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## Quarterly Newsletter

N°4, FEBRUARY 2009



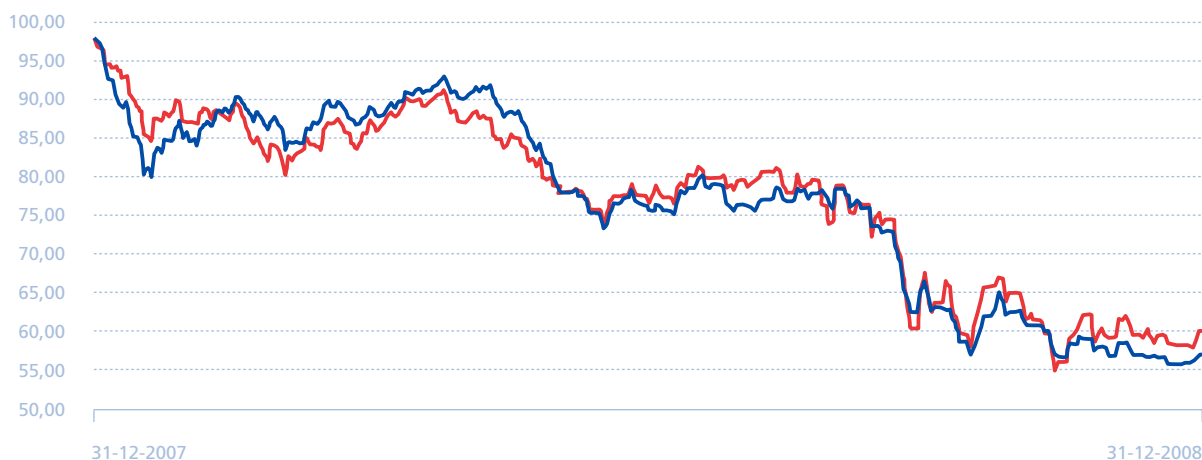


- The trend marked throughout 2008 was unchanged at the end of the last quarter. October was a particularly gloomy month (with drops of over 15%) and the equity markets hit fresh lows in November and December. Our model portfolio (reflected by Bestinver and our Bestinver Global pension fund) made a quarterly loss of 22.9% vs. a decline of 19.9% by the benchmark index.
- On a yearly basis, the performance of our model portfolio reflected by Bestinver (-42.1%) was largely in line with its benchmark (-39.3%). Companies in all countries and industries are falling sharply, although in 2008 Commodities, Banks & Insurance and Real Estate & Construction were the most heavily penalised sectors. We had been avoiding these sectors – where many companies have suffered a significant and permanent loss of value – for many years.

## BESTINFOND

## 2008 Performance

● BESTINFOND ● INDEX (70% MSCI World Index 30% IGBM)

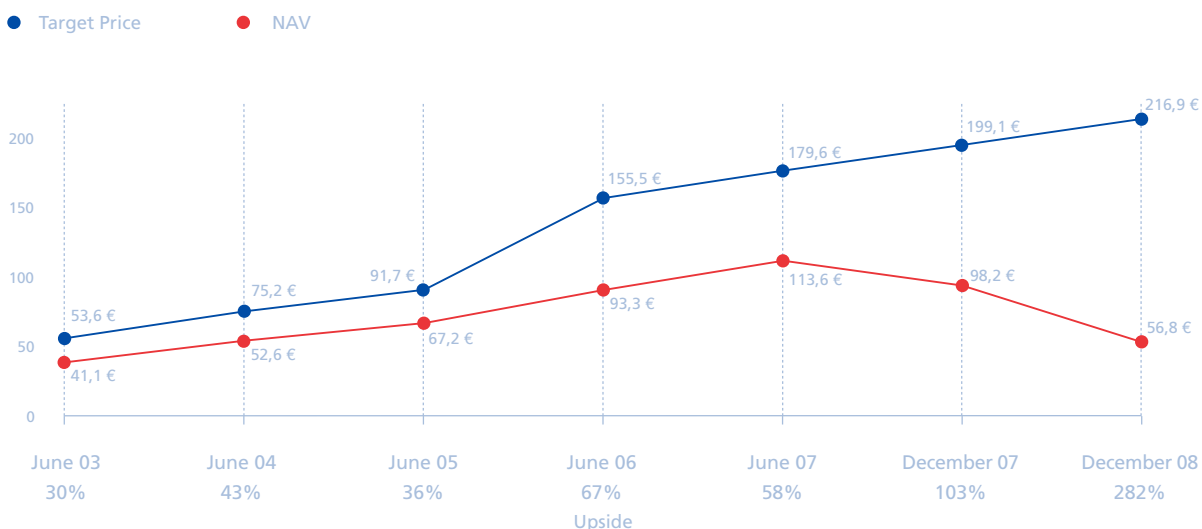


► Bestinver invests in 70% international equities and 30% Iberian equities.

- In 2008 Bestinver's target price increased by 9%, and this, coupled with the drop of 42% in its NAV gave the fund strong upside of 282%.

## BESTINFOND

## Gap between target price and NAV.



BESTINFOND	31-dic-07	31-dic-08	Chg. %
Target Price (€ /sh)	198,5	216,9	9%
NAV (€ /sh)	98,2	56,84	-42%
Upside	102%	282%	
P/E (2009 estimated FCF)	7,4 x	3,9 x	

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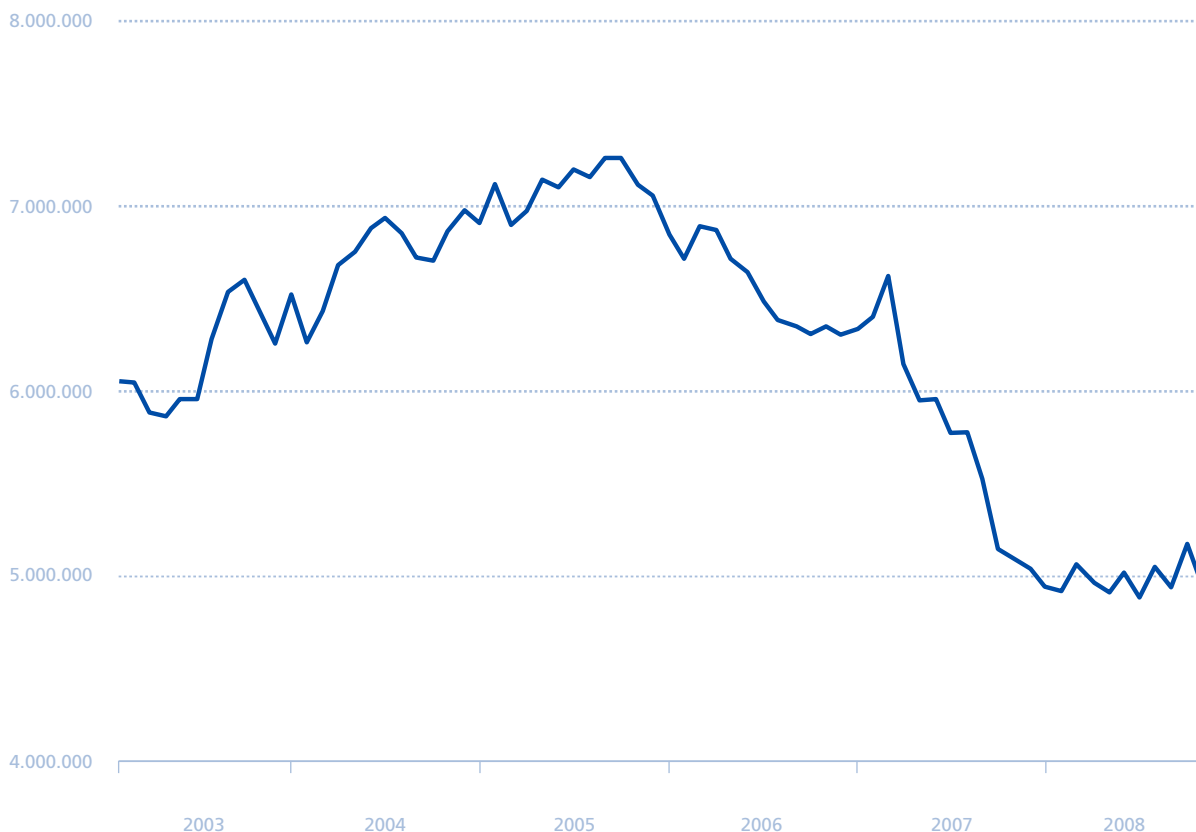


## The Current Environment.

Throughout the year investors have been asking why we have not been able to avoid losses during this slump as we did in other difficult years (1994, 2000, 2001 and 2002). The main reason is that this time **the market is not discriminating and equities are being used as the chief source of financing for private individuals, companies and public institutions alike.** With the credit and real estate markets paralysed, throughout 2008 equities have been the **preferred asset to cover liquidity requirements** (see charts).

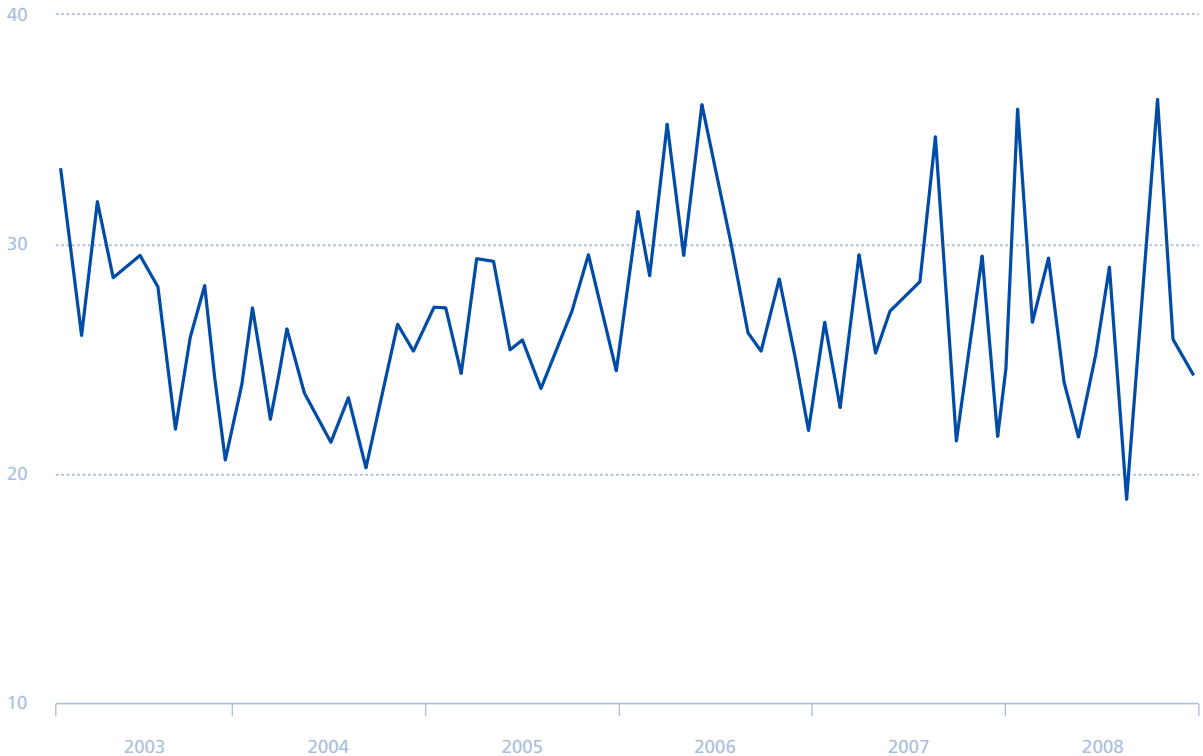
### HOME SALES U.S.A.

### 2003-2008 Performance



## S&P 500 VOLUME TRADED

2003-2008 Performance



This has caused share prices to tumble across the board, including those of most of the companies on our portfolio, even though the underlying trend and outlook for their business has suffered no permanent damage. This is not the first time this has happened, but the movement has never been so intense. However, we would reiterate that this scenario should not be seen as a reason to adopt a more conservative stance but as an extraordinary opportunity to invest at prices that are not frequently seen. For instance, Smurfit Kappa (a company we hold on our portfolio that is a viable business) has dropped 90% from highs, as has Fortis, which is now on the verge of bankruptcy.

Now more than ever it is important to remember that short term earnings (time horizon of less than three years) are not an indication of a fund manager's success or failure. Value Investing offers returns that outstrip the indices in the long term but a manager with an excellent long-term track record may obtain a short-term return that falls short of his benchmark. For instance: In his speech entitled "*The Superinvestors of Graham-and-Doddsville*" Warren Buffet pointed out seven US managers who had obtained a higher yield than the market (8% - 16% higher than the S&P 500 for terms between 13 and 28 years). Despite these impressive long-term results, none of these managers had succeeded in beating the index every year. And six out of the seven even underperformed the market 20%-40% of the time. This shows how **higher-than-average long-term results are perfectly consistent with more lacklustre short-term results, which may even fall short of the index.**

Therefore, we believe that investors should take advantage of the slightly below-index returns obtained by our funds since July 2007 (last high) to invest any idle cash and above all should not jump to the erroneous conclusion that our management is at fault. Equity funds in both Europe and the US are experiencing record levels of redemptions. **Private investors as a whole tend to make mistakes when deciding when to buy and when to sell.** Something similar –although in the other direction- occurred at the end of the 1990s when investors put more cash into equity funds than at any other time in history. Not only was their timing wrong, but so was their chosen asset: they were selling value funds that had dull and undervalued companies on their portfolios to buy into technology sector funds. After three years these had lost between 60% and 90% of their value and some may take decades to recover. Many never will.

This self-destructive behaviour has also been seen in bear markets: nervous investors convince themselves that things can only get worse and that the best move is to sell their equity holdings with a view to buying again when the uncertainty has been dispelled. **At Bestinver we believe that there is no need to shy away from uncertainty - it should be taken advantage of. Investment in equities will always be fraught with uncertainty. Things are never clear-cut on the equity markets, and when they are it is too late to take advantage of them.**

In our view, investors who hold onto their investments will be well rewarded for giving liquidity to those who desperately want to unload their investments. As Warren Buffett said recently in an article published in the New York Times (available on our website) **now is not the time to cling to cash or invest in long-term assets**. Firstly, because these are the worst possible assets for maintaining/increasing purchasing power on a long-term horizon, particularly if the massive liquidity injections and cheaper credit being introduced by all the world's governments eventually give rise to a new inflationary spiral. And secondly, because the opportunity cost of being out of the market now, after the 60% fall from highs, could be sizeable.

In this Quarterly Newsletter we are merely reiterating the points we discussed in earlier editions, and we hope to be able to expand upon these at our annual investors' conference in March.

# International Portfolio



Over the last quarter our international portfolio generated a negative yield of 26%, returning a negative yield of 44.7% over the year, compared to a -39.1% performance by its MSCI benchmark. In the long term, the fund continues to outperform the index, by an annual average of 4.5% and 11.1% for the last five and 10 years, respectively.

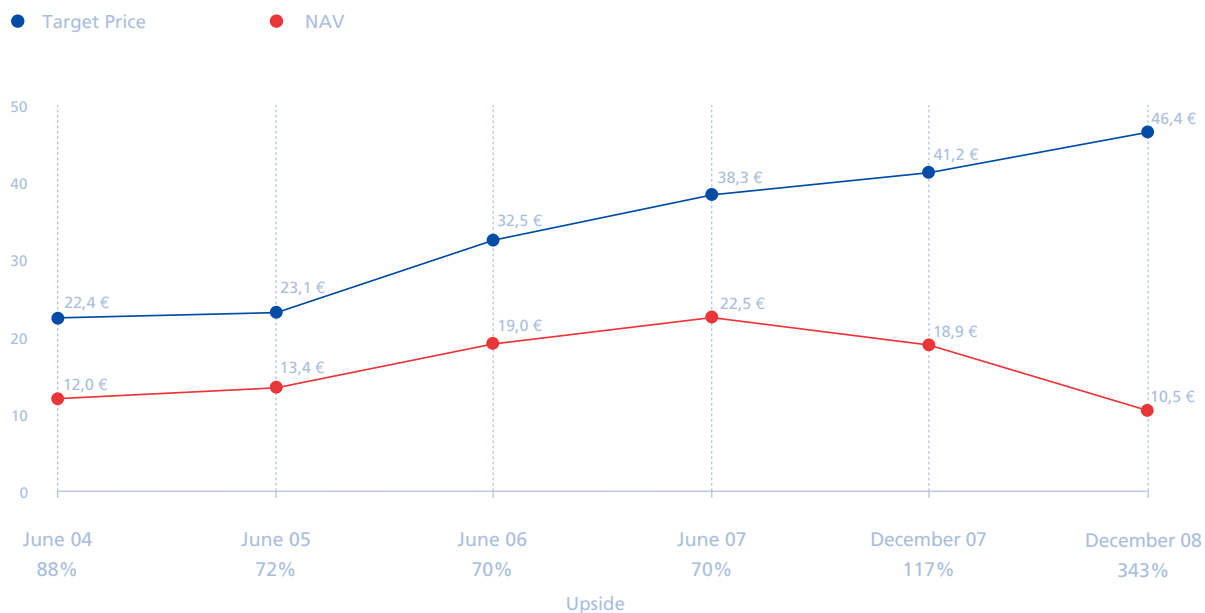
As we have mentioned in previous newsletters, the performance of our portfolio is being dragged down by the market in the short term, even though **it is not exposed to core of the problem (banking and real estate sectors, where we have no exposure whatsoever) and companies with high debt levels account for only 10% of its make-up** (in any case the maturities calendar is relatively undemanding).

In light of the latest downgrades to forecasts for global economic growth, we have cut 28 of our company valuations, raising them in just two cases. However, we would insist that this reduction in value will be temporary for most of the companies affected, 24 of a total of 28. And it is important to note that the price falls on those investments where we have marked down our value are by no means proportional (with prices falling twice or three times more than the drop in value).

This is one of the typical investment opportunities used by value investors to obtain high long-term returns. For instance, some of our investments where values have fallen furthest have doubled or even tripled from lows, or consider the UK company Debenhams whose share price rose 45% in the first few days of January after releasing better-than-expected sales figures. This explains why at the date this newsletter is written Bestinver Internacional's NAV has increased by 5% since the beginning of the year, 2% higher than the benchmark index. Although these examples are not intended to overrate the significance of the underlying trend, they are a reflection of how far and how rapidly market expectations can be revised in just a few days even after a year (2008) when the stock market slump equalled or exceeded historic records.

## BESTINVER INTERNACIONAL

## Gap between target price and NAV.



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The most striking event affecting our international portfolio in the last quarter was the sale of our holding in Ciba, as announced in a press release issued on 13 November, at a price of CHF49.5/sh. On 15 September 2008 we stated that we would not accept Basf's offer at CHF50/sh as our valuation of the company was higher than this (it was later "confirmed" by the projections made by Ciba's management team in the fairness opinion for the takeover bid which set a target price in the range of CHF80-87/sh).

Although it is highly possible that the shares might have reached our target price in the course of 2009-2010, we took the view that the adverse conditions in the financial markets would rule this out in the short term. Also, October brought a further severe correction to equity markets, which allowed us to reinvest the proceeds of the sale at even more attractive prices (the MSCI had fallen by 20.3% since then and the Swiss franc has gained 6.5%, equating to 26.8% outperformance). **We estimate that reinvesting the capital obtained from the sale of Ciba led to an increase in target price of approximately €3.5 per unit for Bestinver Internacional.**

This reinvestment forms part of our habitual strategy of exchanging stocks with lower upside for others with significantly higher upside. Specifically, we have increased our investment in companies we already held on our portfolio, such as BMW, CIR-Cofide and Alapis, increasing their relative weight in our funds, and bought into companies where we had previously been shareholders and sold those shares at a capital gain but whose plummeting share prices once again make them an attractive investment opportunity: these include ThyssenKrupp, Sadia and DSM. Only one company we have never held a stake in previously has been added to our fund, in the chemicals sector. Through these operations we have replaced upside of approximately 100% (Ciba at CHF49.5/sh) for much higher potential returns, in some cases over 300%.

BESTINVER INTERNACIONAL	31-dic-07	31-dic-08	Chg. %
Target price (€ /sh)	41,2	46,4	13%
NAV (€ /sh)	18,9	10,5	-45%
Upside	117%	343%	
P/E (2009 estimated FCF)	6,9 x	3,4 x	

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We understand that for many of our investors the upside we are currently talking about seems spectacular, and hence difficult to believe. We are aware of this and, therefore, over the year we have tried to give examples to show that even at times like the present, when capital markets and bank financing are far from operating normally, there are cases that give credence to our valuations or at least come close to them. Examples are the takeover bids and other corporate transactions that affected us during the year (Corporate Express and Ciba, directly, and Unión Fenosa and Sorigenia, indirectly). Along these lines, we should mention a transaction that was closed in the first few days of January 2009, even though it does not affect our funds. We are talking about the German group RWE's purchase of the publicly-owned Dutch electric company Essen. The valuation assumes multiples that are approximately double those that European electric utilities are currently trading on, and is exactly in line with Bestinver's valuation of electricity assets. It is important to realise that this **discrepancy between current equity valuations and valuations in private transactions** has occurred in a high-visibility sector which is closely followed by the market. And while none of Bestinver's funds has specifically been affected, it does uphold our valuation of the electricity sector to which we are exposed via our investments in Alba and CIR-Cofide.

We expect this upside, which is still growing even though we have lowered the target price for many of our stocks to reflect the decline in global economic growth forecasts, to be reflected shortly in the prices of our share positions. The estimated P/E of the fund is currently 3.4x, implying upside of 343%.

# Our Iberian Portfolio

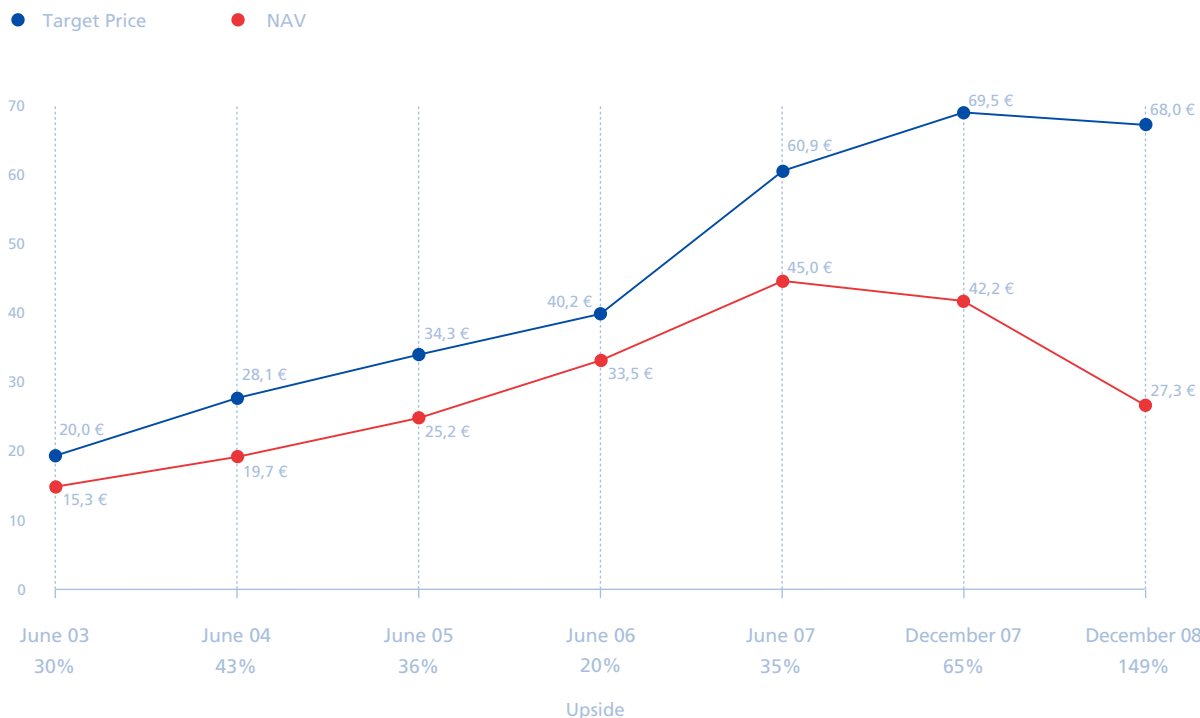


Over the quarter our Iberian portfolio generated a negative yield of 15.7% and has returned a negative performance of 35.2% over the year, compared to -40.6% by its IGBM benchmark.

The annual long-term return is 5.2% and 9.8% higher than index for the last five and ten years, respectively. Over the last three months we have scaled back our valuation of eleven companies, and we have not increased it for any. Once again, this reduction is likely to be temporary rather than permanent in nature and owes largely to the inclement global scenario. We have lowered our valuation permanently for only two companies. These cuts have moderately reduced the value of our portfolio.

## BESTINVER BOLSA

## Gap between target price and NAV.



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In the last quarter of the year, we reduced our exposure to cyclical companies based in Spain even further. For many years we have been following a strategy predicated on investing in export companies and businesses outside Spain, and since 2007, in Portuguese companies. **At year-end 2008 only 24.8% of our Iberian portfolio corresponded to investments in companies with Spain-based markets. Furthermore, most of these investments are in relatively non-cyclical sectors** such as food, beverages and tobacco, insurance, urban services, civil engineering and infrastructure, or which depend on global variables such as energy and metals.

We would like to highlight one interesting feature of this bear market that is related to the biggest investment in our Iberian portfolio, i.e., the holding company Corporación Financiera Alba, and to some of the other investments held on this and our international portfolio. In general, holding companies with investments in listed companies trade at a discount to the market value of their investments net of expenses and liabilities. This discount varies significantly over time.

BESTINVER BOLSA	31-dic-07	31-dic-08	Chg. %
Target price (€ /sh)	69,6	68,0	-2%
NAV (€ /sh)	42,2	27,3	-35%
Upside	65%	149%	
P/E (2009 estimated FCF)	9,1 x	6,0 x	

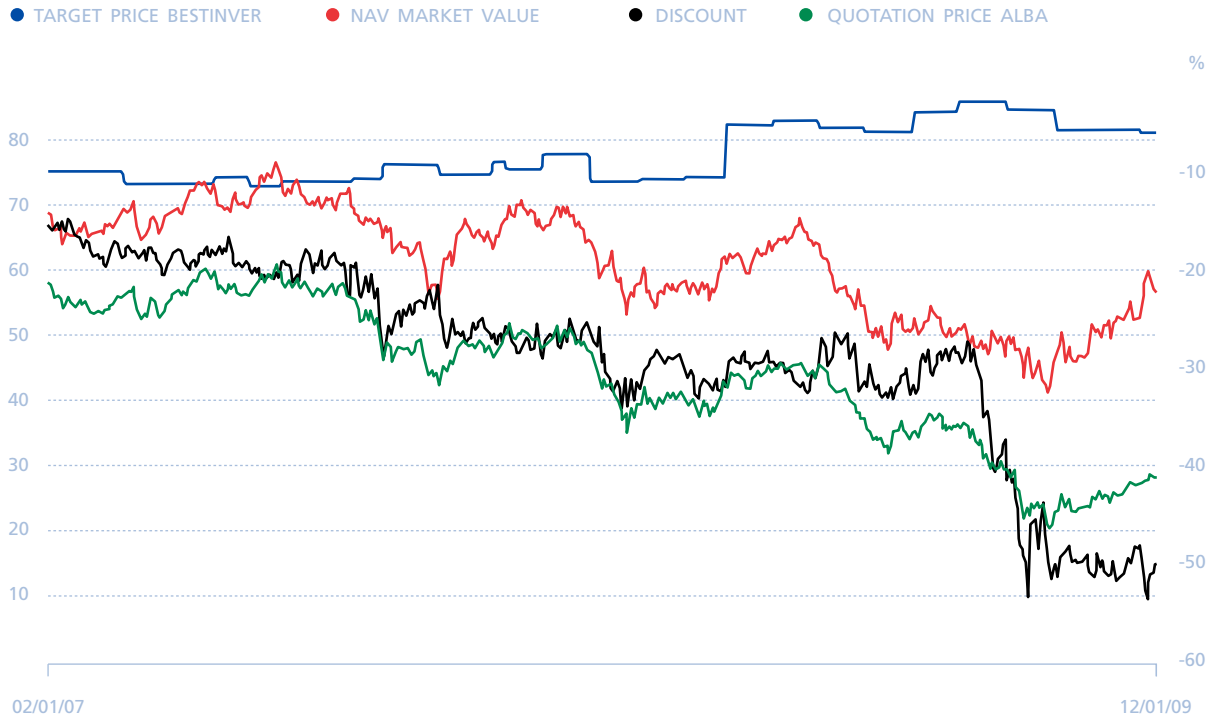
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The discount is applied on the premise that investors always have the, theoretically preferable, alternative of investing directly in the holding company's investees. However, on occasion, this discount becomes excessive and an investment opportunity may arise. Looking specifically at Alba, over the past few months the discount on the market value of its investees, mainly ACS and Acerinox, has increased while at the same time the market value of these investees has plummeted. Therefore, the market is offering investors the paradoxical "two-fold" opportunity of investing indirectly in ACS and Acerinox at a lower discount than ever, precisely when this discount is more unjustified given the sharp fall in their share prices. We also consider that Acerinox and ACS are trading at a discount to their target prices. Furthermore, Acerinox is also a direct investment in our Iberian portfolio. Alba is currently trading at around €27/sh while our target price is €80.

The estimated P/E of the portfolio of our Iberian portfolio is currently 6x, with upside of 149%.

## QUOTATION PRICE ALBA

Performance of the last twenty four months.



**TARGET PRICE BESTINVER:** Price that should be reached by Corporación Financiera Alba in the stock market, following our managers' valuation.

**NAV MARKET VALUE:** Weighted Price in the stock market of the investees in the holding (ACS and Acerinox).

**DISCOUNT:** Gap between market NAV and Alba Quotation Price.

**QUOTATION PRICE:** Price of Alba in the stock market.

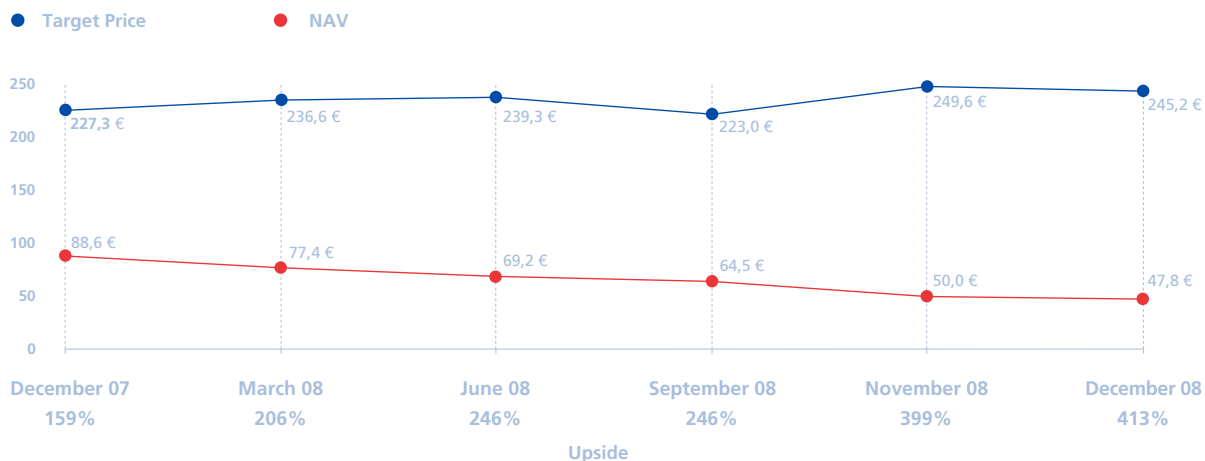


Our hedge portfolio slightly underperformed over the quarter, yielding a negative 25.8% (compared to -21.4% by the MSCI World index). As noted in our previous quarterly newsletters, the Bestinver Hedge Value Fund is concentrated on our strongest investment ideas. Given that our best ideas often stem from falls in the share price of sound companies, it can happen that the very inclusion of such opportunities in the fund drags down its short-term performance. However, **in the long term we expect the opposite to be true, and that our investments in extremely undervalued stocks will offer much higher yields than the equity markets.** The scope and rapidity of the increase in the NAV of this fund in the first few days of January, is, we believe, an example of it large upside.

Our hedge fund is currently trading at an estimated P/E of 2.9x, implying upside of 413%.

## B. HEDGE VALUE FUND

### Gap between target price and NAV.



B. HEDGE VALUE FUND	31-dic-07	31-dic-08	Chg. %
Target price (€ /sh)	227,3	245,2	8%
NAV (€ /sh)	88,6	47,8	-46%
Upside	157%	413%	
P/E (2009 estimated FCF)	5,8 x	2,9 x	

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# Conclusion



Investors in Bestinver funds have to trust in two premises:

**1- In the long term share prices always reflect their value**, which depends on a company's ability to generate sustainable earnings. Equity markets are in a constant, sometimes wild, state of flux and are as **changeable as the psychology that fuels the expectations of the market agents**. Accepting this premise means no more than trusting in the market economy and both are indissoluble.

**2- Bestinver fund managers have proven that they are able to reliably calculate the sustainable earnings level of the companies** they invest in, and therefore, estimate their value. This allows us to take advantage of any deviations in their share prices, as we have been doing over the last 16 years. This belief in the philosophy of value investment gave us very high liquidity in July 1998, helped us evade the dotcom bubble and avoid the turmoil affecting the Spanish banking and real estate sectors over the past few years.

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- All Bestinver returns are expressed in local currency, as net after expenses and commissions.
- Text written by Fernando Bernad Marrase (Bestinver fund manager).
- All of the Bestinver mutual funds are co-managed by the three fund managers: Francisco García Paramés, Álvaro Guzmán de Lázaro, and Fernando Bernad Marrase.
- The current quarterly newsletter as well as the old ones can be found on our website. ([www.bestinver.com](http://www.bestinver.com))
- **Upside:** The fund's scope for revaluation in the opinion of Bestinver fund managers, calculated as the difference between current P/E and target P/E. It is not about the earnings of the fund in a particular period, as, although the fund may be achieving a particular level of return, the goal of the fund managers is to increase this potential, or, at least, to keep it constant.
- **P/E:** Price of free cash-flow at which the fund is trading, based on the P/E estimated by Bestinver's fund managers for each company (includes adjustments such as debt, changes in the cycle, exchange rates, etc.)
- **Price:** The net asset value of the shares in the fund. For the international stock market, the net asset value of the B. Internacional fund is used; whilst for the Iberian stock market, the net asset value of the B. Bolsa fund is used.
- **Target Price:** The net asset value that shares in a fund could reach based on the intrinsic value, in the opinion of Bestinver's fund managers, of all the stocks in the portfolio.

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