



Needham Small Cap Growth Fund: Review of the Third Quarter 2019

In the 3Q19, the Needham Small Cap Growth Fund Institutional and Retail classes returned 3.26% and 3.13%, respectively. The Russell 2000 Index returned -2.40% and the S&P 500 Index returned 1.70%.

I am very pleased with the Fund's quarterly performance, as headline and market volatility continued. The interest rate curve inverted, sparking market fears of a recession. I did not believe a recession was near, allowing the Fund an opportunity to deploy capital at reasonable prices. While global economic growth has been decelerating, I remain constructive on the overall global economy as it adjusts. As the market recovered toward the end of the third quarter, the Fund reduced specific positions that achieved price targets.

While volatility may seem to be a bad word for the overall markets, it is a great chance for active managers to find buying and selling opportunities. In volatile markets, a cash position is truly strategic for small cap fund managers. Many small cap investment opportunities "trade by appointment," and the Needham Small Cap Growth Fund likes to capitalize on these opportunities when liquidity is available to both buy and sell stock positions.

The Fund continued its lean toward a concentrated portfolio of stocks, with the top 10 holdings representing 51.04% of net assets at September 30, 2019. Top holdings at September 30, 2019 included Photronics, Inc. (PLAB), PDF Solutions, Inc. (PDFS), Aspen Aerogels, Inc. (ASPN), Vicor Corporation (VICR) and Cohu, Inc. (COHU).

The Fund's top third quarter contributors included Photronics (PLAB), MACOM Technology Solutions Holdings, Inc. (MTSI), Akoustis Technologies, Inc. (AKTS), TTM Technologies, Inc. (TTMI), Navigator Holdings, Ltd. (NVGS) and Intevac, Inc. (IVAC). The Fund did not have any M&A announcements in the quarter. The Fund's largest third quarter detractors were 2U, Inc. (TWOU), Aspen Aerogels, Inc. (ASPN) and Cohu, Inc. (COHU). Aspen Aerogels remains the Fund's top performing holding year to date.

After a good first half of 2019, the markets, due for a pause, experienced weakness mid-summer. Increased volatility continued throughout the quarter, due in part to headlines focused on trade disputes and restrictions, with particular attention paid to the Huawei ban on both the supply chain and end-customer markets. While these impacts are meaningful and will have negative consequences for industries, such as semiconductors, optical and communications, I also believe that companies have creative plans to balance their exposure to such headwinds. As the market digested almost daily updates from trade uncertainties, patience paid off, and the Fund was able to deploy a significant amount of its cash position into stocks at good value points. The Fund ended the quarter with a cash position of 16.2%, as it sold positions and received positive inflows. I will remain patient as I deploy the Fund's cash position.

My outlook for the remainder of 2019 remains positive, with the possibilities of a phase 1 U.S.-China trade deal, an accommodative Federal Reserve, and value recognition in the Fund's small cap companies that lagged in 2018. I look forward to a year of patience rewarded, and I continue to believe that a favorable environment remains for investment in equities. However, the markets have recovered nicely from the year-to-date lows and it would not surprise me to see a pause in the market recovery.

I am focused on the following three themes: 1) continuation of the growth in the semiconductor capital equipment industry; 2) 5G communication infrastructure build-outs; and 3) military and defense modernization. These three areas of investment impact much of the Fund's portfolio, and I believe that they should create long-term shareholder value.

I expect increased volatility to continue throughout 2019 and into 2020. I also expect the Federal Reserve to remain vigilant in setting interest rate policy that remains a tailwind to risk assets. While global trade negotiations have been painful headlines for many, any resolution to these disagreements should provide a nice tailwind to the global economy as we enter the U.S. general election of 2020. The high-yield markets remain strong, which is also supportive of small cap asset class valuations. I reiterate from past quarterly letters that mergers and acquisitions continued in the small cap universe, and I expect to see increased M&A activity to improve and benefit our portfolio of stocks in 2020.

We welcome our new investors and thank all of our investors for their continued support. If you have any questions, thoughts or concerns, please contact us at (800) 625-7071 or at cretzler@needhamco.com. For information about the funds, please visit our website at www.needhamfunds.com.

Sincerely,



Chris Retzler
Portfolio Manager

AVERAGE ANNUAL RETURNS AS OF 9/30/19

	3 MO	YTD	1YR	3YR	5YR	10YR	SINCE INCEPT.
Needham Small Cap Growth Fund Inst Class**	3.26%	33.57%	12.10%	15.66%	13.01%	11.82%	11.38%
After Taxes on Distributions	3.26%	33.57%	6.26%	11.68%	9.94%	10.14%	9.79%
After Taxes on Distributions & Redemptions	1.93%	19.87%	8.00%	10.60%	9.14%	9.17%	9.26%
Needham Small Cap Growth Fund Retail Class	3.13%	33.06%	11.45%	15.03%	12.40%	11.22%	10.78%
After Taxes on Distributions	3.13%	33.06%	5.58%	11.05%	9.33%	9.54%	9.20%
After Taxes on Distributions and Redemptions	1.85%	19.57%	7.64%	10.11%	8.66%	8.65%	8.74%
Russell 2000 Index	[2.40]%	14.18%	[8.89]%	8.23%	8.19%	11.19%	8.14%
S&P 500 Index	1.70%	20.55%	4.25%	13.39%	10.84%	13.24%	8.16%

The Needham Small Cap Growth Fund inception date is 5/22/02.

**Performance for any periods prior to the inception date of Institutional Class Shares are based on the historical performance of the Retail Class Shares adjusted to assume the expenses associated with Institutional Class Shares.

The Needham Small Cap Growth Fund's Gross Expense Ratio is 2.27% for the Retail Class and 2.03% for the Institutional Class. The Needham Small Cap Growth Fund's Net Expense Ratio is 1.93% for the Retail Class and 1.26% for the Institutional Class. The Net Expense Ratio reflects a contractual agreement by the Fund's investment adviser to waive its fee and/or reimburse the Fund through May 1, 2020 to the extent the Gross Expense Ratio exceeds 1.85% and 1.18% of the average daily net assets of Retail Class Shares and Institutional Class Shares (Expense Cap). The Expense Cap excludes taxes, interest, brokerage, dividends on short positions, fees and expenses of "acquired funds," extraordinary items and shareholder redemption fees but includes the management fee.

Fact Sheet Link: [Needham Small Cap Growth Fund](#)

The information presented in this commentary is not intended as personalized investment advice and does not constitute a recommendation to buy or sell a particular security or other investments.

This message is not an offer of the Needham Growth Fund, the Needham Aggressive Growth Fund or the Needham Small Cap Growth Fund. Shares are sold only through the currently effective prospectus. Please read the prospectus or summary prospectus and consider the investment objectives, risks and charges and expenses of the Funds carefully before you invest. The prospectus and summary prospectus contain this and other information about the Funds and can be obtained on our website, www.needhamfunds.com.

Investment returns and principal value will fluctuate, and when redeemed, shares may be worth more or less than their original cost. Performance data quoted represents past performance, and does not guarantee future results. Current performance may be higher or lower than these results. Performance current to the most recent month-end may be obtained by calling our transfer agent at 1-800-625-7071. Total return figures include reinvestment of all dividends and capital gains.

All three of the Needham Funds have substantial exposure to small and micro capitalized companies. Funds holding smaller capitalized companies are subject to greater price fluctuation than those of larger companies.

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Portfolio holdings are subject to change. The Needham Small Cap Growth Fund's ownership as a percentage of net assets in the stated securities as of 9/30/19: PLAB: 9.58%; PDFS: 6.71%; ASPN: 5.25%; VICR: 4.87%; COHU: 4.46%; MTSI: 2.63%; AKTS: 1.42%; TTMI: 2.01%; NVGS: 4.11%; IVAC: 4.10%; TWOU: 0.68%.