

Dear Client,

Key takeaways coming out of the third quarter include:

1. Equities are off to a strong start during the first three quarters of 2018.
2. The advance in stock prices in 2018 has been largely driven by better-than-expected corporate earnings; despite strong stock price performance, broad equity market valuations are currently at about the same level that they were at the start of the year, and generally appear to be close to “fair value” given the current level of corporate earnings and interest rates.
3. We expect increasing stock price volatility going forward. Salient equity market risks include corporate earnings, trade war concerns, rising inflation and interest rates, and reaction to mid-term elections in the U.S.
4. We believe stocks remain more attractive than bonds over a long-term investment horizon.

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

<u>Index</u>	<u>Third Quarter</u>	<u>YTD</u>	<u>Trailing 12-Mo</u>
S&P 500	7.71%	10.56%	17.90%
S&P 400 Midcap Index	3.86%	7.48%	14.23%
S&P 600 Small Cap Index	4.71%	14.52%	19.05%
MSCI World Index Ex U.S.	0.79%	-2.71%	2.25%
Barclays U.S. Aggregate Bond Index	0.02%	-1.60%	-1.22%

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 very solid gains in the third quarter, continuing the rally that has been in place since the mid-February 2016 stock market lows. From February 15, 2016, through September 30, 2018, the S&P 500 has a cumulative total return of 65%.

U.S. large cap stocks were the best performers in the third quarter (+7.71%); small stocks (+4.71%) and midcap (+3.86) also posted good total returns. After performing well in 2017, international stocks have struggled in 2018; non-U.S. equities managed a positive total return in the third quarter, but have a -2.71% total return for the first three quarters of the year.

The divergence between U.S. stocks and international stocks has become very wide: since year-end 2008, the S&P 500 has returned 276% (14.55% annualized) versus 125% for the MSCI World Index (ex U.S.) (8.66% annualized). The disparity in returns between U.S. stocks and international stocks has been a function of much stronger earnings growth in the U.S. relative to the rest of the world since 2008, and more recently, due to relative dollar strength. At present, the S&P 500 trades at 16x estimated 2019 earnings, versus the MSCI ACWI ex U.S. valuation of 12x estimated 2019 earnings.

Corporate earnings growth has been the primary driver of the solid year-to-date equity returns in the U.S. Earnings results have consistently exceeded consensus expectations during the first two quarters of 2018; we expect solid earnings results as we enter the third quarter reporting period, but as the current earnings expansion ages, there is risk that at some point, consensus expectations catch up to, or exceed, actual results, which could lead to a sea change in equity market sentiment from generally positive to modestly negative. Such a sentiment change would likely be a catalyst for a meaningful equity market pullback.

We continue to believe that the level and trajectory of corporate earnings remains the single most important factor affecting stock returns for the remainder of 2018 and into 2019, particularly for high-profile, large cap companies that have largely led the market's advance so far this year.

After a relatively volatile first quarter, stock market trading volatility over the past two quarters has become more muted, similar to the lower levels of stock price volatility experienced in 2017. We expect that stock price volatility will eventually revert to more normal levels. Catalysts for a choppy market environment might include earnings disappointments by some high profile equity market leaders (Apple? Amazon? Google?), an increase in concerns around trade wars, an increase in concerns about higher inflation and/or interest rates, and reaction to mid-term elections in the U.S.

U.S. stocks remain close to our estimate of “fair value” (even though stock price levels are near all-time highs). We believe U.S. equities are currently priced to provide mid-to-high single digit returns from current levels over the next several years, albeit with the prospect of elevated levels of stock price volatility as the current cycle ages. Our fair value target for year-end 2019 for the S&P 500 is 3,200, which would imply total returns of roughly 10% over the next five quarters.

A meaningful stock market correction (a decline of 10% or more) is overdue by historic standards, but the combination of solid corporate earnings growth (driven by positive corporate financial performance, corporate tax rate cuts enacted at year-end 2017, and the continuation of a relatively low interest environment) has supported the equity market’s continued advance over the past ten quarters.

The U.S. equity market, despite a strong advance over the first three quarters of the year, is actually slightly cheaper at present than it was at the start of the year, as the strong pace of corporate earnings growth over the course of the first three quarters of the year has driven consensus earnings expectations higher than stock prices have risen. Consensus expectations for S&P 500 earnings at the start of 2018 were \$145 per share for 2018, and \$157 for 2019; today consensus earnings are \$163 for 2018 (up 12%) and \$180 per share for 2019 (up 15%).

Despite strong earnings growth to date in 2018, we would not be surprised if stock prices corrected by 15-20% at some point over the next several quarters. A material stock price decline from current levels would, in our view, take equity valuations to very attractive levels and provide an excellent entry point for cash. Alternatively, we would be inclined to reduce commitments to stocks (based on stretched valuations) should stock prices move sharply higher (15-20%) in the short term.

Interest rates drifted high during the third quarter. The yield on the 10-year Treasury ended the quarter at 3.06%, the first time the 10-year Treasury has ended a month at a yield higher than 3% since December, 2013. Bond returns, as measured by the Barclays U.S. Aggregate Bond Index, continue to materially trail equity returns, a condition which will likely persist until such time as stock prices experience a material decline.

Bonds remain relatively unattractive in our view, because 1) interest rates remain low relative to historic levels, and 2) we believe the probabilities favor a continuation toward somewhat higher interest rates on balance over the next several years. We expect yields on the 10-year Treasury will eventually reach a range of 3.5-4.0%. We will become more constructive on bonds once yield levels increase to the point where they exceed long-term inflation expectations by 1% or more.

We are encouraged by the positive returns for stocks to date in 2018, but it has been a difficult environment to commit cash, given the persistent rise in stock prices over the course of the year since the sharp correction experienced between January 26 and February 8. We will continue to exercise discipline and vigilance as we invest cash for clients: a focus on market and company-specific valuation levels, always a central element of our investment process, is even more critical after a period of strong equity market performance.

We remain constructive on the long-term outlook for stocks, but we are mindful of the risks inherent in a capital markets environment that has experienced a very long, virtually uninterrupted stretch of stock price appreciation, against a backdrop of rising interest rates.

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.

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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.
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