VLFAlert

ValueLine funds

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Dear Fellow Shareholder,

Thank you for choosing Value Line Funds as a part of your diversified investment portfolio. For over half a century, Value Line Funds has championed sound investment principles and helped thousands of investors accomplish their financial goals with our actively managed family of mutual funds.

We hope you enjoy this edition of the VLFAlert and thank you for your continued support.

What Tax Reform—One Year Later—May Mean for Your Investment Portfolio

The anticipation of tax reform was one of the drivers of the U.S. equity markets in 2017 and the implementation of tax reform helped keep the momentum going through the first three quarters of 2018. But now, having just filed your taxes for the first time under the new laws, what might tax reform mean for your investment portfolio? Here are just a couple of interesting facts.

Historically, Tax Cuts Have Helped Mid- and Small-Cap Stocks More Than Large-Cap Stocks.

Smaller-cap stocks underperformed large-cap stocks in 2018, but they were outperforming through the first three quarters of the calendar year and only fell behind in the flight to safety that arose in the fourth quarter amidst significant market volatility and heightened political and geopolitical turmoil. One of the reasons smaller-cap stocks had performed well is that they enjoyed a bigger boost from the corporate tax cuts than larger companies. Why?

- **Because most smaller cap companies paid a higher tax rate than their large cap counterparts, providing a bigger potential boost for earnings per share growth rates.** In 2017, companies in the Russell Mid Cap Index and the Russell 2000 Index, measures of mid-cap and small-cap stocks, respectively, being more U.S.-centric in their businesses, paid median effective tax rates of approximately 32% each. This compares to companies in the S&P 500 Index, measuring large-cap companies, which paid a median effective tax rate of 28%. The median effective tax rate for the 30 mega-cap stocks in the Dow Jones Industrial Average was just 23.8%.[1] That means smaller companies had proportionately more to gain in terms of earnings, cash flow and capital spending opportunities when corporate tax rates came down to 21% for all companies.

- **Because the reduced tax burden and repatriation element of tax reform allowed larger cap companies to invest strategically in their businesses through merger and acquisition activity, targeting quality mid- and small-cap companies.** In our view, mid-cap and small-cap companies have become takeover targets, often seeing their shares rise based on its anticipated acquisition price. "With many large-cap companies flush with cash as a result of tax reform, many are looking to buy smaller companies with proprietary products and services to solidify or expand their own businesses. We've already seen several of the holdings in our mid-cap portfolios get acquired, reinforcing the validity of our investment theses when we purchased their shares," explained Steve Grant, portfolio manager of the Value Line Premier Growth Fund and Value Line Mid Cap Focused Fund. "Often, mid-cap companies are considered the 'sweet spot' for deals, since they have surpassed their start-up stage and demonstrated some staying power and business maturity yet haven't become expensive giants yet."

The question some investors may now ask more than one year after tax reform went into effect is—are these stocks still attractive? We believe the answer is yes.

1. **Still strong U.S. economic growth.** U.S. economic growth rates have been better than those seen in many international economies, yet tariff and trade wars continue, disproportionately affecting larger multinational companies. The S&P SmallCap 600 has 78.8% of its revenues derived from the U.S. and the S&P MidCap 400 Index has 73.3%, while the S&P 500 Index has the lowest percentage at 70.9%.[2]

2. **Accelerating earnings growth.** We believe an acceleration in small-caps' earnings growth could drive returns in the absence of multiple expansion.

3. **Favorable market conditions.** Smaller companies have historically performed better than large caps in environments of rising interest rates and U.S. dollar strength.[3]

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4. **More merger & acquisition activity.** We believe merger and acquisition activity will continue to favor mid and small-cap companies.

5. **Historical track record.** Small- and mid-cap equities (SMID) have outperformed small-cap equities alone 87% of the time since the Russell 2500 Index's inception, as measured by rolling three-year index returns. Additionally, SMID has experienced less volatility,[3] which we believe is an important consideration when evaluating the risk profile of an asset class, particularly when most U.S. equity indices are experiencing heightened volatility. While past performance is no guarantee of future results, history may serve as a useful guide to your investment decisions.

Given that Value Line Premier Growth Fund and Value Line Mid Cap Focused Fund emphasize mid-cap stocks and indeed are categorized by independent ratings agency Morningstar as mid-cap growth funds, it's worth considering moving into or increasing your investments in these Value Line Funds, especially if you don't have much exposure currently. We believe mid-cap stocks broadly are still beneficiaries of the tax cuts, which coupled with U.S. economic growth outpacing international economic growth, a rising U.S. dollar, and trade tariffs with international partners, may serve as tailwinds to their potential outperformance versus their larger-cap counterparts moving forward.

If You Were in a Tax Bracket Above 25.6% for 2018, Then Municipal Bonds Are Still Quite Attractive.

Now that you've done your taxes for 2018, you have a better idea of what tax bracket you are in under the new law. So on the fixed income side of your investment portfolio, you should note that at tax rates above 25.6%, a AA-rated 10-year municipal bond would yield more than a 10-year AA-rated corporate bond after taxes.[4] In other words, high-earners' tax rates are still high enough that yields for municipal bonds remain attractive relative to after-tax yields on taxable alternatives. The capping of the state and local tax deduction at just $10,000, effectively increasing the marginal tax rate for taxpayers in high tax states, such as New York, New Jersey, California and several others, should increase investor demand for municipal bonds in high tax states even more.

With the filing of your 2018 taxes still fresh on your mind, this may be a good time to take another look at the Value Line Tax-Exempt Bond Fund, which seeks to provide investors with the maximum income exempt from federal income taxes while avoiding undue risk to principal. Capital appreciation is a secondary objective.

Value Line Funds Include:
Equity Funds
Premier Growth Fund
Larger Companies Focused Fund
Mid Cap Focused Fund
Small Cap Opportunities Fund
Hybrid Funds
Asset Allocation Fund
Capital Appreciation Fund
Fixed Income Funds
Tax Exempt Fund
Core Bond Fund

"We invite you to learn more about how our mid-cap equity funds and our tax-exempt bond fund may help you maximize the effectiveness of your investment portfolio in this era of new individual and corporate tax rates," says Mitchell Appel, President of the Value Line Funds. "We believe it's never too early or too late to build a diversified investment portfolio."

Check out our News & Commentary at vlfunds.com for the latest on the Value Line Funds.

For more mutual fund information, call today: 800.243.2729 or visit our website at www.vlfunds.com

[1]Thomson Reuters, BlackRock Investment Institute and Bloomberg.
[2]"Small and Mid-Cap Stocks Benefit from Tax Cut," U.S. News, June 25, 2018.
[3]"Goldman: Buy Small Caps If Bullish on Trump Plans," Barron's, April 6, 2017.
[4]"What Tax Reform Could Mean for the Muni Bond Market," Schwab, November 14, 2017.

Past performance is no guarantee of future results. You should carefully consider investment objectives, risks, charges and expenses of Value Line Mutual Funds before investing. This and other information can be found in the fund's prospectus, which can be obtained from your investment representative or by calling 800.243.2729. Please read it carefully before you invest or send money.

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