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Changing Market Dynamics on the Horizon for Small Caps

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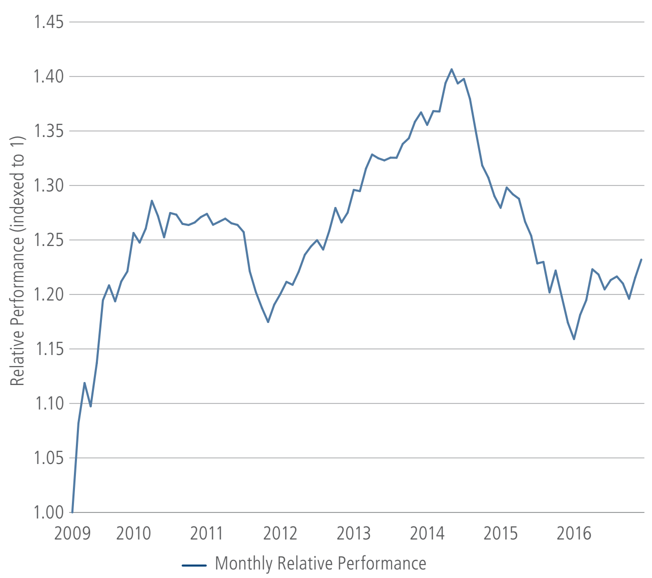
Equities, including small caps, have performed remarkably well since the Great Recession. As you can see in the first chart, leadership within small-cap equities since the market trough in 2009 has been skewed toward companies with business models predicated on high levels of debt. We believe that this outperformance, which peaked at roughly 40% in 2014, may be largely attributable to the abundant refinancing opportunities available in an environment of declining interest rates, refinancing opportunities that are largely exhausted today.

The second chart shows how much more exposed certain small-cap stocks could be to rising rates compared to their large-cap peers. Only 10% of the weighting of the Russell 2000 Index is investment grade rated and thus has access to 30-year debt maturities; in contrast, nearly 90% of the S&P 500 carries an investment grade rating. The much shorter debt maturities of the Russell 2000 Index suggest it will be more impacted by short-term interest rate movements. Looking forward, we believe balance sheet strength will again be a determinant of performance within the small-cap market—which hasn't necessarily been the case since 2009.

Highly Leveraged Small-Cap Stocks Have Outperformed the Small-Cap Market Since 2009

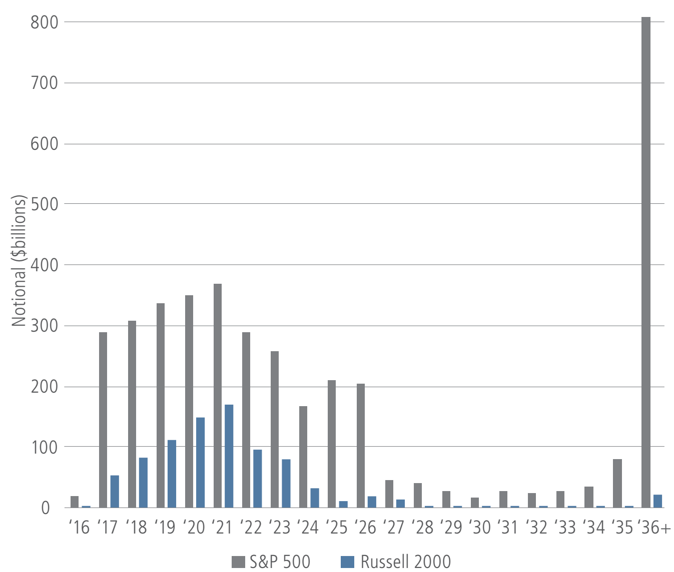
Monthly Relative Performance of Highest Debt-To-Capital Small-Cap Companies, Excluding Financials, versus the Russell 2000 Index



Source: BofA Merrill Lynch Small Cap Research; Russell Investment Group. Data from March 31, 2009 – January 31, 2017. **Past performance is no guarantee of future results.** See Additional Disclosure section at the end of this piece, which is an important part of this presentation.

But a Sea Change in Leadership Could Be in Store if Interest Rates Rise

Debt Maturities of the S&P 500 Index versus the Russell 2000 Index



Source: Bloomberg, Goldman Sachs Global Investment Research based on notional debt excluding financials. Information reflects all bonds outstanding regardless of maturity. Hedges are not included in this analysis.

Implications for Investors

In an environment of rising rates, outperformance within the small-cap market segment could dramatically shift away from lower-quality, high debt businesses. We believe that a focus on identifying higher-quality companies with balance sheet strength, free cash flow generation, high barriers to entry and above-average business models is key to navigating the changing market dynamics of the small-cap universe.

For more information please contact us at:

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This material is intended as a broad overview of the portfolio managers' style, philosophy and process and is subject to change without notice. The portfolio managers' views may differ from those of other portfolio managers as well as the views of Neuberger Berman.

Most of the Fund's performance depends on what happens in the stock market. The market's behavior is unpredictable, particularly in the short term. There can be no guarantee that the Fund will achieve its goal. Recent events in the U.S. and global economies have resulted, and may continue to result, in an unusually high degree of volatility in the financial markets and in the net asset values of many mutual funds, including to some extent of the Fund.

Market Volatility: Markets may be volatile and can decline significantly in response to adverse issuer, political, regulatory, market or economic developments. To the extent that the Fund sells stocks before they reach their market peak, it may miss out on opportunities for higher performance.

Issuer-Specific Risk: The value of an individual security or particular type of security can be more volatile than the market as a whole and can perform differently from the value of the market as a whole.

Sector Risk: To the extent the Fund invests more heavily in particular sectors, its performance will be especially sensitive to developments that significantly affect those sectors. Individual sectors may move up and down more than the broader market. The several industries that constitute a sector may all react in the same way to economic, political or regulatory events.

Small- and Mid-Cap Stock Risk: The stocks of small- and mid-cap companies are often more volatile and less liquid than the stocks of larger companies and may be more affected than other types of stocks by the underperformance of a sector or during market downturns. Compared to larger companies, small- and mid-cap companies may have a shorter history of operations, and may have limited product lines, markets or financial resources.

Value Stock Risk: Value stocks may remain undervalued during a given period or may not ever realize their full value. This may happen, among other reasons, because of a failure to anticipate which stocks or industries would benefit from changing market or economic conditions.

The Russell 2000® Index is an unmanaged index consisting of the securities of the 2,000 issuers having the smallest capitalization in the Russell 3000® Index, representing approximately 10% of Russell 3000 total market capitalization. The index is market cap-weighted and includes only common stocks incorporated in the U.S. and its territories.

The S&P 500 Index is widely regarded as the standard for measuring large-cap U.S. stock market performance and includes a representative sample of leading companies in leading industries. Please note that indices do not take into account any fees and expenses of investing in the individual securities that they track and that individuals cannot invest directly in any index. The Fund may invest in securities not included in the above-described indices.

Past performance is no guarantee of future results.

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