VALUE MATTER / 3Q 2024

Balancing Volatility and Opportunity

Weitz | INVESTMENT MANAGEMENT

WALLY WEITZ, CFA ®
Co-Chief Investment Officer
& Portfolio Manager

BRAD HINTON, CFA ®
Co-Chief Investment Officer
& Portfolio Manager

Market Standoff Continued

During the third quarter, money flowed into stocksother than Nvidia and the other "Magnificents" and a broader group advanced. The bond market also got a boost from investor anticipation of the Fed rate cut that finally materialized in September. Read our latest Fixed Income Insights: ***Not So Fast??*** to learn more.

Although major market indices closed the quarter at record highs, investors continue to be unsettled by an ambiguous economic outlook. The Fed's efforts to slow the economy are working. This means that they can begin to cut short-term rates, but it also means that economic growth is slowing, and the labor market is softening. Since monetary policy works with a lag, many fear a further slowdown or even recession rather than the "soft landing" that seems to be priced into the market.

In our opinion, the attention given to the Fed's actions is misplaced. The Fed's policy reversal is positive, but 5–10-year yields are more important to businesses and long-term investors than the Fed Funds rate. Corporations borrow for multi-year periods and the attractiveness of stocks depends on how stiff the competition is from more predictable bond yields.

We believe the three most important factors in assessing the investment outlook are:

1) expectations for "owners' earnings" over the next several years

2) expectations for the average level of 5–10-year yields over that period

3) the level of stock prices at the beginning of the period

On the ***first*** point, with or without a near-term recession, our expectation for economic growth and corporate earnings over the next 5-10 years is positive. Reinforcing our conviction is confidence in the specific group of companies we own. Even if the domestic and/or global economies show subpar growth, good businesses are flexible and resourceful. In short, we feel confident that our portfolio companies will generate growth in business value over the years. So far, so good.

The ***second*** factor is more problematic. The Fed can nudge short rates up or down, but it cannot ***force*** investors to buy the Treasury bonds that finance the government if yields are unattractive. If inflation proves more robust than expected and/or if the quantity of Treasuries for sale is too large, 5–10-year yields may not stay down at today's comfortable, sub-4% level. If Treasury rates rise, yields on other debt instruments will follow.

The litany of potential causes of higher inflation/interest rates is a familiar one.

- Globalization and robust world trade have been deflationary forces over decades. De-globalization/reshoring, tariffs, restrictions on sales of chips and other technology is ***in***flationary.

- Geopolitical tensions and hot and cold wars, aside from the human cost, create inefficiencies and destroy property that must be replaced. Inflationary.

- Climate change's impact on the intensity of fires, floods, and windstorms raises the cost of damages and the costs of insurance and utilities. Further, some policy measures designed to combat climate change are inflationary, e.g. substituting imported LNG for cheaper coal in Europe.

- Trillions in fiscal stimulus have caused budget deficits and national debt to balloon. The political will to address this is missing (witness extravagant campaign promises to spend and cut taxes). At a minimum, an increased quantity debt financing puts upward pressure on interest rates.

The ***third*** factor is valuation—the starting level of stock prices. Investors will differ on whether stocks are currently fairly valued but by a number of traditional measures, stocks in general are expensive. Our appraisals of dozens of our favorite companies, including several that we own, show price to value ratios nearer full value than we would prefer. As companies reinvest their retained earnings and grow their business values, their prices are likely to track higher, but large gains are harder to come by when the starting point is high.

Outlook and Game Plan

We have been coping with inflated stock and bond prices for years now. There is no certainty that valuation logic will return to markets just because we want it to. As Bloomberg reporter Lisa Abramowitz quipped recently, “This is the market where logic comes to die.” Just the same, in our experience, economic reality eventually wins out because investors eventually notice when the emperor has no clothes.

As we work our way through this mixed bag of economic forces, our expectations are positive but modest. Any number of events and scary headlines could cause temporary corrections but a reasonable economy, strong businesses and a gradual moderation of valuations should give us plenty of room for positive returns over the next several years.

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 10/01/2024, 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 9/30/2024, the following portfolio companies 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:

- NVIDIA Corp.: 0.0 C.A%, 0.0 L.C%, 0.0 M.C%, and 0.0 P.3%.

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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