Q1 2017

# AMG Managers Skyline Special Equities Fund

## COMMENTARY

ASSET CLASS | SMALL CAP

Class N | SKSEX — Class I | SKSIX — Class Z | SKSZX

### Average Annual Returns (%)[1,2] (as of 03/31/17)

| | QTD | YTD | 1 yr | 3 yr | 5 yr | 10 yr | Since Incpt. |
|---|---|---|---|---|---|---|---|
| SKSEX (Class N) | 0.44 | 0.44 | 18.33 | 5.92 | 13.60 | 8.01 | 12.16[3] |
| SKSIX (Class I) | — | — | — | — | — | — | -0.30[4] |
| SKSZX (Class Z) | — | — | — | — | — | — | -0.32[4] |
| Russell 2000® Value Index | -0.13 | -0.13 | 29.37 | 7.62 | 12.54 | 6.09 | — |
| Russell 2000® Index | 2.47 | 2.47 | 26.22 | 7.22 | 12.35 | 7.12 | 9.04[3] |

SKSEX (Class N) Expense Ratio (Gross/Net)[5]: 1.36%/1.33%
SKSIX (Class I) Expense Ratio (Gross/Net)[5]: 1.21%/1.18%
SKSZX (Class Z) Expense Ratio (Gross/Net)[5]: 1.11%/1.08%

*The performance data shown represents past performance. Past performance is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. The investment return and the principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. For performance information through the most recent month end, please call 800.835.3879 or visit our website at www.amgfunds.com. From time to time the advisor has waived fees or reimbursed expenses, which may have resulted in higher returns.*

The **AMG Managers Skyline Special Equities Fund** (N Class) generated a 0.44% return for the quarter ended March 31, 2017, compared to an 2.47% return for the Russell 2000® Index and a -0.13% return for the Russell 2000® Value Index.

## Overview

Small cap stock prices were mixed in the first quarter. Stocks in sectors considered faster growing, including health care and information technology, performed well. Financial stocks, banks in particular, underperformed, giving back some of the gains they generated in last year's post-election rally.

The Fund underperformed the Russell 2000® Index due in part to lack of exposure to the faster growing sectors that drove much of the Index's performance, and outperformed the Russell 2000® Value Index due to a combination of advantageous sector allocation and stock selection.

The risk/reward for equities appears balanced. We believe the outlook for earnings is as favorable as it has been in several years, and if strong growth is achieved, stock prices should respond positively. At the same time, valuations are towards the higher end of their historical range, creating risk to the downside if earnings disappoint.

## Market Review

Stocks were mixed in the first quarter, as indicated by the Russell 2000® Index's 2.5% increase, the -0.1% return generated by the Russell 2000® Value Index and the S&P 500 Index's 6.1% increase. During the first quarter, large cap stocks outperformed small cap stocks, growth stocks outperformed value stocks and health care stocks were among the best performers, while financial services stocks underperformed, reversing trends from the fourth quarter of 2016.

The first quarter reversals indicated waning enthusiasm for buying stocks that are expected to be beneficiaries of the new administration's policies. The failure of Congress to repeal the Affordable Care Act called into question the likelihood that policies such as corporate tax reform and bank deregulation would be implemented. For example, small cap stocks pay higher effective tax rates than large cap stocks. Small cap stocks also tend to have less overseas exposure than large cap stocks and were expected to be greater beneficiaries of acceleration in the U.S. economy brought about by the new administration's policies. Small cap stocks gave back much of their post-election outperformance during the first quarter when investors became less convinced that pro-business policies would be implemented.

The fading "Trump trade" also helps explain the outperformance of growth stocks relative to value stocks. The Russell 2000® Growth Index's 5.4% gain for the quarter included a 2.7% contribution from health care stocks, which rallied when it became clear the Affordable Care Act wouldn't be repealed. For the same period, the Russell 2000® Value Index's -0.1% return included only a 0.4% contribution from the health care sector and a -0.8% contribution from financial stocks, which gave back some of their post-election gains.

## Fund Portfolio Review

The information technology sector contributed most to The Fund's absolute performance during the first quarter due to its large weighting in the Fund and solid absolute performance. Diebold Nixdorf, Incorporated, a provider of ATMs and related services, contributed positively in response to a solid earnings report and evidence of progress in the integration of the recently acquired Wincor operations.

During the quarter, Fund holding CEB Inc., a consulting company, announced it was being acquired at a 25% premium to the price it was trading at immediately prior to the announcement.

The Fund had a low weighting in the underperforming financials sector relative to the Russell 2000® Value Index and underperforming real estate sector relative to both benchmarks. The low weightings and positive stock selection in these sectors contributed to The Fund's return relative to its benchmarks. Realogy Holdings Corp., a residential real estate broker, advanced due to an earnings report highlighted by improving trends in its end markets. The Fund's lack of exposure to the poor-performing energy sector also contributed positively to its performance relative to its benchmarks.

The consumer discretionary sector detracted most from The Fund's absolute performance and was also a significant detractor relative to its benchmarks. Several of the Fund's retail holdings declined due to the

[1] Returns for periods greater than one year are annualized.
[2] Prior to February 27, 2017, the Fund's N shares were known as S shares.
[3] Since the inception of the Fund's Class N shares on April 23, 1987.
[4] Since the inception of the Fund's Class I and Z shares on February 24, 2017.
[5] The Fund's Investment Manager has contractually agreed, through at least May 1, 2018, to limit Fund operating expenses. The net expense ratio reflects this limitation, while the gross expense ratio does not. Please refer to the Fund's Prospectus for additional information on the Fund's expenses.

persistent headwinds (weak consumer spending, online competition) facing brick-and-mortar retailers. The health care sector also detracted from The Fund's performance relative to its benchmarks, particularly the Russell 2000® Index, due primarily to its lack of exposure to strong-performing biotech stocks, which were up 19% during the quarter. Biotech stocks typically do not have earnings and are therefore unsuitable for our investment philosophy.

## Outlook

As stated earlier, we believe the risk/reward for equities appears balanced. Valuations are towards the higher end of their historical range, creating risk to the downside if earnings disappoint. However, the outlook for earnings is favorable, leading to the potential for stock price gains if those expectations are achieved.

Small cap stocks continue to trade towards the high end of their historical valuation range. We believe current valuations are in part a reflection of the low returns available on alternative investments like bonds in a low-interest-rate environment. However, the U.S. Federal Reserve (the Fed) has begun to gradually raise their target interest rate, believing that the economy is healthy enough to withstand a less accommodative monetary policy. If the Fed's move results in meaningfully higher interest rates throughout the economy, equity valuations may not look as attractive relative to bonds.

Current valuations are also supported by an improved outlook for corporate profits. The backdrop is favorable for earnings growth, as indicated by the Fed's confidence that the economy is healthy enough to absorb gradual rate hikes. In addition, economic activity outside the U.S. is expected to accelerate this year after a lackluster 2016. The modest earnings recession experienced by U.S. companies beginning in early 2015 appears to have ended in the second half of last year, providing positive momentum entering this year.

Analysts are expecting first-quarter earnings for companies in the S&P 500 Index to grow at their fastest rate since 2011. In addition, analysts expect companies in the Russell 2000® Index to grow earnings 12% in 2017 and the ratio of earning estimate increases to decreases is at its highest level since 2011.[1]

Another component of current valuations is the expectation that earnings will benefit from a more business-friendly administration and Congress. Stock prices will likely be influenced by the degree of success in implementing corporate tax reform, reduced regulations and other such policies.

We believe the fundamentals of the companies in the Fund remain solid and their valuations are attractive relative to the typical small cap company. Because of our focus on finding the best combination of above-average earnings growth and below-average valuations, The Fund tends to be somewhat more economically sensitive than its benchmarks. We believe the Fund is well positioned to take advantage if earnings improve as we expect.

[1] FactSet Earnings Insight

*The views expressed represent the opinions of the Skyline Asset Management, L.P., as of March 31, 2017, are not intended as a forecast or guarantee of future results, and are subject to change without notice.*

### Top Ten Holdings (%)[2] (as of 03/31/17)

| Company | % of Net Assets |
|---|---|
| Children's Place Inc | 2.46 |
| Manpowergroup Inc | 2.00 |
| First Busey Corp | 1.95 |
| Greenhill & Co Inc | 1.91 |
| Infinity Property & Casualty Corp | 1.86 |
| Essent Group Ltd | 1.79 |
| CBIZ Inc | 1.78 |
| BancorpSouth Inc | 1.75 |
| Brunswick Corp | 1.67 |
| Realogy Holdings Corp | 1.61 |
| TOTAL % | 18.78 |

## Disclosure

***Investors should carefully consider the fund's investment objectives, risks, charges and expenses before investing. For this and other information, please call 800.835.3879 or download a free prospectus. Read it carefully before investing or sending money.***

*Past performance is no guarantee of future results.*

A short-term redemption fee of 2% will be charged on shares held for less than 30 days.

The Fund is subject to risks associated with investments in small-capitalization companies, such as erratic earnings patterns, competitive conditions, limited earnings history, and a reliance on one or a limited number of products.

Companies that are in similar businesses may be similarly affected by particular economic or market events; to the extent the Fund has substantial holdings within a particular sector, the risks associated with that sector increase.

The Fund invests in value stocks, which may perform differently from the market as a whole and may be undervalued by the market for a long period of time.

The Russell 2000® Value Index is a market-capitalization weighted equity index maintained by the Russell Investment Group and based on the Russell 2000® Index, which measures how U.S. stocks in the small-cap equity

[2] Mention of a specific security should not be considered a recommendation to buy or a solicitation to sell that security. Holdings are subject to change.

value segment perform. Included in the Russell 2000® Value Index are stocks from the Russell 2000® Index with lower price-to-book ratios and lower expected growth rates.

The Russell 2000® Index is a small-cap stock market index of the bottom 2,000 stocks in the Russell 3000® Index. The Russell 2000® is by far the most common benchmark for mutual funds that identify themselves as "small-cap".

The Russell 2000® Growth Index measures the performance of the Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values. Unlike the Fund, the Russell 2000® Growth Index is unmanaged, is not available for investment and does not incur expenses.

The Standard & Poor's 500, often abbreviated as the S&P 500, or just "the S&P", is an American stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices.

Unlike the Fund, the indices are unmanaged, are not available for investment and do not incur expenses.

Any sectors, industries, or securities discussed should not be perceived as investment recommendations. Any securities discussed may no longer be held in the Fund's portfolio. It should not be assumed that any of the securities transactions discussed were or will prove to be profitable, or that the investment recommendations we make in the future will be profitable.

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