



Longleaf Partners Fund Commentary

Longleaf Partners Fund made substantial gains throughout the year, rising 20.72% in 2016, a large premium over the S&P 500's 11.96% return. The Fund's outperformance began in mid-February and occurred in spite of higher-than-normal cash in the portfolio. In the fourth quarter, the Fund appreciated 2.03% while the S&P 500 added 3.82%, most of which came following the presidential election.

The Fund outperformed in two distinct market environments. Over the first seven months of the year, the pursuit of high yield and low volatility dominated. Then more cyclical stocks took over, with over half of their last five month returns occurring in November. The Partners Fund's successful performance had little to do with the index's return. We had limited exposure to the markets' preferences in either period.

Solid operational performance and smart capital allocation by our management partners who pursued value accretive transactions drove the Fund's substantial results. The company-specific nature of our 2016 return reinforced the importance of investing with a long time horizon and aligned, shareholder-oriented capable corporate leadership. While it is difficult to predict near-term stock prices, if our businesses are selling at a meaningful discount to their intrinsic worth, are growing free cash flow over the long term, and are run by people who are motivated to build value per share, good returns can be expected. These same characteristics describe our current holdings, are the criteria required for new investments, and therefore form the basis for our confidence in our ability to continue to deliver solid results.

Annual Contributors/Detractors

(2016 investment return; 2016 Fund contribution)

Chesapeake Energy (+377%; +8.46%), one of the largest U.S. producers of natural gas, oil, and natural gas liquids, was the Fund's top contributor to performance in 2016 and gained an additional 12% in the fourth quarter. Earlier in the year, we transitioned our equity position into heavily discounted bonds and convertible preferred stock, which offered equity-like returns higher in the capital structure and a potentially faster payback. As the bonds rose close to par, we exited them. At the end of the third quarter, we converted all of our appreciated preferred securities into common stock for an attractive premium. Over the course of the year, management executed beyond expectations, selling various assets, improving the

balance sheet through discounted debt repurchases, reducing operating and capital expenditures, and renegotiating midstream contracts. The most recent asset sales in the fourth quarter included a portion of the company's properties in the Haynesville Shale in northern Louisiana for proceeds of approximately \$915 million. Signed or closed asset sales reached \$2.5 billion in 2016, exceeding management's original target of \$1 billion. To further strengthen its balance sheet, the company secured a term loan and convertible debt offering, which raised more capital at better terms than expected. Since the beginning of 2012, Chesapeake has reduced debt by 50%, and its remaining fixed liabilities should be well covered in the coming years. The company has targeted a two times net debt over earnings before interests, taxes, depreciation, and amortization (EBITDA) with cash flow neutrality by 2018 and 5 to 15% of annual production growth by 2020. We salute CEO Doug Lawler and Chesapeake's board, with Brad Martin as Chairman, for their successful pursuit of shareholder value in the face of massive headwinds.

CONSOL Energy (+131%; +3.96%), the natural gas and Appalachian coal company, also contributed large gains over the year. CEO Nick Deluliis, management, and the board, led by Chairman Will Thorndike, monetized assets and continued to cut costs in the pursuit of separating the coal and gas businesses which is expected to happen in 2017. Following the disposition of its metallurgical coal assets in the first half of the year, CONSOL sold its high cost Miller Creek and Fola thermal coal mines to a private buyer at a price above our appraisal. The company also delivered positive free cash flow (FCF) for the year, which many thought very unlikely at the start of 2016. In the fourth quarter, CONSOL announced the unwinding of a joint venture with Noble Energy in which the company received \$205 million in cash from Noble while maintaining ownership of valuable EBITDA-producing properties. Recent transactions involving other companies' gas assets in Appalachia, as well as CONSOL's own midstream master limited partnerships' (MLP) prices, support our appraisal of CONSOL, which is much higher than the stock price.

Wynn Resorts (+28%; +2.29%), the luxury gaming and hotel operator with prime real estate in Las Vegas, Macau, and Boston, was another significant contributor during the year, despite a slight retreat in the fourth quarter. The total Macau market reported higher gross gaming revenues year-over-year

Average Annual Total Returns (12/31/16): Since Inception (4/8/87): 10.42%, Ten Year: 3.20%, Five Year: 9.63%; One Year: 20.72%

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 longleafpartners.com.

As reported in the Prospectus dated May 1, 2016, the total expense ratio for the Longleaf Partners Fund is 0.93%. The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.50% of average annual net assets.

in most months of the second half, indicating stabilization and a return to growth. In August, the company opened the Wynn Palace in Cotai (Macau). The property has ramped up more slowly than some analysts had hoped, but Wynn has a history of careful openings and eventual success. During the fourth quarter, sentiment shifted up and down, as some positive industry level data points were offset by concerns over Chinese policy changes that could potentially impact Macau indirectly. In the U.S., Las Vegas had solid results, and the company received the final licenses necessary to begin construction of Wynn Boston Harbor, which is expected to open in 2019. Wynn also announced plans to develop part of its Las Vegas golf course property into a hotel, restaurants, and other attractions. In December, the company sold 49% of its retail assets in Las Vegas for over twenty times EBITDA, which was accretive to our value and well above where the stock trades. The sale was also further evidence of how our heavily-aligned partner, Steve Wynn, continues to build value per share and pursue value recognition for shareholders.

FedEx (26%; 2.16 %), the global transportation and logistics company, was also a leading contributor for 2016 after gaining 7% in the fourth quarter. The company raised guidance for fiscal year 2017 and continued to buy back its discounted shares. Our appraisal increased as expense reductions in Express over the last several years helped raise margins. Investing in growth at Ground depressed margins in that division but should have meaningful payoff longer term. The TNT acquisition, finalized in May, should materially benefit profitability by increasing the final mile density of FedEx's business across Europe. Management indicated that the integration of TNT should generate at least \$750 million of annual synergies across its network over the next few years. We believe that CEO Fred Smith and his capable leadership team will continue to drive value growth for shareholders.

Scripps Networks (+32%,+1.92%), the media company whose three main brands are HGTV, Food Network, and Travel Channel, had solid advertising revenue gains during the year, and the stock continued its rise in the fourth quarter, gaining 13%. Ratings were strong overall in 2016, and HGTV ended up as the third most watched U.S. cable channel behind ESPN and Fox News. The company's advertising has more exposure to stable categories than most competitors and also earns premiums per viewer over the competition. The year did see a decline in distributor fees paid to Scripps, but this was due to one-time items that will be lapped next year. Part of the stock's discount is related to international expansion which has not yet produced profits but has created startup costs and non-cash amortization. Scripps' high-profile lifestyle channels could be valuable content for other media and entertainment companies, as evidenced by AT&T's recent bid for Time Warner at an attractive multiple relative to Scripps' stock price.

Level 3 Communications (+4%; +031%), a global fiber and integrated communications network company was the primary contributor to the Fund's fourth quarter return. The stock rose 22% with the announcement of a merger with CenturyLink, Inc., equating to \$66.50 per Level 3 share, a 42% premium to the closing price prior to the announcement. This deal offers

numerous benefits for shareholders. The combined company will increase the capacity and reach of CenturyLink's domestic and Level 3's global high-bandwidth fiber networks. Although CenturyLink has been tainted by the performance of its legacy landline business, its Qwest fiber network is a high quality asset. Projected synergies total \$975 million, with \$125 million in reduced capital expenditures and the remaining \$850 million split in half between operating expense reductions and moving data usage onto the company's own network. Additionally, Level 3 will get four directors on the new board. CenturyLink CEO Glen Post has announced that the new CFO will be Sunit Patel who has successfully integrated large acquisitions and managed balance sheets well in his tenure at Level 3.

CK Hutchison (-14%; -1.59%), a global conglomerate comprised of five core businesses (retail, telecommunications, infrastructure, ports, and energy), was the Fund's only noteworthy detractor for the year. The stock declined in the first half of 2016 in the wake of the rejection by European regulators of its acquisition of U.K. telecom company O2, in addition to Brexit which created concerns about the impact on the company's sizable operations in Europe and the U.K. Following a strong third quarter where the company announced a merger creating the largest Italian mobile operator, the stock lost ground in the fourth quarter after the U.S. election. A stronger U.S. dollar and expectations of tougher trade weighed on Hong Kong stocks in general and on the Hong Kong dollar's relationship to the British pound and euro, where over half of the company's earnings before interest and taxes (EBIT) originate. Our owner-operator partners, Victor Li and his father Li Ka-shing, continued to focus the company on its core competencies by selling its aircraft leasing business during the quarter.

Annual Portfolio Activity

Given the long running bull market and additional rise in 2016, finding new businesses that met our requisite discount proved challenging. Additionally, with our strong returns, prices of many holdings grew closer to appraisals, and some of the biggest performers became more heavily weighted in the portfolio. We trimmed a number of positions and exited **McDonald's**, **Aon**, and **National Oilwell Varco** in the first quarter, as well as **Philips** in the third quarter. Cash rose in the portfolio during the first quarter and remained in the teens throughout the year. We were able to buy two new investments in the Fund—**Ralph Lauren** in the second quarter and **T. Rowe Price (TROW)** in the fourth. TROW is a diversified investment advisory firm with a dominant position in U.S. target date fund retirement assets, which account for about twenty percent of assets under management (AUM). TROW's funds have performed well and had net inflows, even with the active management headwinds the industry has faced. Over the last ten years, the company has put capital into building its international investments and distribution. The company currently has just below twenty percent of AUM in international funds and a mid-single digit percent of total AUM coming from offshore investors. As this business grows, margins should rise accordingly. The company's balance sheet has net cash, and we are confident in the aligned management

team who has a record of prudent capital allocation

Outlook

The Fund's price-to-value (P/V) in the low-70s% offers attractive upside. Much uncertainty remains as to how U.S. tax, trade, and regulatory policies will change in the new administration. More volatility, lower market correlations, and higher interest rates would likely unearth new opportunities for the Fund's 18% cash. For example, we are already beginning to find more prospects in healthcare following the sector's decline amid controversies around drug pricing and questions over the future of the U.S. system.

Most importantly, we believe our companies can grow their values substantially and have the ability to deliver good returns in a variety of scenarios. For example, our two largest holdings, Level 3 and FedEx, as well as LafargeHolcim, benefitted from merger activity in 2016 and have significant revenue prospects from their combinations that are not included in projected synergies, and they have skilled leadership with experience at successful company integrations. We hold numerous other businesses that have had meaningful capital investment programs over the last few years that should begin to generate returns in 2017 and beyond. These include Wynn's newly opened Palace in Macau, United Technologies' Pratt jet engines, T. Rowe's international business, and varied projects at Alphabet. As 2016 showed, CEOs and boards who are competent and shareholder-oriented create value. Our corporate partners, as well as the quality of our businesses, give us confidence in our future prospects.

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 longleafpartners.com. Please read the Prospectus and Summary Prospectus carefully before investing.

RISKS

The Longleaf Partners 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. Mid-cap stocks held by the Fund may be more volatile than those of larger companies.

The S&P 500 Index is an index of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe. An index cannot be invested in directly.

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.

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.

Master limited partnership (MLP) is, generally, a limited partnership that is publicly traded on a securities exchange.

EBIT is earnings before interest and taxes.

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

Brexit ("British exit") refers to the June 23, 2016 referendum by British voters to leave the European Union.

As of December 31 2016, the holdings discussed represented the following percentages of the Longleaf Partners Fund: Chesapeake Energy, 4.5%; CONSOL, 6.1%; Wynn, 5.9%; Scripps, 4.8%; FedEx, 9.5%; Level 3, 9.7%; CK Hutchison, 6.1%; Ralph Lauren, 3.5%; T. Rowe Price, 2.5%. Fund holdings are subject to change and holdings discussions are not recommendations to buy or sell any security. Current and future holdings are subject to risk.

Funds distributed by ALPS Distributors, Inc.