October 8, 2019

Longleaf Partners Small-Cap Fund Commentary

3Q19

Longleaf Partners Funds

Longleaf Partners Small-Cap Fund gained 0.17% in the third quarter, taking year-to-date (YTD) performance to 9.46%, ahead of our absolute annual goal of inflation plus 10%. The Russell 2000 Index declined -2.40% in the quarter and gained 14.18% YTD. Despite the current challenging performance endpoint, the Fund has delivered strong absolute returns and outperformed the Russell 2000 over the long term.

As one of the largest shareholders in the Fund, we are not pleased with our returns over the trailing 1, 3 or 5-year periods. Over the last 3 and 5 years, the Fund's large cash holding (averaging just over 21% in both periods) and our relative underweight to the top performing information technology sector were together responsible for over 100% of relative underperformance in both periods. We have been early – and therefore wrong – in our view that markets were overvalued and due to correct. As a result, we missed the highest-flying sectors and held elevated cash balances, which has been a large drag on our relative returns. While this has been painful in the near-term, we believe that not holding these overvalued pockets of the market and having cash to

---

Average Annual Total Returns for the Longleaf Partners Small-Cap Fund (9/30/19): Since Inception (2/21/89): 10.44%, Ten Year: 11.78%, Five Year: 5.56%, Three Year: 5.03%, One Year:-7.56%. Average Annual Total Returns for the Russell 2000 (9/30/19): Since Inception (2/21/89): 9.27%, Ten Year: 11.19%, Five Year: 8.19%, Three Year: 8.23%, One Year: -8.89%.

Returns reflect reinvested capital gains and dividends but not the deduction of taxes an investor would pay on distributions or share redemptions. Performance data quoted represents past performance. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the fund may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by visiting southeasternasset.com. As reported in the Prospectus dated May 1, 2019, the total expense ratios for the Longleaf Partners Small-Cap Fund is 0.92%.

be a liquidity provider when opportunity arises have positioned us well prospectively to generate long term, risk-adjusted absolute returns.

While our trailing 1-year performance is ahead of the index, the negative absolute returns have been disappointing, with over 100% of absolute underperformance coming from three stocks: CenturyLink, CNX Resources and Realogy. CNX and Realogy were also the largest absolute detractors over the trailing 3 and 5-year periods. The drivers of stock performance for each of the three were unrelated and were a combination of company-specific and broader industry concerns (that also impacted their peers). Over the last 12 months, our values at CenturyLink and CNX have been stable to growing, and we have seen the quality of both investments improve. We have added to both positions and feel that these businesses help position the portfolio for strong future absolute and relative performance. Please check out our recent podcast with CNX Chairman Will Thorndike if you would like to hear more on the company's transformation during our ownership at https://southeasternasset.com/podcasts/will-thorndike-on-cnx-outsiders-and-private-equity/. We also added to Realogy, but more recently its value has declined. It remains one of the most discounted positions in the portfolio today, but it is not a full weight in the portfolio.

We are confident in our ability to deliver strong future performance based on the high quality of the businesses in our portfolio, coupled with our management partners' focus on closing the price-value gap. Some metrics would not suggest that our portfolio is high quality, but we define "quality" as competitively advantaged business that we can understand, run by great partners who will prudently grow free cash flow (FCF) per share over the long term. We do not focus on a trailing volatility measure or a projected revenue growth rate for the next one-to-two quarters. Over the last 10 years, many of our biggest winners were viewed as "low quality" in the short-term, with Texas Industries, DreamWorks and Sonic all far more shorted than their less-volatile peers before they ultimately sold to knowledgeable industry players at values above our conservative appraisals. Our partners at Madison Square Garden, Lamar Advertising and Dillard's were also heavily bet against before they each took actions to grow and unlock value per share that were recognized by the market.

We strongly believe that our five most recent new investments – GCI Liberty, Summit Materials, Lazard, PotlachDeltic and Dillard's – all increased the overall quality of our portfolio. GCI Liberty has great cable assets and top-tier people at Liberty Media whom we know well and have partnered with in multiple ways throughout our history. Summit has irreplaceable assets with pricing power in aggregates and cement, even if these were briefly obscured by bad weather and input cost inflation when we initiated the position. Lazard's high return businesses are well-entrenched and are more defensive than the stock price would suggest. While it is the only one of the five recent purchases whose stock price is currently below our weighted average purchase price, it has been the largest share repurchaser in the portfolio this year, as management has taken advantage of this discount. We have owned the unique timberland assets at Potlach and Deltic three times before our most recent ownership, and the management today is the strongest we have ever seen. Dillard's is generally discounted as a dying department store company run by a management team that doesn't dance to the sellside's quarterly tune, yet we had a great history with the Dillard family in our first round of ownership. We believe the value of the company is now tilted even more to its highest quality real estate; thus, it too is at an all-time high on quality.

Contributors/Detractors

(Q3 Investment return; Q3 Fund contribution)

Summit Materials (15%, 1.17%), the cement and aggregates company, was the largest contributor for a second quarter in a row. The company's aggregates volume grew 4% and pricing grew 8% year-over-year, while cement volumes increased 3% with further positive pricing. Consolidated earnings are still depressed from the Mississippi River's historically extreme flooding, which necessitates expensive truck and rail transport until water levels normalize. As these logistics challenges ease, Summit's margins should rebound, and the company has maintained its strong local market positions and pricing power in a difficult period. Southeastern remains very engaged with multiple parties after filing a 13D last quarter.

CenturyLink (8%, 0.66%), the fiber and telecom company, was another strong contributor after reporting a relatively flat quarter in line with expectations and maintaining free cash flow guidance. We expect the improving sales department and faster pace of new installations to drive accelerated growth in the key Enterprise business in the coming quarters. CEO Jeff Storey and CFO Neel Dev continue to make progress in improving the cost structure, with a further $200-300 million per year of additional cost savings identified and a focus on increasing cash flow. CenturyLink's management has intentionally run off non-core, unprofitable businesses, like low-speed consumer internet and voice, while intelligently investing to expand the network's Enterprise fiber coverage and growing high-margin revenues over the long term. As CenturyLink's Enterprise growth inflects to outweigh the legacy declines later this year and next, we expect both the company's top line and consolidated EBITDA per share to grow. The company trades at a roughly 65% discount to our appraisal today and a multiple of 4-4.5x free-cash flow. We are engaged with management to explore additional options to close the price-value gap, as there continues to be a healthy amount of M&A in the industry at multiples above where we appraise CenturyLink's parts.

Neiman Marcus (-25%, -1.40%), the luxury retailer, was the largest detractor in the quarter as the bonds that we own fell after weak industry results and a lack of Neiman-specific clarity given that the company had yet to report fiscal year-end results as of 9/30. The company's next round of maturities comes due in two years and amount to less than one third of annual EBITDA. The fund's second and third lien notes mature in 2024, with both bonds currently trading at wide discounts to our anticipated recovery values. As high-end competition shrinks, Neiman has both margin help within its own control and several intriguing strategic options that could close the price to value gap quickly.

OCI (-14%, -0.68%), a leading producer of nitrogen fertilizers and natural gas-based chemicals, was also a primary detractor this quarter. The stock price weakness was primarily due to the decline in the methanol spot price, which is strongly correlated to oil, and one-off negative effects of an unplanned shutdown at the company's nitrogen fertilizer facility in Beaumont, TX. To the positive, OCI has significantly de-levered over the past years from >4x net debt/operating cash flow and is targeting a ratio in the 2x range next year. OCI's structurally lower cost position (as a result of low feed-in natural gas costs) and well-located plants, greater volume leverage and embedded optionality from asset monetization position the company well to outperform its peers going forward. CEO Nassef Sawiris, an owner-operator focused on optimizing the capital structure and generating significant free cash flow, is always open to creative strategic outcomes for the company, which we believe are likely in the future.

Portfolio Activity

We added to heavily discounted Park Hotels and Realogy while continuing to buy our newest position in Dillard's, which we initiated in the second quarter. We also trimmed strong performers GCI Liberty and Formula One Group, as both appreciated in the quarter. The pipeline of prospective investments has steadily improved throughout the year after the market rebound in Q1. We have met with and pre-qualified several interesting investment prospects across a range of industries that could come into the portfolio if we get a market pullback.

Outlook

The portfolio ended the quarter with a strongly discounted price-to-value ratio (P/V) in the low-60s% and 13.9% cash, which we can put to work quickly as new opportunities qualify. We expect to see continued progress in our high-quality holdings, as our management partners pursue catalysts that could drive significant near-term payoffs. We believe our more recent purchases outlined at the start of the letter could soon join the "quality in retrospect" list of holdings that have historically gone from most hated to top performers. We are grateful for your long-term partnership and will continue to endeavor to communicate with you as candidly as possible. We recently redesigned our website to enable better access to portfolio information and communication from your portfolio managers. We would encourage you to visit the new site at www.southeasternasset.com.

See following page for important disclosures.

Before investing in any Longleaf Partners Fund, you should carefully consider the Fund's investment objectives, risks, charges, and expenses. For a current Prospectus and Summary Prospectus, which contain this and other important information, visit https://southeasternasset.com/account-resources. Please read the Prospectus and Summary Prospectus carefully before investing.

RISKS
The Longleaf Small-Cap Fund is subject to stock market risk, meaning stocks in the Fund may fluctuate in response to developments at individual companies or due to general market and economic conditions. Also, because the Fund generally invests in 15 to 25 companies, share value could fluctuate more than if a greater number of securities were held. Smaller company stocks may be more volatile with less financial resources than those of larger companies.

The Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3,000 Index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index. An index cannot be invested in directly.

A 13D filing is generally required for any beneficial owner of more than 5% of any class of registered equity securities, and who are not able to claim an exemption for more limited filings due to an intent to change or influence control of the issuer.

EBITDA is a company's earnings before interest, taxes, depreciation and amortization.

Operating Cash Flow (OCF) measures cash generated by a company's normal business operations.

Free Cash Flow (FCF) is a measure of a company's ability to generate the cash flow necessary to maintain operations. Generally, it is calculated as operating cash flow minus capital expenditures.

P/V ("price to value") is a calculation that compares the prices of the stocks in a portfolio to Southeastern's appraisal of their intrinsic values. The ratio represents a single data point about a Fund and should not be construed as something more. P/V does not guarantee future results, and we caution investors not to give this calculation undue weight.

As of September 30, 2019, the top ten holdings for the Longleaf Partners Small-Cap Fund: CenturyLink, 8.8%; Summit, 8.5%; Kodak, 7.9%; Graham Holdings, 6.7%; GCI Liberty, 5.8%; Mattel, 5.1%; PotlatchDeltic, 4.8%; Lazard, 4.6%; OCI, 4.1%. Fund holdings are subject to change and holding discussions are not recommendations to buy or sell any security. Current and future holdings are subject to risk.
Funds distributed by ALPS Distributors, Inc.

LLP000950
Expires 1/31/2020