Perspective Over Predictions

Weitz | INVESTMENT MANAGEMENT

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In the third quarter, stocks gave back some of their first-half gains. The S&P 500 fell -3.3%, bringing its year-to-date gain to +13.1%. Our stock funds followed a similar pattern. A handful of giant tech stocks continued to account for the lion's share of this year's index gains. Dubbed the "Magnificent Seven" (financial writers can't help themselves), Microsoft, Meta Platforms (Facebook parent), Alphabet (Google parent), Amazon.com, Apple, Tesla and NVIDIA (maker of chips used in AI applications) collectively rose by over 90%, completely eclipsing more moderate gains among other index components.

These ***are*** amazing companies, and we are very happy to own several of them in our funds, but quite a few other very good, albeit less "magnificent," businesses are quietly doing better than their stock prices might indicate. This augurs well for broader-based future returns.

All Eyes are on the Fed

In the meantime, investors and the financial media act as if the only important investment consideration is "How high will interest rates go?" and "How long will they remain high?" We think that it is a mistake to be stuck on this narrow focus.

Two years ago, the Fed acknowledged that higher inflation rates might not be "transitory." They telegraphed a 180-degree change in policy and promised to push short-term interest rates up enough to get the inflation rate down to its 2% target and extinguish inflationary expectations. The relatively rapid increase in the federal funds rate from roughly zero to more than 5% was a shock to the economy and triggered last year's bear market.

The domestic economy has been slowing, and most inflation metrics are moderating. The Fed's campaign seems to be working, and there is general acknowledgement that few, if any, further rate increases will be needed. So far, so good.

But worries persist. Will tight money cause a recession, or will the economy have a "soft landing?" Are rate ***cuts*** necessary to launch a new bull market? What if the anti-inflation campaign fails and inflation flares up again? Anxieties are high.

Perspective Required

We have no short-term answers or trading ideas to offer. We try to invest in a way that does not require clairvoyance. We do have to have some working assumptions about the issues of the day and key economic variables. For clients who are curious, we offer these with humility and a reminder that our opinions can evolve quickly.

- Fed Chair Powell has promised to keep rates high for long enough to be sure inflation is truly under control. He has suggested that this may take a long time – possibly years. The Fed may find success sooner than expected (or its definition of success may be adjusted), but we are assuming that rates will stay around current levels for a very long time. We are not counting on seeing rates near zero any time soon. Maybe ever.
- At current, more historically normal interest rate levels, bonds present much stiffer competition for investor capital than they have for over a decade. Stocks still offer significant advantages over fixed income securities, but their ***relative*** attractiveness declines as interest rates rise. Another way to say this is that price-to-earnings (P/E) ratios generally decline as rates rise. This process is well underway, but stock investors should get over blind hopes for a return to valuation (P/E) levels we enjoyed a few years ago.
- Over the past 20 years, rates stayed within a 0-5% range most of the time. A whole generation of investors and managers have never experienced higher rates. But some remember 1970-2000 when 5% was more

like **the *floor*** for rates that ranged from 5-20%. The quick run up in rates last year caused some financial pain (new home buyers seeking mortgages and banks with too many long-term, fixed-rate loans and bonds), but 5% is ***not*** high by historical standards. Investors and companies have coped with higher rates in the past, and they are already adjusting to today's levels.

- There are always plenty of things to worry about – as citizens, parents, and Earthlings, as well as investors. ***Plenty***. But our assumption is that companies with competitive advantages, smart and flexible management teams, and solid finances will always find ways to move forward, build business value and earn higher stock prices.

Outlook

Investors have been through a lot over the past five years. Some events have been unprecedented. Others represent the "changing changelessness" of human nature. Current preoccupation with Fed policy will pass and be replaced by other uncertainties. We believe that our collection of businesses is positioned to generate healthy returns for us over the next several years. Companies with temporary issues, or that hit the occasional pothole, will offer new opportunities.

Finally, a cause for optimism that deserves a paragraph of its own: Strong companies "make their own breaks." Over the years, quite a few of our portfolio companies have made opportunistic acquisitions during recessions and other times of financial stress or crisis. Some of these have been transformational. We are not predicting or cheering for financial trouble or pain, but these companies' businesses are worth a lot more today because of opportunities born of hard times.

So, we suggest investors look up from the financial news of the day and focus on the 3-5-year horizon.

IMPORTANT DISCLOSURES

The opinions expressed are those of Weitz Investment Management and are not meant as investment advice or to predict or project the future performance of any investment product. The opinions are current through 10/17/2023, are subject to change at any time based on market and other current conditions, and no forecasts can be guaranteed. This commentary is being provided as a general source of information and is not intended as a recommendation to purchase, sell, or hold any specific security or to engage in any investment strategy. Investment decisions should always be made based on an investor's specific objectives, financial needs, risk tolerance and time horizon.

Portfolio composition is subject to change at any time. Current and future portfolio holdings are subject to risk.

Past performance is not a guarantee of future results.

As of 09/30/2023, the following portfolio company constituted a portion of the net assets of Conservative Allocation Fund, Large Cap Equity Fund, Multi Cap Equity Fund, and Partners III Opportunity Fund as follows:

- Alphabet, Inc.: 1.8%, 7.4%, 6.9%, and 6.3%.
- Apple, Inc.: 0.0%, 0.0%, 0.0%, and 0.0%.
- Amazon.com, Inc.: 0.0%, 3.7%, 0.0%, and 4.7%.
- NVIDIA Corp.: 0.0%, 0.0%, 0.0%, and 0.0%.
- Meta Platforms, Inc.: 0.0%, 4.0% 3.9%, and 3.6%.
- Microsoft Corp.: 2.2%, 0.0%. 0.0%, and 3.0%.
- Tesla, Inc.: 0.0%, 0.0%., 0.0%, and 0.0%.

Investors should consider carefully the investment objectives, risks, and charges and expenses of the Funds before investing. This and other important information is contained in the prospectus and summary prospectus, which may be obtained at weitzinvestments.com.

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