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Weitz Partners Value Investor WPVLX

Not getting it done.

Morningstar's Take WPVLX

Morningstar Rating	★★
Morningstar Analyst Rating	Neutral

Morningstar Pillars

Process	Neutral
Performance	Neutral
People	Positive
Parent	Positive
Price	Negative

Role In Portfolio
Supporting

Fund Performance WPVLX

Year	Total Return (%)	+/- Category
YTD	6.30	-1.52
2016	6.22	-4.15
2015	-9.25	-8.18
2014	7.91	-3.05
2013	30.87	-0.63

Data through 5-31-17

5-26-17 | by Kevin McDevitt, CFA

Weitz Partners Value hasn't produced sufficiently in either its current or former incarnations under its current management. Plus, its high fees create a further hurdle to future success. For these reasons, the fund's Morningstar Analyst Rating is cut to Neutral.

This fund's comanagers, Brad Hinton and Wally Weitz, officially embraced a high-quality strategy in April 2016. But, as they said at that time, this was more an iteration than a sea change. The fund has been moving away from its value-oriented, contrarian roots since the 2007-09 credit crisis. In fact, the fund has since landed in the large-growth portion of the Morningstar Style Box as often as large-blend.

As a result of these shifts, the fund's portfolios have migrated from value to blend to, as mentioned, growth. This makes benchmarking the fund's results somewhat problematic. Arguably, though, the Russell 3000 Index remains the best comparator for this multicap fund.

But no matter which index is used, the fund hasn't delivered. Since Hinton joined Weitz as comanager in August 2006, its 6.5% annualized gain since then lags the Russell 3000 Index by 1.9 percentage points. The fund has not done any better on a risk-adjusted basis, either. To be sure, not all of this falls on Hinton's shoulders. Weitz had been the sole manager since the 1983 inception, and the fund lagged its benchmark by 1 percentage point annualized during the five years prior to Hinton becoming comanager. The fund's record was exceptional during its first 20 years, which is why the fund still beats its index since inception, but it hasn't come close to repeating those results since.

Hindering their efforts is a high expense ratio; what's worse, it has moved in the wrong direction. As of the fund's 2016 annual report, the expense ratio stood at 1.24%, already 34 basis points greater than the large-cap no-load median. But in the December 2016 prospectus, it rose to 1.26%. This higher expense ratio makes the fund's odds of long-term outperformance that much longer. For now, investors are best served looking for cheaper and better options.

Process Pillar Neutral | Kevin McDevitt, CFA 05/26/2017

This all-cap strategy has shifted further in the direction of quality. With a less differentiated approach, the fund's Process rating is cut to Neutral. The team cut the discount rate it uses to value companies to 9% from 12%. This increases a company's estimated fair value and will allow more companies, especially high-quality ones, to enter their target range. Deep-value turnaround plays will be less common, and high-quality compounders more so. The team typically looks for stocks that are selling at 70% or so of their estimated fair value. But the required margin of safety also depends on company quality. Distressed or commodity-oriented companies must be selling at even deeper discounts to draw the team's interest.

The team looks out as far as 10 years when discounting free cash flows or a firm's franchise value, although its investment horizon is usually closer to three to five years. Quality differences between companies are incorporated into valuation estimates through the terminal multiple and the projected return on capital. Firms now receive a quality score of 1-7 across metrics such as competitive position, cash flow consistency, reinvestment runway, return on invested capital, and management quality. Financial leverage will also get greater scrutiny, unlike in the past when high leverage was tolerated. The March 2017 portfolio's 40.4% average debt/capital ratio was below the Russell 3000 Index's 42.0%.

Though this fund has become more growth-oriented, its March 2017 15.5% cash weighting shows management's caution when it comes to valuations. Since 2009, the fund has also shifted its sector exposure, moving into technology in particular while cutting back substantially on financials. Its overweighting in consumer discretionary stocks remains significant at 40.0% of the equity portfolio, though it's still well below the 48% level it reached in early 2010.

With a greater emphasis on quality and reduced financial leverage, the portfolio's average debt/capital ratio has fallen. It reached 47.6% in mid-2015 but fell to 40.4% by March 2017. Quality shows in other ways. Only 5.5% of the companies covered by Morningstar equity analysts do not have a Morningstar Economic Moat Rating versus 13.2% for the Russell 3000 Index. The portfolio's average return on assets was in line with the index's.

The clearest difference between this fund and most large-blend peers is its all-cap mandate. About 47%

of the equity portfolio was in mid- and small-cap stocks versus only about 20% for its typical peer. The fund also has more mid- and small-cap exposure than the Russell 3000 Index, which has a combined 25.7% in such companies. This can make the fund more volatile than either its average peer or the index, although over the long term its standard deviation has been in line with the index because of its cash stake.

Performance Pillar Neutral | Kevin McDevitt, CFA 05/26/2017

During its long history, this fund has been all over the (style) map, which makes its results difficult to assess. The fund has made full use of its all-cap flexibility through the years, so it has little in common with any one peer group or benchmark. (The large-blend large-blend Morningstar Category is its current resting place.) The Russell 3000 Index, which includes the 3,000 largest U.S. companies, is its best comparator.

It's beaten this bogy by 1.2 percentage points annualized since its 1983 inception through April 2017, but most of that outperformance came in the first 20 years of its existence. Indeed, the fund lags the Russell 3000 Index by 1.9 percentage points annualized since Brad Hinton became comanager in August 2006. For this reason, the fund earns a Neutral Performance rating.

The fund's results in down markets are also mixed. It fared better than the Russell 3000 Index during the 2000-02 bear market largely because it avoided inflated tech stocks during the bubble. However, the fund got blindsided by the 2007-09 credit crisis, when it took a 30% financials stake into 2007's fourth quarter. Management now requires a greater margin of safety for its contrarian picks, and its greater caution helped the fund hold up a bit better than the index during 2011's third-quarter correction, although it fared far worse during the 2015-16 sell-off. The fund fell 22% peak-to-trough (May 22, 2015-Feb. 11, 2016) versus the index's 14.9% loss.

People Pillar Positive | Kevin McDevitt, CFA 05/26/2017

This fund's comanager, Brad Hinton, is a nice complement to longtime manager Wally Weitz's areas of expertise. Weitz's comfort zone has traditionally been in media and financials, while Hinton is behind the fund's foray into technology stocks. The duo's experience and complementarity earn the fund a Positive People rating. Hinton joined Weitz as an analyst in September 2001 and has been a comanager here since 2006.

Weitz has been running this fund since its 1983 inception, providing a high level of continuity. The firm has also been successful in retaining talent. This is partly because of Weitz's 2006 decision to sell 2% of the firm each year to employees. The firm's April 1, 2013, name change from Wallace R. Weitz & Company to Weitz Investment Management reinforced this shift to a greater focus on the broader team.

Weitz and Hinton have substantial skin in the game. Both own shares in the fund worth more than $1 million. This fund isn't either manager's only responsibility: Hinton also runs Weitz Balanced WBALX and comanages Weitz Value WVALX with David Perkins. Weitz is a comanager on Weitz Hickory WEHIX, too, and sole manager of Weitz Partners III Opportunity WPOIX. Hinton joined Weitz as co-CIO in April 2017, bequeathing his director of equity research role to Drew Weitz. This move freed Hinton from management responsibilities, giving him more time to spend on portfolios and company research.

Parent Pillar Positive | Kevin McDevitt, CFA 08/13/2015

Weitz Funds gets good marks for stewardship, with the main detractor being the family's slightly above-average overall fees. All of the managers invest in the funds that they run, with firm founder Wally Weitz parking more than $1 million in each of his charges. The independent board members also have significant positions in the funds. As a firm, Weitz has resisted the temptation to introduce trendy funds and has not shown any hint of empire-building. It has a clean regulatory record, too.

Weitz has a strong and established investment culture. Wally Weitz founded the firm in 1983 and is still at the helm, running the advisor and comanaging several portfolios. The equity team is composed of eight portfolio managers and analysts who average about nine years of experience at the firm, excluding Weitz himself.

Admirably, Weitz has worked hard during the past nine years to build the organization behind him. He has promoted internally and in 2006 began selling 2% of the firm each year to employees. Both practices should motivate the team and keep retention strong. The firm's five-year manager-retention rate through July 2015 is 100%. These moves also show a proactive approach to succession planning.

The fund boards have done a good job closing funds before they get too big. However, they haven't cut fees as much as they could. Several funds have above-average expenses.

Price Pillar Negative | Kevin McDevitt, CFA 05/26/2017

This fund's 1.24% expense ratio as of the latest annual report is well above the 0.90% median for its large-cap no-load peer group. What's worse, the latest prospectus (as of Dec. 16, 2016) shows the expense ratio increasing by 2 basis points to 1.26%. The fund's Morningstar Fee Level is High. Quite simply, the fund isn't cost competitive, and thus it receives a Negative Price rating.

The firm introduced an Institutional share class (WPVIX) in July 2014. Its expense ratio is capped at 0.99% with a $1 million minimum, while the expense ratio on the Investor shares is capped at 1.30% through July 2017.

Past performance is no guarantee of future results. Weitz Partners Value Fund-Investor Class (WPVLX) average annual total returns for the one, five, and ten-year periods ended March 31, 2017, were 11.06%, 9.09% and 5.12%. Weitz Partners Value Fund-Institutional Class (WPVIX) average annual total returns for the one, five, and ten-year periods ended March 31, 2017, were 11.39%, 9.22% and 5.18%.The returns above 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 1.26% and 1.07% (gross) of the Fund's Investor and Institutional Class net assets, respectively. The Investment Adviser has agreed in writing to limit the total annual operating expenses of Investor Class shares and Institutional Class shares (excluding taxes, interest, brokerage costs, acquired fund fees and expenses and extraordinary expenses) to 1.30% and 0.99% of the respective Classes' average daily net assets through July 31, 2017.

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 www.weitzinvestments.com/funds_and_performance/fund_performance.fs. Included is a reference to the term "margin of safety." This term refers to purchasing common stock at a price that is less than what a company is believed to be worth, on a per-share basis. A potential "margin of safety" may limit downside risk and optimize the potential for growth. Portfolio composition is subject to change at any time. Current and future portfolio holdings are subject to risk. Investors should consider carefully the investment objectives, risks, and charges and expenses of the Fund before investing. Institutional Class shares became available for sale on July 31, 2014. For performance prior to that date, this report includes 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. 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., 1125 South 103rd Street, Suite 200, Omaha NE 68124-1071, weitzinvestments.com, 800-304-9745 or 402-391-1980. Weitz Securities, Inc. is the distributor of the Weitz Funds.

Weitz Funds, Weitz Investment Management, Inc. and Weitz Securities, Inc. disclaim any liability for information contained in this article and are not affiliated with Morningstar. The Analyst Report states "The firm recently announced that it would lower the fund's management fee to 0.85% but that the overall expense ratio for the Investor share class wouldn't change." For clarification, the Fund's fee schedule for investment advisory fees includes breakpoints, so that the first $1 billion of fund assets is charged 0.90% for investment advisory fees, and the second $1 billion of fund assets is charged 0.85% for investment advisory fees. See the Funds' Prospectus for additional detail.

The Analyst Report states that the expense ratio of WPVIX is 1.18%. This is incorrect. The correct expense ratio is 0.99%.

at least a three-year history, Morningstar calculates a Morningstar Rating™ based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a fund's monthly performance (including the effects of sales charges, loads, and redemption fees), placing more emphasis on downward variations and rewarding consistent performance. The top 10% of funds in each category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars and the bottom 10% receive 1 star. (Each share class is counted as a fraction of one fund within this scale and rated separately, which may cause slight variations in the distribution percentages.) The Overall Morningstar Rating for a fund is derived from a weighted average of the performance figures associated with its three-, five- and ten-year (if applicable) Morningstar Rating metrics. Weitz Partners Value Fund was rated against the following numbers of U.S.-domiciled Large Blend funds over the following time periods: 1,248 funds in the last three years, 1,113 funds in the last five years, and 822 funds in the last ten years. With respect to these Large Blend funds: Weitz Partners Value Fund-Investor Class received Morningstar Ratings of 1 star, 2 stars and 2 stars for the three-, five- and ten-year periods, respectively; and Weitz Partners Value Fund-Institutional Class received Morningstar Ratings of 1 star, 2 stars and 2 stars for the three-, five- and ten-year periods, respectively.

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1125 South 103rd Street, Suite 200 Omaha, NE 68124-1071 t (800) 304-9745 f (402) 391-2125 weitzinvestments.com