

Value Fund

3Q 2018 Quarterly Commentary



Investment Style: Large-Cap Value

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The Value Fund's Institutional Class returned +5.59% during the third quarter compared to +7.71% for the S&P 500 and +7.42% for the Russell 1000. For the first nine months of calendar 2018, the Fund's Institutional Class returned +9.06% compared to +10.56% for the S&P 500 and +10.49% for the Russell 1000. Since adopting its large-cap company mandate on June 30, 2008, the Fund's Institutional Class has generated average annual returns of +8.99% compared to +10.70% for the S&P 500 and +10.70% for the Russell 1000.

For domestic equity investors—both public and private—it remains the best of times. Consumers are confident. Economic growth has accelerated. Borrowing costs are reasonable. Animal spirits are high. Fundamentally speaking, all is relatively calm. Against this backdrop, we continue to keep our collective noses to the ground in search of mispriced risk. One question we've been asking ourselves with greater frequency of late: Which stock carries more risk to the long-term investor—a durable "compounder" trading at 30 times forward earnings nine years into a market expansion or a more cyclical/less-defensible business trading at 10-12 times expected earnings nine years into an economic expansion? Courtesy of Mr. Market, ample versions of both are on offer today. Should either be bought/owned? Our preference, as always, is "quality at a reasonable (or better) price." We seek to avoid compromise on either variable.

Three of the Fund's largest holdings—Berkshire Hathaway (+15%), Allergan (+15%) and Liberty Broadband/Charter Communications (each +11%)—were the most meaningful contributors to third quarter performance. Investors cheered Berkshire Hathaway's strong second quarter results as well as the decision to grant CEO Warren Buffett and Vice Chairman Charlie Munger greater autonomy in repurchasing the company's stock.

We agree the prior constraint of 1.2 times book value had become less germane as Berkshire's wholly owned, non-financial operating businesses continue to contribute a larger share of earnings. Allergan's stock participated in the strength across most of healthcare during the third quarter. The company's first-ever Medical Aesthetics Day on September 14 served as a welcome reminder of the attractiveness of the company's core growth engine. Cable sentiment also began to rebound thanks to improved operating results across the sector. As the calendar approaches 2019, we believe the tactical investments and heavy operational lifting Charter has tackled the past couple of years will begin to bear fruit in the form of substantial free cash flow per share growth.

Through the first nine months of calendar 2018, Mastercard (+48%) and Amazon (+71%) join Allergan (+18%) as the largest contributors to Fund performance. We trimmed positions in all three holdings during the third quarter, principally on valuation. In November last year, we increased our position in Allergan to 6.0% of net assets at what we believed was an increasingly attractive discount to our estimate of business value. As the stock appreciated and Allergan's weighting in the Fund increased, we elected to sell some shares to keep the position size in line. At just shy of 12 times our estimate of 2019 cash earnings, however, we believe Allergan's prospects remain underappreciated.

Our mission is to maximize our clients' wealth over a period of many years.

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Facebook (-15%), Mohawk Industries (-18%) and LabCorp (-3%) detracted a combined 100 basis points (-1%) from third quarter performance. Facebook, and social media more broadly, remains under a microscope. Our read of the data continues to suggest that user perception is far less negative than that of traditional media and numerous elected officials. This is not to make light of the challenges facing the company. Maintaining the trust of its vast user base is both critical and complicated on a global scale. Facebook's common advertising platform and portfolio of digital properties (Facebook, Instagram, WhatsApp, Messenger) remain uniquely valuable media assets. Never have advertisers of all sizes been able to attain such a specific reach. Nor have users seen curated recommendations with a near-frictionless ability to purchase. These capabilities should further improve over time, providing the opportunity for many years of potentially double-digit organic growth. We added to our Facebook position during the quarter.

Shares of Mohawk Industries, which we began purchasing last quarter, declined as input inflation continues to pressure profitability. The structural characteristics of the flooring markets Mohawk operates in are attractive, as is the company's competitive position in each, but pricing often lags cost increases. Investors appear to envision a fragile demand environment over the next several years, presumably due to higher interest rates, peak-ish employment and softening results for the public homebuilders. While cautious, we are more constructive and believe Mohawk's current stock price (\$170) provides an attractive margin of safety for those with a multi-year investment horizon. We added modestly to our position at the end of July, with room to further increase the Fund's exposure should the stock continue to weaken.

Discount retailer Dollar Tree (-24%) and European cable provider Liberty Global (-17%) join Mohawk (-18%) as the primary detractors from calendar year-to-date performance. The uneven pace of improvement at Dollar Tree's Family Dollar unit over the past 12 months has kept a lid on business value growth and raised concerns that Dollar Tree's rationale for the Family Dollar purchase three years ago was flawed. We continue to see several potential paths to improved performance at Family Dollar, with the Dollar Tree banner's strength providing ballast in the interim. Liberty Global's operating results remain mixed, with improvements in the U.K. offset by ongoing difficulties in Belgium and Switzerland. While we continue to believe the stock is undervalued, we have greater conviction in the ability of domestic cable peer Charter to

grow over the next several years and have focused the Fund's incremental cable purchases there as a result.

The Fund initiated new positions in discount broker turned bank Charles Schwab and aggregates producer Vulcan Materials. We closed the Fund's small position (0.2% of net assets) in Perspecta, which was spun out of DXC Technologies in May. With a \$4 billion market capitalization, it was not aligned with the Fund's larger-company mandate. Schwab is a business we added to our on-deck list several years ago. Since then, the company has methodically gained market share from major banks and traditional brokers, with innovative, low-cost platforms tailored to both individuals and investment advisors. We find ourselves drawn to scale businesses that consistently share the benefits of size directly with their customers. We believe Schwab to be such an enterprise, and the company's results suggest clients continue to "vote with their feet" by bringing new accounts and a greater share of their assets. Using relatively conservative forecasts, we estimate Schwab's intrinsic value to be in the low \$60s today.

We'll close with a brief reintroduction to Vulcan Materials. The aggregates business (stone used for highways and bridges) has long been one of our favorites, boasting high barriers to entry, strong pricing power and minimal risk of obsolescence. Demand for Vulcan's products spans the public works, industrial, commercial and residential end markets. Public infrastructure, which represents roughly half of Vulcan's revenue, has seen sluggish spending over the past several years despite passage of a five-year federal highway bill in late 2015 and increased state and local transportation funding. In our view, visibility into public demand over the next several years is as healthy as it's been in a decade. This should result in healthy unit growth, even if private construction levels cool off for a period of time. The combination of steadily rising volumes and mid-single-digit price increases should drive an attractive stream of double-digit profit growth over our investment horizon, and we estimate Vulcan's price-to-value to be in the 70-75% range.

Quarterly Top Performers (%)	Return	Average Weight	Contribution	Quarterly Bottom Performers (%)	Return	Average Weight	Contribution
Berkshire Hathaway Inc.-Class B	14.71	8.71	1.25	Facebook, Inc.-Class A	-15.37	3.09	-0.50
Allergan plc	14.70	5.82	0.87	Mohawk Industries, Inc.	-18.16	2.01	-0.35
Liberty Broadband Corp.-Series C	11.33	6.35	0.71	Laboratory Corp. of America Holdings	-3.26	4.68	-0.15
Oracle Corp.	17.48	4.25	0.69	Twenty-First Century Fox, Inc.-Class A	-6.39	1.83	-0.13
Mastercard Inc.-Class A	13.42	4.25	0.55	Dollar Tree, Inc.	-4.06	3.50	-0.13

Contributions to performance are based on actual daily holdings. Securities may have been bought or sold during the quarter. Return shown is the actual quarterly return of the security or combination of share classes. Source for return shown is FactSet Portfolio Analytics.

Performance data represents past performance, which does not guarantee future results. *The investment return and the principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. Current performance may be higher or lower than the performance data quoted. Performance data current to the most recent month end may be obtained at weitzinvestments.com.*

Average annual total returns for the Fund's Institutional and Investor Class for the one-, five- and ten-year periods ended September 30, 2018, were 12.38%, 8.25%, 9.55% and 12.13%, 8.06%, 9.46%, respectively. Returns assume reinvestment of dividends and redemption at the end of each period, and reflect the deduction of annual operating expenses, which as stated in the most recent Prospectus are 1.09% (gross) and 1.22% of the Fund's Institutional and Investor Class net assets, respectively. Returns also include fee waivers and/or expense reimbursements, if any; total returns would have been lower had there been no waivers or reimbursements. The Investment Adviser has agreed in writing to waive its fees and reimburse certain expenses (excluding taxes, interest, brokerage costs, acquired fund fees and expenses and extraordinary expenses) to limit the total annual fund operating expenses for Institutional Class shares and Investor Class shares to 0.99% and 1.30%, respectively, of each Class's average daily net assets through July 31, 2019.

Institutional Class shares became available for sale on July 31, 2014. For performance prior to that date, returns include the actual performance of the Fund's Investor Class (and use the actual expenses of the Fund's Investor Class), without adjustment. For any such period of time, the performance of the Fund's Institutional Class would have been similar to the performance of the Fund's Investor Class, because the shares of both classes are invested in the same portfolio of securities, but the classes bear different expenses.

Average annual total returns for the S&P 500 and the Russell 1000 indices for the one-, five- and ten-year periods ended September 30, 2018, were 17.91%, 13.95%, 11.97% and 17.76%, 13.67%, 12.09%, respectively. Index performance is hypothetical and is shown for illustrative purposes only. Comparative returns are the average returns for the applicable period of the reflected indices. The S&P 500® is an unmanaged index consisting of 500 companies generally representative of the market for the stocks of large-size U.S. companies. The Russell 1000® Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000® Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. Russell Investment Group is the source and owner of the trademarks, service marks and copyrights related to the Russell Indices. Russell® is the trademark of Russell Investment Group.

As of September 30, 2018: Allergan plc comprised 4.9% of Value Fund's net assets; Amazon.com, Inc. 2.0%; Berkshire Hathaway Inc.-Class B 7.9%; The Charles Schwab Corp. 2.0%; Charter Communications, Inc.-Class A 1.3%; Dollar Tree, Inc. 3.2%; DXC Technology Co. 1.5%; Facebook, Inc.-Class A 3.1%; Laboratory Corp. of America Holdings 4.6%; Liberty Broadband Corp.-Series C 6.7%; Liberty Global plc-Class C 3.3%; Mastercard Inc.-Class A 3.8%; Mohawk Industries, Inc. 2.0%; Oracle Corp. 4.5%; Twenty-First Century Fox, Inc.-Class A 1.8%; Vulcan Materials Co. 1.6%. Portfolio composition is subject to change at any time. Current and future portfolio holdings are subject to risk.

Included is a reference to the term "margin of safety". This term refers to purchasing securities at a price that is less than our estimate of intrinsic value. A potential "margin of safety" may limit downside risk and optimize the potential for growth.

Investors should consider carefully the investment objectives, risks, and charges and expenses of the Fund before investing. The Fund's Prospectus contains this and other information about the Fund and should be read carefully before investing. The [Prospectus](#) is available from Weitz Investment Management, Inc. Weitz Securities, Inc. is the distributor of the Weitz Funds.