



Take Away The Punch Bowl, Small-Cap Stocks May Keep Drinking

Interest Rate Hikes And Small Cap Stock Returns

After years of speculation, many investors believe that some form of a rate hike may finally be near. The Fed's recent talk about raising interest rates has many investors considering the logical adjustment to an eventual new era of Fed tightening. How rate hikes might affect small-caps equities is of great interest to our team and our shareholders.

While exact dates and periods of past tapering actions or interpretations of "Fed speak" can't be measured precisely, we can take a look at past periods of interest rates hikes and their effect on small cap equities. From this data, investors may gain some historical context to enhance their perspective regarding future Fed actions and market returns.

The previous six times the Fed embarked on a tightening cycle and the associated small cap returns are below:

During each of the last six instances, small cap returns have provided positive average returns over the 3-, 6-, 12- and 18-month periods following Fed tightening

RUSSELL 2000 INDEX RETURNS FOLLOWING FED FUNDS RATE INCREASE

Hike Date	3 months after	6 months after	12 months after	18 months after
8/7/80	13.9%	12.7%	27.0%	13.0%
2/1/83	16.6%	27.8%	17.6%	3.3%
10/1/86	-0.5%	22.9%	28.9%	7.3%
2/4/94	-2.6%	-5.4%	-2.7%	16.5%
6/30/99	-8.3%	6.4%	13.4%	3.8%
6/30/04	-4.1%	9.5%	9.4%	16.4%
Averages	2.5%	12.3%	15.6%	10.0%

During each of the last six instances, small cap returns have provided positive average returns over the 3-, 6-, 12- and 18-month periods following Fed tightening. Notably, small cap stocks generally performed very strongly for the first twelve months following a rate hike, followed by a pull back during the ensuing six month period. This indicates that, historically, if there is a time for concern regarding small cap returns in relation to Fed actions, that time is typically twelve months following a rate hike.



It makes sense that small cap stock prices would rise following a rate hike if you consider the natural business cycle. Stock prices anticipate economic growth at the beginning of a cycle, followed first by economic improvements and then Fed rate hikes as a last response. When the Fed finally gets around to “removing the punch bowl,” it is likely that economic growth is well underway and stock prices are continuing to rise in response.

We don't know exactly when the Fed may begin increasing interest rates. But if and when we do begin to see Fed rate hikes, the stock market should in theory be higher because companies' corporate earnings will be higher. And as seen in the data, small cap stocks have historically continued to climb for up to one year following the date of the initial rate hike.

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The Fund's investment objectives, risks, charges, and expenses must be considered carefully before investing. The statutory and summary prospectus contain this and other important information about the investment company and may be obtained by calling 800-331-8936 or by visiting www.perrittcap.com. Read carefully before investing.

The Russell 2000 Index consists of the smallest 2,000 companies in a group of 3,000 U.S. companies in the Russell 3000 Index, as ranked by market capitalization. It is not possible to invest directly in an index.

Mutual fund investing involves risk. Principal loss is possible. The Funds invest in smaller companies, which involve additional risks such as limited liquidity and greater volatility than larger companies. The Funds invest in micro cap companies which tend to perform poorly during times of economic stress. The Ultra MicroCap Fund may invest in early stage companies which tend to be more volatile and somewhat more speculative than investments in more established companies.

