companies with strong, durable business franchises that are able to earn highly competitive returns on capital, that have good prospects for business value growth over time, and that trade at attractive valuations.

We expect 2019 to be a very challenging year for investors, characterized by significant bond and stock price volatility, as the current economic and market cycles age. If corporate earnings show continued solid growth in 2019 (which we anticipate), stocks will likely outperform bonds on balance, given current valuations and the intermediate and long-term total returns implied by those valuations.

We appreciate your ongoing support and offer our best wishes for a happy and healthy 2019!

We encourage you to contact us if you would like to talk about your portfolio and our 2019-20 outlook in detail.

Sincerely,

Edson L. Bridges III, CFA
CEO

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.

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. Investing in value stocks presents the risk that value stocks may fall out of favor with investors and underperform other asset types during given periods. Equities, bonds, and other asset classes have different risk profiles, which should be considered when investing. All investments contain risk and may lose value.

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

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

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 MSCI Emerging Markets Index is maintained by MSCI Inc. formerly Morgan Stanley Capital International and is an index used to measure equity market performance in global emerging markets.

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.

Basis point refers to a common unit of measure for interest rates and other percentages in finance. One **basis point** is equal to 1/100th of 1%, or 0.01%, or 0.0001, and is used to denote the percentage change in a financial instrument.

Duration is a measure of the sensitivity of the price of a bond or other debt instrument to a change in interest rates. A bond's term is a linear measure of the years until repayment of the principal is due. It does not change with the interest rate environment.

It is not possible to invest directly in an index.

Fair value is a rational and unbiased estimate of the potential market price of a good, service, or asset.