## Dear Investor

**Q1 2006 fund return: 9.88%**

Sparinvest Global Value gained 9.88% in the first quarter of 2006. This performance compares with a 3.91% return of the MSCI World Index, and it is therefore satisfactory in both relative and absolute terms.

The table below presents the return for the fund in the first quarter of 2006 and 2005 compared with different stock market indices:

| | Q1 2006 | 2005 |
|---|---|---|
| **Sparinvest Global Value (EUR)** | **9.88%** | **31.39%** |
| MSCI World Index | 3.91% | 26.17% |
| MSCI World Value Index | 4.39% | 26.24% |
| MSCI World Small Cap Index | 8.84% | 33.33% |

*MSCI World Index, MSCI World Value Index and MSCI World Small Cap Index are all indices that contain a broad selection of companies from all over the world. All returns on investment are in EUR.

**Economics**

This quarter, the Federal Reserve continued to raise interest rates and its new chairman, Ben Bernanke, chose to follow the hard stance against inflation inherited from Alan Greenspan with an additional rate hike after the March FOMC meeting. In Europe, the ECB raised interest rates by 0.25% in February. This decision was questioned by the analyst community as market participants saw very little inflationary pressure and feared that too many ECB interventions could jeopardise the economic upturn. But very soon the ECB was proven right when March statistics revealed a record growth in several leading indicators including the German Ifo-index.

The US economy will continue to set the macroeconomic agenda in 2006. The latest trade and current account statistics point towards the largest ever current account deficit. Americans borrowed 7% of GDP abroad during the fourth quarter of 2005. Obviously, this is not a sustainable level of spending but, nonetheless, the market questions whether or not we will see additional US rate hikes in 2006.

From an overall perspective, the business climate is still first rate. Globalisation has taken effect and most economies seem to tolerate higher growth levels before inflationary pressure kicks in. This, in turn, means that interest rates can be kept at a fairly low level from a historical perspective allowing cheap financing of corporate investments, housing and private consumption and demand.

The only issue to embitter the corporate joy is the record high oil prices. With Iran flexing its military muscle and insisting on developing uranium enrichment capabilities for energy production – despite having the second largest proven oil reserves in the world – there is little reason to expect less tension in the Middle East and a significantly lower oil price in the near future.

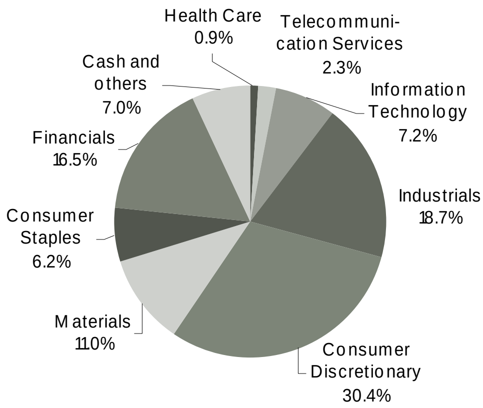
On the bright side, Japan continues to report that its economy expands at a steady rate and, furthermore, there are signs that the growth is finally driven by private domestic demand. Industrial production and consumer confidence also remain strong.

**Fund update**

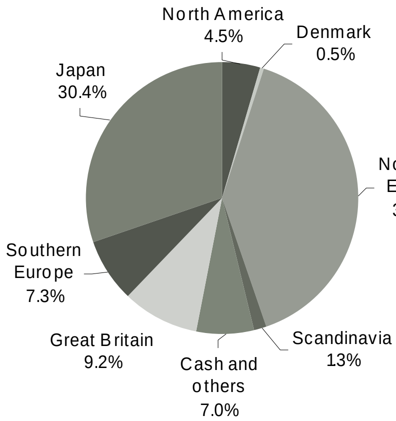
3 new investments and several takeover approaches

At the end of the quarter, the cash position was 6.96% of total capital. The assets are invested in 101 companies with the following industry and country breakdown:

**Sector allocation**




**Geographic allocation**




The 10 largest positions make up 29.84% of the total portfolio holdings:

| Capital | Sector | Share |
|---|---|---|
| Volkswagen AG | Consumer Discre. | 3.40% |
| Salzgitter AG | Materials | 3.29% |
| Man AG | Industrials | 3.19% |
| Fraport AG | Industrials | 3.04% |
| BAA Plc | Industrials | 3.03% |
| Mitsui Sumitomo Ins | Financials | 2.86% |
| Hochtief AG | Industrials | 2.86% |
| Nipponkoa Insurance | Financials | 2.82% |
| Peugeot | Consumer Discre. | 2.74% |
| J. Sainsbury | Consumer Staples | 2.61% |

During the quarter we sold our shares in Japanese Hitachi-Koki and Scandinavian Airlines System (SAS). We made additional investments in 66 companies, and we bought the shares of three new companies.

The additions are Swiss semiconductor manufacturer Micronos, Danish shipping and oil conglomerate AP Moller Maersk and the Swiss Banque Cantonale Vaudoise.

We had takeover approaches or bids for six of our holdings. The Spanish construction company Grupo Ferrovial made an offer of 810 pence a share for British airport operator BAA in February. BAA is mostly known for running one of the largest and busiest airports in the world, London Heathrow. The BAA board immediately rejected the offer claiming that it was nowhere near a fair valuation of the stock. Now, private equity funds are rumoured to be waiting on the sidelines to join the fight over BAA. But one of the most likely bidders, Australian Macquarie, the recent buyer of Copenhagen Airports, decided to cut a deal with Ferrovial instead. A group of large BAA holders have indicated that Ferrovial would get more traction with a bid above 900 pence a share.

Another British holding, De Vere Group, an owner of luxury hotels, received an approach about a possible takeover. The company chose not to disclose the suitor but analysts expect Spanish NV Hoteles SA to be the most likely bidder. Private equity fund Blackstone supposedly made an 800 pence per share offer for a 13% stake after competing private equity fund Permira approached De Vere in December and suggested a buyout.

Yet another UK company, House of Fraser, was approached by private equity fund Apax Partners offering to finance a management buyout. In mid-March, House of Fraser, the third-largest UK department store chain, announced that the talks had ended and its shares fell to their pre-offer level.

At Dutch manufacturing conglomerate, Stork, the CEO announced in February that the company was investigating the pros and cons of going private. Later, at the shareholder meeting in March, the two largest shareholders indicated that they favoured a public-to-private transaction because this would help Stork reach its full potential.

Finally, the press reported two weeks ago, that Paris-based Thomson SA, the world's largest maker of set-top boxes, would receive a EUR 5 billion offer from a group of banks. That same week, the shares of Swiss travel operator Kuoni Reisen jumped 15% on improved sales figures and unconfirmed takeover speculation.

**Hitachi Koki**
Target reached

The Japanese company Hitachi Koki operates in two distinct business segments: power tools and life-science products. The entrance barriers in these industries are very high, and Hitachi Koki has more than half a century's worth of experience as one of the market leaders. In 2002, the strength of the company's balance sheet and future long-term profit potential was attractive. Furthermore, the management focused on streamlining the operations and lowering the cost structure of the company.

At that point, the company was entirely free of debt, and its shares were trading around half of book value.

We bought Hitachi Koki shares in September 2003 at a price of 487 JPY. Although we do not seek to be market timers, this turned out to be a very attractive buying point. At the time, Hitachi Koki had experienced a period of declining sales and had lost one quarter of revenue year over year. Not long after, the situation improved significantly, and the share price has climbed steadily ever since. In January, Hitachi Koki reached our intrinsic value target, and we sold off at an average price of 2,040 JPY per share. This translates to a nominal return of 329% and an annual return of 84%.

**SAS**
Target reached

Scandinavian Airlines System is the largest airline in the Nordic region. The company operates routes to and from Scandinavian cities for transportation of passengers and cargo. The company is also a part owner of several local airlines, a member of the well-known Star Alliance and flies to destinations worldwide. Like most other airlines, SAS has been through dire straits after 9/11. Record high fuel prices further worsened the outlook.

However, management had a clear cost-cutting and core-competency focused strategy on how to return to profitability. At the same time, they were willing to sell off significant parts of the business, to focus on profitable routes and launch some very tough rounds of layoffs. SAS presented a three-year plan in 2002 and we bought our first stake in June 2002 at around DKK 51 per share.

SAS did keep their promise and regained profitability in Q4 of 2005. We sold in January at an average price of DKK 82.9 as the company reached our intrinsic value target. This compares to a nominal return of 62.5% and a weighted annual return of 16.5%.

**The near future**

Last quarter we emphasised, that investors should not expect stocks to perform as well as the global stock market has done during the last three years. In general, we refrain from providing guidance to our investors and we never try to set short-term return expectations. Having said that, we are of course pleased with the first quarter performance but find it somewhat unlikely that this pace can be maintained and that this kind of performance will continue in the quarters to come.

We remain disciplined and continue to focus on downside risk before looking at potential return. As always, we prefer companies with a wide margin of safety in terms of asset backing i.e. hidden value in land, property, plant and equipment - and at the same time we demand that the companies have long-term stable earnings potential. We are still able to find healthy and undervalued companies around the world. By the end of Q1, our portfolio had an average price to book ratio of 1.47 compared with 3.83 for the MSCI World Index.

Like all other trades in life, value investing is a wide concept with generous room for interpretations. In this context, however, it is fair to state that Sparinvest Global Value belongs to the very conservative end of the spectrum. The persistent discipline in the investment process demands that our investors should be ready to accept lower-than-market returns in the short term in order to achieve a higher-than-market return in the long run. The risk of permanent loss of capital in Sparinvest Global Value is limited, and the upside potential continues to be very satisfactory. We have a genuinely positive view of the potential of our investments in the future.

Yours sincerely,

Sparinvest Asset Management

Jens Moestrup Rasmussen
Head of Equities and Lead Portfolio Manager
April 4th, 2006

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