Longleaf Partners International Fund gained 0.76% in the second quarter, adding to the Fund’s strong absolute return in the first three months of 2019. The 13.37% year-to-date (YTD) performance was well above our absolute annual goal of inflation plus 10%. The MSCI EAFE Index added 3.68% in the second quarter and gained 14.03% YTD. As the Fund’s manager and largest shareholder group, we are focused on delivering solid absolute and relative returns over three-year periods rather than three months. We believe the last three years, when the Fund rose 13.66% per year and the Index added 9.11%, are more representative of the long-term outperformance that the Fund could deliver.

Longleaf International's European investments helped performance in the second quarter, while declines at companies based in Hong Kong and China offset some of the gains. Like the Fund, the Index generated all its positive return from European holdings, but the much lower weighting (less than 4%) in China and Hong Kong versus

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Average Annual Total Returns (6/30/19): Longleaf Partners International Fund: Since Inception (10/26/98): 7.56%, Ten Year: 6.63%, Five Year: 2.54%, One Year: 5.40%. MSCI EAFE Index: Since 10/26/98: 4.51%, Ten Year: 6.90%, Five Year: 2.25%, One Year: 1.08%.

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, 2019, the total expense ratio for the Longleaf Partners International Fund is 1.18% (gross) and 1.15% (net). The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.15% of average annual net assets.
the Fund (over 25%) negatively impacted relative results. Worries about the outcome of Trump's trade war plus tighter credit in China, political friction and spiking interest rates in Hong Kong weighed on Asian businesses. Ironically, a drawn-out trade war and government oversight could strengthen the moat of Baidu, the Fund's primary performance detractor, as non-Chinese competitors like Alphabet would receive more scrutiny and be less likely to succeed in China's search market. The region's macro challenges have not hurt the premium prices being paid for Hong Kong real estate, which comprises the majority of our appraisals at both Great Eagle and CK Asset. Both continue to sell assets at good prices. Our investment cases for these companies, as well as for Melco, are tied more to the longer-term growth in the standard of living of China's massive population than a near-term political or economic trend.

When stocks are at extreme discounts, shareholder-oriented corporate managements go on offense, which can lead to unanticipated quick payoffs independent of broader stock market moves. We are engaged with our corporate partners to pursue opportunities to build and gain recognition of value. For example, the Fund's best performer in 2018, Belmond, which we finished selling in the quarter, rose instantly when management announced a strategic review that eventually led to the sale of the company at a large premium to the stock's price. Much management-led activity has occurred this year. Baidu authorized its third ever stock repurchase to take advantage of the deep share price discount. EXOR tried to merge its FCA holding with Renault-an effort that may not be over. LafargeHolcim sold assets in several emerging markets at attractive valuations. The Fund's newer holding, LANXESS continued intelligent capital allocation moves by completing an aggressive share buyback and pursuing the sale of a non-core business segment. Lazard issued 10-year debt to aggressively buy its severely discounted stock at a meaningful double-digit pace. CEO Lawrence Ho announced the sale of Melco International's Cyprus properties to operating company Melco Resorts to provide more capital to the parent, while opportunistically purchasing almost 20% of Australian casino company Crown. MinebeaMitsumi completed its previously announced tender offer of U-Shin at a discounted price. OCI announced the separation of its Middle Eastern assets into a joint venture.
Our confidence in the Fund’s future results has much to do with our belief in the ability of our corporate leaders to deliver self-help that grows value per share and ultimately generates rewarding payoffs.

**Contributors/Detractors**
(Q2 Investment return; Q2 Fund contribution)

C&C Group, (27%, 1.02%), the manufacturer and distributor of branded beer, cider, wine, soft drinks and bottled water, performed well in the quarter for multiple reasons. Competition worries in Ireland eased as Bulmers’s market share stabilized. In Scotland, Tennent’s grew revenue 7% over the last year and remained well positioned. The AB InBev relationship successfully pushed Magners in the off-trade in England and Wales. Last year’s acquisition and subsequent integration of Matthew Clark and Bibendum has exceeded management’s expectations and provided further distribution channels for C&C’s brands. At the company’s Capital Markets Day, CEO Stephen Glancey highlighted C&C’s ownership culture, emphasizing the importance of all employees having skin in the game.

EXOR (9%, 0.75%), the European holding company of the Agnelli family, made gains as Chairman and CEO John Elkann continued to apply an admirable approach to capital allocation and portfolio management in the quarter. The company extensively explored consolidation in the auto industry through Fiat Chrysler, in this instance through a proposed combination with Renault. We believe there is substantial strategic logic and potential shareholder value in such a move. The French state and Nissan, Renault’s Japanese partner, were not immediately in favor of a combination, though the rest of Renault’s board voted to proceed. There still may be potential for a constructive deal, but if there is no deal with Renault, there are other opportunities to explore. We are confident that management and the family owner-partners will evaluate every value-creating angle.

Baidu (-28%, -1.43%), the dominant online search business in China, was the primary detractor in the quarter. Baidu reported 2019 first quarter results in line with initial guidance, and Baidu Core revenue grew 16% year-over-year (YOY). However, second quarter growth guidance fell below expectations, mainly due to economic weakness
impacting advertisers’ budgets and increased online advertising inventory creating price pressure across the industry. Baidu’s migration of all medical ad landing pages from third party sites onto its own servers to improve advertising quality and Baidu’s control over content also negatively impacted short-term ad sales. Baidu’s search dominance remained intact as traffic grew - June daily active users increased 27% YOY on Baidu’s App and Smart Mini Program monthly average users rose 49% from the previous quarter. Additionally, the company’s AI initiatives in areas such as voice activated smart speakers and autonomous driving represent substantial future earnings upside. The deeper stock price discount provided Baidu’s management the opportunity to launch an additional US$1 billion share buyback program beyond its existing US$500 million one. The company is paying a low-single-digit free cash flow (FCF) multiple for a strong cash-generative and hard-to-replace asset.

Great Eagle (-15%, -0.72%), a Hong Kong real estate company that invests in and manages high quality office, retail, residential and hotel properties around the world, declined amid the China turmoil and spiking Hong Kong interest rates. Although most Hong Kong real estate companies are discounted, Great Eagle is more compelling to us because Chairman Lo Ka Shui, who owns over 26% personally and is a beneficiary of a family trust that owns another 32%, has focused successfully on building long-term shareholder value. He has been extremely disciplined on the prices he will pay for properties and methodically has been building the Langham brand in the luxury hotel market. The stock has grown at a double-digit rate since we first purchased it in 2015, even with the second quarter dip. In the second half of 2019, the company will be pre-selling units in its ONTOLO residential development at prices that should be significantly above Great Eagle’s cost in the project. Lo recognizes the undervaluation in the current price and recently bought more shares personally.

**Portfolio Activity**

During the quarter, we added to several of the Fund’s more recent purchases as our conviction level grew and prices cooperated. We established one new position, Domino’s Pizza Group (DPG) in the UK. We have followed the company for years and long admired the underlying business quality and cash generation capabilities, along with the potential for continued growth. DPG is the master franchisee holder in perpetuity of the right to oversee Domino’s operations in the U.K., Ireland and several
European markets. DPG pays the U.S. company, Domino’s Pizza, Inc., a royalty fee for use of the name and intellectual property. DPG became attractively discounted in part because of the Brexit overhang on U.K. consumer companies, but primarily due to tension between key franchisee groups and the current executive team. We believe there are readily available solutions to that disagreement and plenty of opportunities to grow and realize value. We are actively engaged with the company on the way forward.

We exited three investments – two that successfully reached appraisal and one where the case deteriorated. We sold luxury hotel company Belmond. French luxury-goods company LVMH announced its acquisition of Belmond in December, but we delayed selling for tax reasons until the Fund’s gains went long-term. We salute the management team with whom we were engaged, for recognizing the company’s deep undervaluation and announcing a strategic review that served as the catalyst for getting a fair bid for the company and a 110% return for the Fund.

We sold Yum China (YUMC), the operator of KFC and Pizza Hut restaurants in China, for the second time in the three years since its separation from YUM! Brands in the U.S. Under the leadership of CEO Joey Wat and CFO Jacky Lo, KFC grew same store sales, as did Pizza Hut for the first time since 2018. The company also opened new stores faster than anticipated. Management returned capital to shareholders through buybacks and dividends. The gap between the share price and our appraisal quickly closed, and the investment gained over 40% during our holding period of seven months.

Although the sum-of-the-parts of thyssenkrupp was deeply discounted, we sold the position because the path to unlocking the different segments’ values became narrower and more uncertain. The proposed Steel JV with Tata was blocked by regulators, and the macro environment was pressuring FCF such that value was not growing. We moved on to more compelling opportunities but recognized an over 40% loss during our holding period, most of which was reflected in performance prior to the second quarter.

**Outlook**

Most of the price pressure in the Fund came at the hands of macro concerns over global economic growth, trade wars and geopolitical uncertainties. Corporate
fundamentals performed much better than the market, enabling our research team to build a robust on-deck list of prospective opportunities, including the new investment in Domino’s. The portfolio is close to fully invested with 6% cash and trades at a mid-60s% price to value ratio (P/V).

Not only is the Fund attractively priced, but most of our investment cases are so far playing out as we anticipated. At many holdings, we are engaged with CEOs and boards who, in our view, are taking actions to drive value growth and create catalysts for recognition. The patterns for how stocks reach intrinsic worth are unpredictable, but appreciation can happen quickly. One of Southeastern’s competitive advantages is taking a multi-year perspective to stock ownership, as prices ultimately should migrate to growing values. Given the discount in the portfolio, positive business fundamentals and corporate partners pursuing catalysts, we believe significant payoffs could occur in 2019 and beyond.

*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 International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

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

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.

As of June 30, 2019, the top ten holdings for the Longleaf Partners International Fund: EXOR, 8.9%; CK Hutchison, 6.4%; LafargeHolcim, 6.1%; MinebeaMitsumi, 6.0%; Melco, 5.8%; LANXESS, 5.1%; Bolloré, 4.6%; CK Asset, 4.6%; C&C Group, 4.4%; Baidu, 4.4%. 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.
LLP000914
Expires 10/31/2019
Longleaf Partners International Fund gained 12.52%, surpassing our annual goal of inflation plus 10% in the first quarter and exceeding the MSCI EAFE Index's 9.98% return. The last three month's results were similar to the compounding success of the last three years, where the Fund delivered 12.32% annually versus 7.27% for the Index.

Almost all the Fund's holdings made gains, and there were no notable decliners in the portfolio. The businesses that were primary drivers of performance had little in common beyond delivering solid results. As is normally the case in our concentrated, high active share portfolio, each company had its own idiosyncratic outcome - from overshooting cost reductions to returning capital to owners to rumored asset sales. In aggregate, European based investments were larger contributors than those in Asia, despite currency headwinds for the dollar versus European currencies.

The market's rebound, following a double-digit fourth quarter decline in 2018, provided a tailwind. Even as the issues of global economic slowdown, tariff and trade


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The total expense ratio for the Longleaf Partners International Fund is 1.19% (gross) and 1.15% (net). The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.15% of average annual net assets.
disruptions, and geopolitical unrest remained unresolved, investor concern appeared to dissipate. We have little insight into how macro questions about China’s growth, Brexit’s eventual outcome, inverted yield curves and trillions in negative yielding debt will be answered, but we are confident these uncertainties will continue to provide opportunities to disciplined, long-term business owners like ourselves. Indeed, we are finding plenty to do in Asia, the U.K. and Europe.

Even with the Fund’s strong returns, most holdings sell for under 80% of our appraisal, and the entire portfolio remains in the high-60s%. During the quarter, we bought one new investment and added to several positions, including Lanxess, which we bought in 4Q18 and is a partially recycled Southeastern holding because it owns Chemtura, formerly a Longleaf Small-Cap investment. With cash below 5%, our biggest challenge is determining which new qualifiers present the best risk-adjusted return and whether those warrant replacing an existing investment. The breadth of opportunity leaves us optimistic about prospective long-term returns.

**Contributors/Detractors**

(Q1 Investment return; Q1 Fund contribution)

EXOR (20%, 1.57%), one of Europe’s leading investment holding companies and the Fund’s largest position, was a contributor. The main component pieces of our EXOR appraisal are FCA, PartnerRe, CNHI and Ferrari. In late 2018, FCA declared a special dividend after selling Magnetti Marelli and announced a new recurring dividend, doubling EXOR’s annual corporate free cash flow (FCF). FCA’s balance sheet started 2019 with €1.9 billion of net cash after the company generated €4.3 billion of Industrial FCF allowing the board to make these dividend commitments. EXOR CEO John Elkann is an owner-operator who has grown corporate value and seen the stock compound at nearly 20% per year since we invested in 2012. Notably, value has compounded just as quickly such that EXOR remains heavily discounted on our conservative appraisal. We have an overweight position in this collection of high-quality businesses and assets that have ample transformation value and are selling at a deep discount to the sum-of-the-parts and at lower multiples than peers.
OCI (35%, 1.32%), a leading producer of nitrogen fertilizers and methanol, was a strong contributor. OCI grew FCF 210% year-over-year and EBITDA (earnings before interest, taxes, depreciation, and amortization) over 100%. Strong cash generation should continue to help the company rapidly deleverage - net debt declined $327 million, and Net Debt/Operating Cash Flow fell from 7x to 4.4x over the last year. Volumes stepped up 16%, with U.S. assets increasing production up to 115% of nameplate, as OCI grew into its new capacities. Multiple strategic options are available to the company, which sells well below the replacement cost of its assets, and rumors of Saudi interest in the methanol plants helped the stock. CEO Nassef Sawiris is an owner operator who remains focused on value creation and recognition.

LafargeHolcim (20%, 1.32%), the world's largest global cement, aggregates, and ready-mix concrete producer, was another top contributor to the Fund's return. After eighteen months as CEO, Jan Jenisch is delivering both operating efficiencies and value-accruing asset sales. Recent results showed efficiency gains and pricing that offset cost inflation. Cost savings were ahead of target, with Aggregates and Ready-Mix EBITDA margins improving considerably. The company also eliminated CHF400 million in central corporate expenditures. These cost initiatives combined with more favorable markets should meaningfully grow LafargeHolcim's earnings power. The company has pushed through pricing in its North American business. Latin America and Middle East & Africa are showing signs of stabilizing in 2019. Europe should experience modest growth this year. The company closed the sale of its Indonesian assets at an attractive price, and management plans to accelerate divestments in other regions over the next two years, providing meaningful cash proceeds to reinvest.

Yum China (34%, 1.17%), the operator of KFC and Pizza Hut restaurants in China, was a contributor to performance during the quarter. Yum China (YUMC) reported good fourth quarter results with KFC recording same store sales growth of +3% on top of high comparables last year. Pizza Hut reported positive store traffic growth. These positive trends continued into the first two months of 2019, and YUMC's disciplined expense control mitigated margin pressure from promotions and cost inflation. The company remains committed to opening new stores, with the plan of adding 600-650 in 2019 and a total stores target of 10,000 by 2021. In addition to delivering solid operating results, CEO Joey Wat and CFO Jacky Lo returned $191 million to
shareholders in the fourth quarter, primarily via share repurchases, and are committed to returning $1.5 billion over three years.

Melco International (16%, 1.12%), the Asian casino and resort holding company, rose after its operating business, Melco Resorts, reported strong Q4 results that beat forecasts. EBITDA gained 25% year-over-year, up 44% quarter-over-quarter. The new Morpheus Hotel within City of Dreams has ramped up well. Melco plans to build new non-gaming attractions at Studio City in 2019 to drive mass traffic and gross gaming revenue. The company has secured 98% ownership in the tender offer for its Philippines business. With more infrastructure built in the region, Macau’s overall visitation, particularly of Melco’s more important non-VIP business, should grow well longer term.

CK Asset (22%, 1.04%), the Hong Kong and China real estate company, reported solid results for 2018, with dividends increasing 12% year-over-year and book value per share growing 11%. In 2018, CK Asset sold the Center at below a 2.5% cap rate. CK Asset’s hotel portfolio increased profits 22% with improvements in room rates and occupancy. Two hotels will open in 2019 and add around 15,000 rooms and serviced suites. Given relatively high land prices in Hong Kong, we expect Managing Director Victor Li to continue to deploy cash flow into global projects that offer attractive returns.

**Portfolio Activity**

We trimmed four of the Fund’s stronger recent performers as their price to values (P/Vs) rose and reallocated to other investment opportunities. We bought one new, undisclosed position and added to several of the most discounted investments, including Lanxess, which we started buying in the fourth quarter. Lanxess is a specialty chemical company led by Matthias Zachert, viewed as a highly capable European CEO. Historically, the business was more cyclical and reliant on commodity products, led by a heavy emphasis on rubber production for tires. Since returning to Lanxess in 2014, Zachert has migrated the focus to specialty chemicals with stronger, less volatile growth prospects. The sale of the rubber business at a very attractive price, the 2017 acquisition of Chemtura, a focus on costs and efficiencies and a new share buyback program to take advantage of the low share price have highlighted Zachert’s ability to drive long-term business value.
Team Update

We welcomed Taieun Moon as a junior analyst in our Singapore office in the quarter. Taieun interned for Southeastern last summer and joins us full time following his graduation from The University of Hong Kong. We also concluded our search for a junior analyst in London. Alicia Cardale will join Southeastern in May. She has interned at several investment firms and most recently worked at a U.K. real estate company. Alicia has a Master’s degree in Real Estate from the University of Reading. We look forward to the broad depth that Taieun and Alicia will add to our research team.

In March, we shut down the concentrated Europe Fund (“SCV”). Although SCV had a strong performance record over its four years, in the last fifteen months the Fund’s cash balance grew to more than three-quarters of NAV. Over the same period, the International Fund’s cash declined from 22% to less than 3%, as we were finding opportunities, including several European qualifiers. SCV’s idea generation was no longer benefitting Southeastern’s broader client base, and our investment partners could own the most compelling European engagement opportunities via the more flexible and less costly International and Global Funds. Consequently, we returned the capital to our partners, much of which was internal to Southeastern and will be re-deployed into Longleaf International. Because Scott Cobb was solely focused on managing SCV, he will depart from Southeastern upon its closing. We thank Scott for his years of service to Southeastern and our clients.

Outlook

When prices become as discounted as they were in December, it is not surprising to see a strong rally. We believe, however, that the portfolio offers substantially more upside. The P/V is in the high-60s%, and cash is less than 5%. Additionally, we are finding a number of new opportunities that meet our criteria both in Asia and Europe. We are confident that we have a foundation of strong companies and solid partners that may deliver rewarding results over the next three years.

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Active share measures how much an equity portfolio’s holdings differ from those of the benchmark index.

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

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.

Leverage refers to the use of debt. De-leverage refers to a decrease in debt.

Aggregates are materials such as sand or gravel that are ingredients in concrete.
Book Value is the value of an asset as carried on a company’s balance sheet.

Cap rate (capitalization rate) is the rate of return on a real estate investment property based on expected income.

As of March 31, 2019, the top ten holdings for the Longleaf Partners International Fund: EXOR, 8.2%; Melco, 7.2%; LafargeHolcim, 6.8%; CK Hutchison, 6.7%; MinebeaMitsumi, 5.6%; CK Asset Holdings, 5.1%; Millicom, 4.9%; OCI, 4.8%; Bollore, 4.7%; Great Eagle, 4.7%. 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.

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Longleaf Partners International Fund Commentary

4Q18

Longleaf Partners International Fund declined -9.90% in the fourth quarter, pushing the 2018 return to -7.08%. The Fund significantly outperformed the MSCI EAFE Index for both periods. The Index fell -12.54% in the quarter and -13.79% for the year. Pressure on stocks built with headlines of trade wars, higher U.S. interest rates, geopolitical unrest, economic slowdowns in multiple countries, including China, and falling oil prices.

Several factors contributed to the Fund's outperformance over the Index. The primary driver was strong individual stock returns at various successful companies, including four that we sold after a relatively short holding period to fund more discounted qualifiers. The Fund also held less exposure to Financials, the worst performing and most detracting sector in the Index. The International Fund owned EXOR and Fairfax, a combination of re-insurance and industrial businesses that held up much better than the more heavily levered institutions in the sector. Additionally, the 20% cash in the Fund at the outset of 2018 helped the relative return, while also providing dry powder for new opportunities over the course of the year.

Average Annual Total Returns (12/31/18): Longleaf International Fund: Since Inception (10/26/98): 7.09%, Ten Year: 5.83%, Five Year: 0.33%, One Year: -7.08%. MSCI EAFE Index: Since 10/26/98: 3.95%, Ten Year: 6.32%, Five Year: 0.53%, One Year: -13.79%.

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The total expense ratio for the Longleaf Partners International Fund is 1.19% (gross) and 1.15% (net). The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.15% of average annual net assets.
Although the International Fund outperformed the Index and most of its peers, the Fund declined during the year. The strong U.S. dollar negatively impacted both the Index and the Fund’s results by approximately 3%. Businesses that had meaningful economic exposure in emerging markets (EMs), including China, collectively impacted results. Emerging markets declined as the Federal Reserve began increasing interest rates and later as fear of a U.S.-China trade war developed. The EM sell-off, however, also provided opportunities to add to EM-exposed telco Millicom and to Macau gaming company Melco. In addition, we established new positions in Bolloré, which is Africa exposed, Bcele of Mexico, Bharti Infratel of India and three undisclosed holdings in the fourth quarter, including two with sizable EM customer bases.

In our view, returns for the year did not reflect the progress within the portfolio. We not only invested the cash but also had much higher turnover than normal as the opportunity set expanded throughout the year. We sold one company, Yum China, early in 2018, and seven others in the second half. We deployed the proceeds into over half a dozen material new investments, while opportunistically adding to existing holdings. In addition to EM-related qualifiers, German industrials became more appealing, as political and economic uncertainty made Germany among the worst performing European countries within EAFE. In aggregate, portfolio repositioning, value growth and stock price declines moved the price-to-value (P/V) ratio near 60%, a level that has historically preceded strong returns*.

Just as performance did not reflect portfolio enhancements, many stock prices did not indicate the positive progress that our companies and management partners made throughout the year. Several businesses sold assets for attractive prices, including Fairfax, CK Asset, LafargeHolcim, CK Hutchison, EXOR and Baidu. Belmond agreed to be bought by LVMH. Importantly, the primary business segments at most of our core holdings grew, for instance North American Cement at LafargeHolcim, Partner Re at EXOR, Retail at CK Hutchison, North American Fertilizer at OCI, Core Search at Baidu, Bearings at MinebeaMitsumi and Mass Gaming at Melco. Numerous companies in the Fund repurchased shares, thereby increasing the remaining value per share.

Choppy markets and the economic uncertainty that feeds them could last for a while. While many CEOs we talk to are optimistic about revenue growth, they are cautious about rising labor and materials costs on a local level and increases in trade barriers and geopolitical friction potentially impacting revenues and margins. To manage investment risk, we incorporate conservative-to-skeptical assumptions about the
future, invest in a limited number of companies, have a broad and deep research network and engage with managements.

Even though the Fund outperformed the Index, we are neither pleased nor complacent about 2018 absolute returns. As your largest co-investors in the Fund, we believe it is a compelling time to add to Longleaf International. We believe the EAFE is overdue for a relative tailwind after being almost tripled by the U.S. market over the last ten years\(^1\). The Fund’s attractive P/V, and the underlying strength of the businesses we own lead us to believe that the Fund may generate strong absolute and relative results going forward. Most importantly, we have partnered with management teams who, in our view, can control their own destiny in terms of value realization, and we are working with boards and leaders at certain holdings to accelerate this realization.

**Contributors/Detractors**
(2018 Investment return; 2018 Fund contribution; Q4 Investment return; Q4 Fund contribution)

Belmond (105%, 4.49%, 37%, 2.22%), a collection of iconic luxury hotels located mostly in Europe, was the largest contributor in the fourth quarter and for the year. Owned hotels are over 85% of the asset value, with management fees and other leisure businesses the remainder. In August, the company announced a strategic review and ran a competitive sales process. In December, LVMH, the Paris-based luxury-goods company, whose brands include Fendi, Louis Vuitton and Dom Pérignon, agreed to pay $25 per share in cash, valuing Belmond’s equity at around $2.6 billion. This share price premium of more than 80% since the August announcement reflected a fair value for those assets. The sale is expected to close by June of 2019.

Hikma Pharmaceuticals (54%, 2.04%, -, -), a multinational injectables and generic pharmaceuticals company based in the U.K., was the Fund’s other primary contributor in 2018. We bought Hikma in October 2017, knowing we had an owner in Chairman and CEO Said Darwazah and two quality segments in the flagship Injectables segment

\(^1\) 10-Year cumulative return for S&P 500 was 243% and for MSCI EAFE was 85%.
and the Branded MENA business that were being temporarily overshadowed by a more competitive environment in the smaller U.S. oral generic drug segment.
Darwazah proved himself an excellent partner when he brought in well-respected industry veteran Siggi Olafsson to take over as CEO. In a short period, the company made considerable progress in its Injectables operations, the Generics environment improved and the stock exceeded our appraisal leading to a complete exit of the position by August.

LafargeHolcim (-25%, -1.77%, -17%, -1.11%), the largest global cement, aggregates and ready-mix concrete producer, was the biggest 2018 detractor in the Fund after a notable decline in the fourth quarter. Weaker cement demand in Latin America, the Middle East and Africa, as well as higher energy and transportation costs globally impacted profits. With two thirds of revenues tied to emerging markets, broader EM concerns heavily contributed to the stock price weakness. CEO Jan Jenisch believes efficiency gains and pricing will offset cost inflation. The cost savings program is ahead of target, and Aggregates and Ready-Mix margins are improving. The company's North American business, which represents over one quarter of our appraisal, grew profits during the year. The company announced the sale of its Indonesian assets at an attractive price, and management plans to accelerate divestments over the next two years, providing meaningful cash proceeds to reinvest.

thyssenkrupp (-36%, -1.58%, -32%, -1.62%), the German steel conglomerate, declined in the fourth quarter, making it among the Fund's 2018 detractors following our second quarter purchase of the stock. In July, the CEO and Chairman each resigned under pressure from activist investors. In September, the company named Guido Kerkhoff, who had been CFO and interim CEO, as permanent CEO and announced the decision to split thyssenkrupp into an Industrials business and a Materials business. We identified the strategic potential early in the year but underestimated the time and expense required to effect the split. If approved by shareholders in March of 2020, the split can help each division more properly reflect our appraisal of its parts. Industrials will consist of three units: Elevators (the largest part of our appraisal), Automotive Supplies and Core Plant Construction. Materials will contain Materials Services, Slewing Bearings, Forging, Marine and a 50 percent interest in the joint venture of thyssenkrupp's and Tata's European steel businesses. While being early has led to a
painful experience in the short term, we are confident in our assessment of the eventual asset value once the transformation completes in approximately 18 months.

CK Hutchison (-21%, -1.53%, -17%, -1.25%), a Hong Kong based conglomerate of telecommunications, health & beauty, infrastructure, global ports and energy, fell during the final quarter and the year. While a trade war between China and the U.S. will pressure less than 5% of its Ports business, concerns of this trade tension generated broad negative sentiment around Asian stocks. In Italy, the company’s Telecommunications business struggled as increased competition from a new entrant pressured prices. In the second half of the year, declining oil prices impacted Husky Energy, the Canadian energy associate of CK Hutchison. These short-term headwinds negatively impacted sentiment, but the company’s cash flow, as well as management’s capital allocation decisions, helped our appraisal grow in the mid-single digits for the year. Chairman Victor Li sold CK Hutchison’s interests in several infrastructure projects at 12X EBITDA (earnings before interest, taxes, depreciation, and amortization) and redeployed the proceeds to acquire the Italian telecom joint venture at 5x EBITDA. The company also repurchased its discounted shares for the first time in almost two years.

Baidu (-32%, -1.53%, -31%, -1.52%), the dominant online search business in China, declined in the fourth quarter and hurt results for the year. Lower growth guidance for the fourth quarter reflected macro uncertainties in China, and U.S.-China trade discussions distorted U.S. listed share prices of Chinese companies such as Baidu. The recent stock decline did not reflect the future earnings power of the company or the progress made during 2018, when our appraisal grew over 20%. During the year, Baidu completed non-core divestments of Financial Services and Global DU and IPO’d video business iQiyi. Baidu Core grew with news feed and AI-related business contributing over 20% of revenue. In July, Baidu launched the first fully autonomous Level 4 minibus with King Long Motor. CEO Robin Li announced a US$1 billion share buyback program to take advantage of the discounted share price.

MinebeaMitsumi (-35%, -1.47%, -21%, -0.98%), the Japanese manufacturer of high precision equipment and components, negatively impacted performance for the year. Most of the stock’s decline was related to worries that Apple iPhone screens will entirely shift from LED to OLED technology and that iPhone sales will slow. MinebeaMitsumi supplies Apple with LED backlight and camera actuators, but this
division represents less than 5% of the company's intrinsic value. The core miniature ball bearings business with over 60% global market share increased pricing in October, while units continued to grow at the historic mid-single digits rate. In November, MinebeaMitsumi offered to acquire U-Shin, a Japanese auto parts manufacturer specializing in locks, at below 4X EBITDA. This value-accrative acquisition will double the size of the auto-related business and improve automotive distribution, and further demonstrates management's capabilities in acquiring and fixing undervalued Japanese opportunities. CEO Yoshihisa Kainuma personally bought 1.5% of outstanding stock, and the company is repurchasing discounted shares.

Melco (-30%, -1.41%, 2%, 0.29%), the Macau-based gaming company, declined for the year over concerns about decelerating growth with ongoing U.S.-China trade war issues, a slower Chinese economy and weakening Renminbi. The decline in China's A-share markets and slow-down in neighboring province Guangdong (export hub of China) are likely to impact gross gaming revenues, but we believe most of the impact will be on the lower-margin VIP business. Increased profits from growing, higher-margin Mass visitors should compensate for any VIP decline over time, as infrastructure improvements (HK-Zhuhai-Macau bridge, high speed rail, etc.) and additional hotel room supply make Macau more accessible. Despite the stock's decline, during 2018, our appraisal grew as reported earnings doubled. CEO Lawrence Ho created value for shareholders via buying out minorities at Melco Resorts Philippines at attractive multiples, IPOing Studio City to create opportunity for an ownership increase in 2019 and repurchasing discounted shares.

OCI (-19%, -0.86%, -36%, -2.41%), a global producer of nitrogen fertilizers and natural gas-based chemicals, was the primary detractor in the fourth quarter, primarily due to the decline in the methanol spot price, which is linked to oil. To the positive, non-methanol-related assets, which represent three quarters of the value, did well. African facilities resolved gas supply issues and achieved 95%+ utilization rates. The company sells for less than the replacement cost of its assets and our conservative estimate of the discounted cash flow value. CEO Nassef Sawiris is an owner-operator focused on optimising the capital structure and generating significant free cash flow.
Portfolio Activity
In a particularly active year, we exited nine holdings, including Ferrovial in the fourth quarter. The Fund had previously held this Spanish transport infrastructure company that owns toll roads in Europe and North America, airports in Europe, including London Heathrow, and infrastructure construction and servicing businesses. The company’s Spanish and British businesses faced increasing headwinds, including Catalonia and Brexit uncertainty. Given less certain prospective value growth and the rising interest rate environment, we sold the position. During our two-year investment, the Fund earned over 15% as traffic and pricing increased on the company’s toll roads and at Heathrow, even as European headwinds mounted.

As markets declined in 2018, we invested in thirteen new qualifiers, some of which quickly did well and we sold for even more compelling opportunities. The three new positions purchased in the fourth quarter included one-and-a-half “recycled” names that we previously owned. The half includes assets from a company that was once held in Longleaf Partners Small-Cap Fund and was acquired by the foreign business we recently bought. It serves as a good example of how operating as a single research team, without silos based on geography or strategy, leverages our knowledge and opportunity across Southeastern. The three new positions, which are in disparate industries, remain undisclosed. Two are European based but with global markets, and one is Asian based.

Outlook
The Fund has more prospective investments than cash. We view EM and EM-related opportunities as the most discounted, with Asia Pacific the most undervalued region. More recently, Europe moved to the cheap bucket. The U.K., Germany and Italy face concerns over Brexit, China trade and Italy’s budget fights with the European Union. The equal-weighted P/V on the broad international universe we track moved from overvalued at the start of the year to high-80s% at the end of December. The Fund’s P/V moved to the low-60s%, with the prospect of dropping into the 50s% as one company is approaching full value and likely to be replaced with one of several very undervalued on-deck qualifiers.

In 2018 the Fund reached its twentieth anniversary. Southeastern has come a long way since moving one American from Memphis to Tokyo in 1998 and a second Memphis
team member to London three years later. Since inception, the Fund has produced 300 basis points per year of excess return versus the EAFE Index. Returns in concentrated value investing can be lumpy, as the Fund’s track record demonstrates, with strong outperformance interspersed between more difficult periods. We view the firm’s unique global structure and decision-making process today as a long-term research advantage that can continue to deliver what we believe will be superior results for our clients over the coming decades.

- We have four researchers in Singapore and a junior analyst starting in 2019. There are four researchers in London, with a search currently underway to add a junior analyst. We continue to broaden and deepen our global research capabilities. A critical mass in each office makes our research more comprehensive, allowing people to brainstorm and get instant feedback in person and involving multiple people in management engagement or other research meetings.

- Southeastern seeded Asian and European regional strategies four years ago to create more ways for the international research team members to own the opportunities within their territories. Idea generation has increased, feeding more prospective investments to the International Fund, and more people on the team have developed a broader portfolio management perspective.

- Seven of the overseas analysts are from countries other than the U.S. (the eighth has dual U.K. citizenship). We believe locals committed to staying in their regions bring diverse views with more understanding of cultural nuances and opportunities and provide a unique network of research contacts that expands over time.

- The Fund has held meaningful stakes in over 170 companies during our successful 20-year history. Southeastern’s cumulative research and results have enhanced our reputation and increased our relationships globally, increasing access to corporate managements and boards for productive engagement and research insights.
We operate as a single, integrated research team with the eight offshore analysts and seven Memphis-based analysts reviewing and challenging one another’s work. We bring to bear all the team’s collective investing experience, industry knowledge and network of helpful contacts across three continents before committing our clients’ and our own capital.

Southeastern has developed from a U.S. firm with overseas offices into a global investment company, with nine of our fifteen analysts, including Josh Shores, who lives in Memphis after spending most of the last decade in our London office, focused primarily on investments outside of the U.S. As Co-PM of the International Fund and a member of Southeastern’s Executive Committee, Josh helps insure a global perspective, as our Memphis-based firm provides the resources needed to deliver successful results around the world.

In our view, the Fund’s strong returns over the last three years reflect the progress that we have made in fully developing our global team. We believe that the next twenty years can be even more successful, not only because of the set of businesses and corporate partners in the portfolio today, but because we are armed with our deepest-ever international research following a decade when both our style of investing and owning companies outside of the U.S. have been dramatically out of favor. This is a time when we think investors adding to Longleaf International may be particularly rewarded.

See following page for important disclosures.
Quarter-ends since 1998 were identified where the International Fund's "price-to-value ratio" (P/V) was less than 60%. From each quarter end identified, the 1, 3, and 5 year cumulative returns for the Fund and the MSCI EAFE were calculated. Those returns were then averaged and the 3 and 5 year returns were annualized. The results were: 17.00% for 1 year, 10.49% for 3 year, and 11.28% for 5 year for the International Fund and 6.95%, 6.25% and 9.08% for the EAFE Current circumstances may not be comparable.

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 International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

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

IPO is an initial public offer.

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.
As of December 31, 2018, the top ten holdings for the Longleaf Partners International Fund: EXOR, 7.8%; Melco, 7.2%; CK Hutchison, 6.9%; LafargeHolcim, 6.2%; MinebeaMitsumi, 6.1%; Millicom, 5.8%; Vestas, 5.7%; Belmond, 4.9%; Bollore, 4.8%; CK Asset Holdings, 4.8%. 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.
LLP000850
Expires 4/30/2019
Longleaf Partners International Fund gained 3.19% in the third quarter, on pace to exceed our absolute goal of inflation plus 10%, as well as the MSCI EAFE Index’s 1.36% return. The Fund’s last 3 months comprised all the Fund’s 3.13% year-to-date (YTD) rise, which exceeded the Index decline of -1.43%. Over the last 9 months, the Fund maintained positive results, in spite of the headwinds of a rising U.S. dollar, trade war fears, Emerging Market weakness and uncertainty over Brexit’s unwinding next year. European and Asian markets were broadly negative, declining -2.5 to -2.9%, and Emerging Markets fell more than -7.5%.

With around twenty holdings, performance usually comes from just a few stocks. Company-specific events and management-led outcomes drive the Fund’s investment results, which generally have little to do with what drives the broader index. Stock prices often move up in a short number of days as sentiment quickly changes. For example, Belmond was the Fund’s largest contributor for the quarter and YTD, as management announced the company would do a strategic review to consider selling some or all of its luxury hotels, and the stock gained 43% in just 4 days. Hikma rose sharply following several positive earnings reports. OCI had several meaningful step-ups in its price over the last year, as its new plants ramped up production and nitrogen

Average Annual Total Returns (9/30/18): Since Inception (10/26/98): 7.74%, Ten Year: 4.80%, Five Year: 3.82%, One Year: 2.81%.

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.

The total expense ratio for the Longleaf Partners International Fund is 1.19% (gross) and 1.15% (net). The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.15% of average annual net assets.
fertilizer prices rose. Within just a few months of purchase, Televisa and Vocus each gained approximately 30%.

Living patiently with idiosyncratic payoff patterns can be difficult but is necessary. More often investors make decisions based on stock price performance without regard to the direction of a company’s underlying business value. Chasing performance puts capital at risk, with the danger usually realized too late. We usually do not know when payoffs among our portfolio companies will occur, but most values are appreciating, and many current holdings offer significant upside potential with our management partners pursuing restructuring, substantial repurchases at deep discounts and sales of assets or entire businesses.

The juxtaposition of rapid, large payoffs in some of the Fund’s companies against broader market declines resulted in quite a bit of portfolio activity in the quarter. Trims and four exits funded three new companies, plus additions to five other positions. We have a robust on-deck list of qualifiers, including stocks declining in the broad Asian correction and companies trading at a discount because of geopolitical concerns in countries such as the U.K. and Italy. Conglomerates are a current common source of undervaluation. Companies such as EXOR, the Fund’s second largest position, CK Hutchison and Thyssenkrupp trade for substantial discounts to our sum-of-the-parts appraisals. We continue to consider which names can be sources of cash for purchases with a view toward minimizing risk of loss and maximizing portfolio return.

**Contributors/Detractors**

(Q3 Investment return; Q3 Fund contribution)

Belmond, (64%, 2.85%) a collection of iconic luxury hotels located mostly in Europe, was the Fund’s largest contributor in the quarter. Owned Hotels are over 85% of the asset value, with Hotel Management fees another 5-10%. In August, management announced a strategic review of the Hotel Portfolio, which could result in a possible sale of some (or all) of the properties. Operationally, management confirmed guidance of $140-150 million for this year and the EBITDA target of $240 million by 2020. Group bookings for 2019 were up 70%, which should strengthen transient pricing. The company also announced that following last year’s Caribbean hurricane, Cap Juluca and La Samanna will re-open by the end of the year. Belmond is a good example of several important Southeastern traits. First, the payoff came swiftly, driven by the unanticipated news of a strategic review, which did not change the value of the assets but made value recognition more likely. Second, our engagement with management
was positive and collaborative, and we are pleased our partners decided to seek maximum value via outside bidders. Third, Belmond illustrates how our global research team benefits from being a single unit, as opposed to geographic or industry silos. The Fund’s Co-Manager Staley Cates surfaced the idea from the U.S.; our hotel CEO partners and board members from investments past and present helped confirm our case; and our London analysts handled the local engagement with CEO Roeland Vos, as well as the assessment of the company’s primary properties.

OCI (18%, 1.33%), a leading producer of nitrogen fertilizers and natural gas-based chemicals, was a strong contributor this quarter, as new projects continued to ramp up and commodity price strength came through. The methanol market should remain strong for the coming 4 to 5 years due to lack of supply and increasing demand. In the quarter, OCI completed its tender for the remaining shares of OCI Partners, the master limited partnership primarily made up of a single integrated methanol and ammonia facility on the U.S. Gulf coast. The price paid is already looking good as methanol’s price has continued to increase since the deal was announced. CEO Nassef Sawiris delivered value growth through this transaction as well as the successful completion and ramp up of major plants in Iowa and Texas in the last few years. With large capital expenditure (capex) projects complete, free cash flow should grow meaningfully.

CK Hutchison (10%, 0.71%), a conglomerate of telecommunications, health & beauty, infrastructure, global ports and energy, was a contributor in the quarter. CK Hutchison reported strong first half results, with (year over year) YOY revenue and EBITDA up +16% and +19%, respectively. Interim dividend per share grew by 11.5%, the first double-digit increase in the past decade. The company highlighted the strength of its Retail segment, which is the largest health and beauty retailer in the world with over 14,000 stores, 12 brands and 130 million loyalty members that contribute over 62% of sales. Oil price recovery added to Husky results. In the first half, revenue increased by 37% YOY and EBITDA by 47%. In the quarter, CK Hutchison announced the sale of its interests in several infrastructure projects at a 12X earnings and redeployed the proceeds to acquire an Italian telecom joint venture at 5X earnings. Management also repurchased the company’s discounted shares in the quarter for the first time in almost 2 years.

Melco (-34%, -2.20%), the Macau based gaming company, was the only notable detractor in the quarter. Investor sentiment soured on Macau due to concerns that growth will decelerate with ongoing U.S.-China trade war issues, a slower Chinese economy and weakening Renminbi. Following analyst downgrades, stock prices for
most Macau peers were down 40-50% in the last few months. While we agree that the decline in A-share markets and the slow-down in neighboring province Guangdong (export hub of China) will impact gross gaming revenues, we believe most of the impact will be on the lower-margin VIP business. Increased profits from the growth in the higher-margin Mass business should compensate for any VIP decline over time, as ongoing improvements in infrastructure (HK-Zhuhai-Macau bridge, high speed rail, etc.) and additional supply of hotel rooms make Macau more accessible. Melco is facing additional pressure, as the company looks to IPO its Studio City joint venture in this tough market to fund phase two of this property. On a more positive note, Melco’s new Morpheus hotel tower near its City of Dreams casino opened in June this year and is ramping up in line with expectations.

Portfolio Activity
An increasing list of qualifiers created more activity in the quarter. We purchased three new companies, two of which remain undisclosed, as we are still building positions. We exited Genting Berhad because its value stagnated and the Malaysian political environment grew less certain. We sold three additional businesses as their stock prices neared our appraisals. Hikma, a multinational, family-owned and operated, generic pharmaceutical company with three divisions: Branded Generics with products sold primarily in the Middle East and North Africa (MENA), Injectable Generics (U.S., MENA and Europe) and U.S. Oral Generics, was a successful investment, gaining 55% in the 10 months that we owned the company. The Injectables and Branded Generics made up most of the value with high barriers to entry. Over our holding period, our appraisal grew double-digits with considerable progress made in Injectables operations and what turned out to be a more favourable Generics environment. Hikma is an example of not only two quality businesses being temporarily overshadowed by a more competitive one (Oral Generics), but also of the importance of aligned corporate leadership. Much of the turn in results occurred after Chairman Said Darwazah proved his long-term ownership mentality by standing down from the CEO role to bring on well-respected industry veteran Siggi Olafsson.

Vocus was both a new purchase and an exit in the quarter after a quick 27% gain. Vocus is a full-service telco operator providing fixed network services (data, fiber, internet, voice) to Enterprise, Wholesale and Retail customers in Australia and New Zealand. Vocus sold off due to repeated earnings downgrades, management turnover, balance sheet concerns and National Broadband Network related worries. We initiated a position when the stock fell below the replacement cost of its fiber network. Good
2018 fiscal year results, debt refinancing and the appointment of a new, proven CEO created a rapid payoff before we were able to purchase a meaningful position.

Televisa, the Mexican media and cable company that we purchased earlier in 2018, reported solid results with the Cable segment growing at double digits. The Content segment, a laggard in recent years, reported 9% growth in advertising sales, higher network subscription prices and a step-up in its Univision royalty stream. As in the case of Vocus, we got a small position of Televisa before the stock ran away from us, gaining 32% over our brief holding period.

**Outlook**

Fear-laden markets usually yield investment opportunities. In less than 15 months, the Fund went from a high 29% cash position to being almost fully invested. We are well-positioned to capitalize on the uncertain environment, as we reach the 20th anniversary of the International Fund. Our 15-person global research team is finding prospective qualifiers around the world, working together across offices in Memphis, Asia and Europe. Our analysts are locals who intend to remain in their regions, because we view understanding cultural differences and norms and building long-term networks as critical to our research quality. Additionally, our cumulative research and investments over two decades have built our network and credibility, giving us insights and opportunities to engage with managements.

The International Fund owns strong businesses with capable management partners, who are focused on growing value for shareholders and pursuing value recognition. The Fund's price-to-value ratio (P/V) is in the low 70%s, which does not account for any assets or companies that might be sold at higher take-out multiples. As we continue to swap some of our higher P/V investees for compelling on-deck opportunities, the Fund will become even more discounted. We believe it is an attractive time to add to the International Fund.

*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 International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

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

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

Price / Earnings (P/E) is the ratio of a company’s share price compared to its earnings per share.

IPO is an initial public offer.

Capital Expenditure (capex) is the amount spent to acquire or upgrade productive assets in order to increase the capacity or efficiency of a company for more than one accounting period.

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.

As of September 30, 2018, the top ten holdings for the Longleaf Partners International Fund: OCI, 8.0%; EXOR, 8.0%; CK Hutchison, 7.3%; LafargeHolcim, 6.6%; Belmond, 5.5%. Melco,
5.1%, Thyssenkrupp, 5.1%; Baidu, 4.9%; Millicom, 4.7%; CK Asset, 4.7%. 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.
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Longleaf Partners International Fund declined slightly in the quarter, returning -0.06%, but outperformed the MSCI EAFE Index, which lost -1.24%. The Fund’s -0.06% return year-to-date (YTD) also exceeded the Index’s -2.75%. The Fund had a handful of companies with double-digit gains, but the small aggregate impact of a few detractors and a strong U.S. dollar offset the positive contributors. Currency translation cost the International Fund approximately -3%, reflecting foreign exchange fluctuations rather than challenges to our companies’ underlying operations or quality. Companies with large perceived emerging market (EM) and trade related exposure came under pressure in the quarter. The Emerging Market Index fell almost 8% as rising U.S. bond yields, heightened geo-political tensions, weaker EM currencies and increased prospects of a trade war all conspired to create the sell-off in EM equities.

We manage the portfolio without regard to index weights or style categories, and our returns come from the outcomes at our businesses, rather than top-down market sectors. For example, oil prices reached their highest level since 2014, making Energy the only notable positive impact to the Index. The sector rose 11%, while no other

**Average Annual Total Returns (6/30/18): Since Inception (10/26/98): 7.68%, Ten Year: 2.77%, Five Year: 5.71%, One Year: 5.25%.

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, 2018, the total expense ratio for the Longleaf Partners International Fund is 1.19% (gross) and 1.15% (net). The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.15% of average annual net assets.
sector generated more than 1%, and most were negative. The worst performing sector was Financials, down 6%. By contrast, the Fund outperformed the Index with no exposure to Energy and with a positive return for Financials (two insurance related businesses). Additionally, “growth” once again outperformed “value,” with an almost 3% difference in just the last three months. Our investment criteria require “growth” and “value” - quality businesses that will grow purchased at material discounts to what they are worth.

The most notable development of the quarter was having more investment qualifiers than cash after two years of higher than average cash levels and limited qualifiers. Cash ended the quarter in the low single digits, down from 13% three months ago and a recent high of 29% in June 2017. As predicted, we found compelling opportunities without an overall market correction. We began to find undervalued high quality companies in the latter part of 2017, as performance dispersion among global share prices widened. New investments ramped up in the first quarter. Over the last three months, we added two additional companies to the portfolio and increased the Fund’s stake in some of the more recent purchases. We have a robust on-deck list of prospective investments, and the remaining cash already has been allocated to a new buy order.

**Contributors/Detractors**
(Q2 Investment return; Q2 Fund contribution)

Hikma Pharmaceuticals (+19%, +1.07%), a multinational generic pharmaceutical company based in the U.K., had a strong quarter and was the largest contributor for the quarter and YTD. The company has three divisions: Branded Generics with products sold primarily in the Middle East and North Africa (MENA), Injectable Generics (U.S., MENA and Europe), and U.S. Oral Generics. The company reported positive results and ongoing cost reductions and reiterated guidance for the year, in spite of challenging pricing pressures across the U.S. Oral Generics industry. Injectables and Branded Generics make up the majority of our value and are strong underlying businesses with high barriers to entry. For decades, Southeastern has found opportunities in this kind of “good segment / bad segment” situation. The short-term focus on lower margin Oral Generics is overshadowing the growing, higher margin Injectables business, as well as the rising demand for Branded Generics in EM. We believe that the aligned and experienced leadership of CEO Siggi Olafsson and
Executive Chairman Said Darwazah, whose family owns 25%, will further grow the company and build value per share. During the quarter, we trimmed our position to reflect the higher price-to-value ratio (P/V) and to fund new purchases.

OCI (+17%, +0.87%), a leading producer of nitrogen fertilizers and natural gas-based chemicals in the U.S., Europe and the Middle East, was one of the largest contributors this quarter. The company refinanced its debt, pushing out maturities and lowering cost. OCI has reached a deleveraging phase, as free cash flow will ramp up materially with the methanol plant now online, the completion of major capital expenditure (capex) projects, and a positive pricing environment. The Iowa plant benefited from fertilizer pricing's “Midwest premium” to New Orleans (NOLA), which CEO Nassef Sawiris indicated is likely to increase, given the logistics of getting product to the Corn Belt. Methanol's 2Q contract prices were strong at $490 (vs. mid-$300s last year). Global demand for both nitrogen and methanol is increasing. The pricing outlook is strong for the foreseeable future with no new capacity coming online in the next 4-5 years and Chinese exports down 80% with the possibility of going away completely, given their cost disadvantage to U.S. natural gas and the Chinese government’s shutdown of higher polluting coal plants. In the quarter, OCI tendered for the remaining shares of OCI Partners, the master limited partnership (MLP) that is majority owned by OCI, primarily made up of a single integrated methanol and ammonia facility on the U.S. Gulf coast. OCI sells for well below the replacement cost of its assets. Sawiris is an owner-operator focused on value creation and recognition, as well as optimizing the capital structure and generating significant free cash flow.

C&C (+19%, +0.67%), the Irish cider and beer company, was a strong contributor in a quarter that saw the company make a significant acquisition that improves its route to market in England and Wales. C&C was able to buy Matthew Clark Bibendum, one of the largest distributors in the U.K., at a significant discount to its potential value because C&C was the only buyer able to move quickly in a deal that required fast closure. In addition to the deal, price increases over the last two years and a shift toward higher margin sales helped Scotland perform well, and the competitive environment in Ireland appeared to stabilize. C&C's management has been disciplined on capital allocation, holding back capacity for just such an opportunity while paying a dividend and shrinking the share count opportunistically. Our patience in supporting that approach has been vindicated with this opportunistic deal.
MinebeaMitsumi (-21%, -0.80%), the Japanese manufacturer of high precision equipment and components, was the largest detractor in the quarter. The company’s conservative forecast for this financial year ending March 2019 was below investor expectations. In May, a rumor that Apple would adopt OLED screens for all of its iPhones next year further affected Minebea’s share price because the company provides LCD backlights for Apple. This rumor was unverified and, we believe, unlikely to be true, given that MinebeaMitsumi recently decided to increase capital expenditures for the backlight business. More importantly, MinebeaMitsumi’s entire backlight business accounts for only about 2% of our appraisal, making the size of the stock move unwarranted. Minebea’s cash cow ball bearings business remained strong, with volume expected to be up 10% and revenue up 17% this fiscal year. Although optical devices and mechanical parts within the Mitsumi division are having a slow start in the first half of this fiscal year, demand is expected to increase in the second half, and the company has increased capacity by 50% for both sub-segments. Free cash flow generation continued to grow under the leadership of CEO Yoshihisa Kainuma, whose family owns over 6% of the company. Barring any major mergers and acquisitions, MinebeaMitsumi will be in a net cash position within two years. We added to our stake during the quarter after initiating the position earlier in the year.

CK Hutchison (-10%, -0.66%), a Hong Kong listed conglomerate of telecommunications, health & beauty retail, infrastructure, global ports, and energy was a detractor in the quarter. Italy’s telecom market had more aggressive competitive pricing than expected. Retailer Watson China’s comparable store sales growth in Q1 2018 was still slightly negative (-0.5%), despite gradually improving. The British pound and euro weakness impacted CK Hutchison’s numerous European assets. Additionally, concerns over a potential trade war between China and the U.S. not only pressured the company’s ports business, but also generated broad negative sentiment around Asian stocks. CK Hutchison’s well-balanced mix of businesses across the globe means that the short-term challenges facing some segments should not alter the long-term attractiveness of the entire portfolio. Overall, the company expects to deliver strong year-over-year organic earnings growth, partially helped by commodity price recovery. At 5x earnings, the acquisition from VEON of the 50% of the Italian mobile telecom operations that CK currently does not own will further boost earnings and accelerate merger synergies. In May, Victor Li took on the additional role of Chairman from his father, the founder.
Victor has proven his ability to run the business over the last four years, and we expect any market uncertainty about Li Ka-shing’s departure to be short-lived.

**Portfolio Activity**

During the quarter, we added two new, undisclosed investments to the Fund. One of these is a conglomerate with industrial businesses that have been impacted by tariff and trade concerns. The other is a telecommunications (Telco) company, a sector that has been weak around the world. Immediately after the quarter, we started buying a second new Telco.

We added to several holdings that became more discounted relative to the underlying strength of their core businesses. We also took Vestas Wind Systems, which we bought in the first quarter, to a full position. In the first quarter, we purchased Cemex convertible bonds, a small position that we sold in the second quarter, as other more discounted and higher quality opportunities emerged. We exited the Fund’s minimal stake in MLog, and we trimmed several more fully valued positions to enable adding to more discounted existing and new companies.

**Outlook**

The International Fund has become more compelling for long-term investors. The P/V sits in the low-70s%, and we are fully invested in competitively advantaged businesses managed by competent executives. Successful acquisition integration should help produce higher earnings at LafargeHolcim and C&C. Furthermore, at Fairfax Financial, Melco, OCI, Ferrovial and Belmond, we expect under-earning or non-earning assets to contribute substantial additional earnings. Additionally, the values of the wonderful businesses at Hikma, Melco, Ferrovial, Millicom and Minebea are dwarfing their poorer segments that created the misperceptions for us to invest. As the Fund’s largest owner, we are encouraged by having more investment qualifiers than liquidity for the first time in a while. We are confident that our companies’ increased earnings generation over the next couple of years in combination with the market’s more appropriate weighing of our investees’ values can yield important excess returns.

*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 International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. An index cannot be invested in directly.

MSCI Emerging Markets Index is a free float-adjusted market capitalization index designed to measure equity market performance of emerging markets. 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.

Capital Expenditure (capex) is the amount spent to acquire or upgrade productive assets in order to increase the capacity or efficiency of a company for more than one accounting period.

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.

As of June 30, 2018, the top ten holdings for the Longleaf Partners International Fund: EXOR, 8.3%; OCI, 7.0%; CK Hutchison, 7.0%; LafargeHolcim, 6.7%; Hikma Pharmaceuticals, 5.5%; CK Asset, 5.1%; Ferrovial, 4.9%; Baidu, 4.9%; Fairfax, 4.8%; Belmond, 4.7%. 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.
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Longleaf Partners
International Fund Commentary

1Q18

Longleaf Partners International Fund returned 0% in the first quarter versus the -1.53% performance of the MSCI EAFE Index. EXOR, the Fund’s largest position, had the most substantial impact by far. The absence of any meaningful performance detractors also benefitted results. Even with flat results thus far in 2018, over the last 12 months the International Fund’s 14.18% return substantially outpaced our absolute goal of inflation plus 10%.

During the quarter, markets outside the U.S. fell for various reasons including the threat of global trade wars in response to U.S. tariffs, anticipation of where Brexit negotiations will lead and concerns around the impact of U.S. inflation on higher interest rates and a weaker U.S. dollar. EAFE’s dollar-denominated return understated the amount of selling pressure overseas. In local currency, the index fell an additional 2.75%. (Because of the Fund’s significantly different country weights and cash, it gained only 60 basis points from the translation to USD implying company specific factors were more responsible for the relative results.) Over time currency fluctuations should broadly cancel out, but the company specific outperformance can endure.

Average Annual Total Returns (3/31/18): Since Inception (10/26/98): 7.78%, Ten Year: 2.61%, Five Year: 5.51%, One Year: 14.18%.

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.

At March 31, 2018 the total expense ratio for the Longleaf Partners International Fund was 1.33%. Effective April 1, 2018, the total gross expense ratio for the Longleaf Partners International Fund is 1.19% with a total net expense ratio of 1.15%. The expense ratio is subject to fee waiver to the extent a fund’s normal annual operating expenses exceed the following percentages of average annual net assets International Fund 1.15%.
During the 22 month period since the Fund’s cash exceeded 10%, we have patiently adhered to our Business/People/Price criteria, knowing that qualifiers would emerge with or without a market crash. The first quarter illustrated that increased volatility and only a minor market pullback could create enough dislocations for us to be productive. We bought stakes in five new companies and sold one fully valued company – substantial progress over three months for a portfolio that normally contains 20 companies and has low turnover. Cash reserves fell to 13%. Our on-deck list of prospective investments grew, an encouraging sign for further cash deployment.

The Fund’s new holdings came from around the globe with two in Japan, two in Mexico, and one based in Europe. These opportunities were mostly company or industry specific, rather than due to a broad turndown, although the Mexican stock market’s decline of over 6% in the quarter helped. Japan actually rose slightly, but opportunities there have expanded over time with improving governance and limited analyst coverage. In spite of progress, the governance standards in Japan and across Asia generally remain behind the West, where engagement can be more productive. Our cumulative network across the region after 20 years with offices on the ground, combined with the backgrounds of our Asian analyst team, gives us an important advantage in assessing corporate managements and understanding how generational change among controlling families might play out. We believe we will continue to find hidden gems in Asia and, as importantly, avoid those companies where managements are not focused on building shareholder value. Similarly, our long-time local presence and large contact network in Europe has enhanced our decision making and successful engagement in that region.

In another positive development, the Longleaf Trustees approved a fee reduction effective April 1 that will lower the cost of owning the Fund by at least 18 basis points per year. Assets in Southeastern’s regional strategies that help feed ideas to the Fund have grown over the last three years while International Fund assets have remained steady. Southeastern proposed sharing the economies of scale across all non-U.S. investors by reducing the Fund’s management fee to 1.10% on the first $500 million and 0.90% on the balance and capping total expenses at 1.15% (versus a 1.33% expense ratio in the first quarter). As the largest investors in the Fund, the employees at Southeastern pay the same fees as our clients and are committed to one share class where all investors are treated fairly and equally.
Contributors/Detractors
(Q1 Investment return; Q1 Fund contribution)
EXOR (+16%, +1.49%), one of Europe's leading investment holding companies, was the Fund's largest position and most substantial contributor in the quarter. The main component pieces of our appraisal are Fiat Chrysler Automobiles (FCA) (35%), PartnerRe (24%), CNH Industrial (19%), and Ferrari (17%). FCA's profits increased, and takeover speculation also pushed its stock up. PartnerRe's value was affirmed by two acquisitions of reinsurers, XL and Validus, at around 1.5X book value, well above both what EXOR paid for PartnerRe and our appraisal multiple. EXOR trades at a large discount to the market values of its component pieces. We believe the discount is unwarranted, as CEO John Elkann and his management team can produce additional double-digit value growth organically and via transactions, such as the planned spin out of Magneti Morelli from FCA later this year.

Hikma (+11%, +0.69%), a multinational, family owned and operated generic pharmaceutical company that we bought in October 2017 positively impacted results. The company has three divisions: Branded Generics with products sold primarily in the Middle East and North Africa (MENA), Injectable Generics (U.S., MENA and Europe) and U.S. Oral Generics. Brexit uncertainty and the challenging outlook for the U.S. generics industry provided Hikma at a discount. Disruptions in the least important segment, U.S. Oral Generics, overshadowed strong Injectables and Branded Generics businesses with high barriers to entry, which comprise 75% of our appraisal value. In the quarter the company brought in a new CEO in well-respected industry veteran Siggi Olafsson. Former CEO, now Executive Chairman Said Darwazah, vacated the operating position to focus on strategy and capital allocation. The Darwazah family owns 25% of the company through a family holding vehicle fully aligning them with other shareholder interests, as evidenced by this significant hire.

AIN Holdings (+30%, +0.62%), the largest prescription pharmacy chain in Japan, was a new investment in the quarter and quickly contributed. Japan's prescription dispensing pharmacy industry is highly fragmented among 58,000 pharmacies, mostly run by single-store operators. AIN, with roughly 1,000 stores and 3% market share, is the largest and most profitable chain. Despite the government's downward drug price revisions, the pharmacy market is expected to grow 3-5% annually, as prescriptions increase with an aging population and fulfilment moves from hospitals to pharmacies.
Japan's most recent price revision for April 2018 penalizes large chains, which gave us the opportunity to buy the stock at a discount. CEO Kiichi Otani, who owns over 9% of the company, remains confident that AIN can repeat its historic success at overcoming the impact of price controls. The company's net cash balance sheet should give AIN an advantage in both ramping up organic growth via on-site hospital pharmacies and acquiring under-performing pharmacies at single-digit earnings before interest, taxes and amortization (EBITDA) multiples. During the quarter, the company reported increased sales and margins and continued to close unprofitable stores while opening new stores that have a rapid payback.

OCI (-8%, -0.46%), a leading producer of nitrogen fertilizers and natural gas-based chemicals, was the largest detractor in the quarter. The stock declined in spite of higher methanol prices and debt refinancing that will reduce interest costs. A main source of short-term price pressure in the quarter was that a relatively large holder (Abraaj Capital) had to sell in order to raise capital for its other businesses. OCI has six production facilities located in the Netherlands, United States, Egypt and Algeria, and its new U.S. methanol plant in Texas will ramp up in 2018. As major capital expenditure projects come to completion, cash flow will accelerate meaningfully. The company sells for well below the replacement cost of its assets. CEO Nassef Sawiris is an owner-operator who remains focused on value creation and recognition, as well as optimising the capital structure and generating significant free cash flow.

**Portfolio Activity**

In addition to buying AIN discussed above, we purchased four other companies in the quarter, three of which remain undisclosed. Vestas is a global leader in onshore wind equipment and a provider of aftermarket services to the wind industry. Historically, rapid market evolution, low barriers to entry and government subsidies characterized industry economics. We have no competence in evaluating such a situation. However, we began investigating this business as the levelized cost of energy for new onshore wind (at good locations) reached parity with traditional power providers, reducing the reliance on subsidies and moving the industry more towards traditional, industrial company characteristics that we can understand. Competitive advantages from economies of scale, accumulated know-how and a global service network should drive future success. The market’s pullback, along with lower-than-expected results at the company provided enough of a discount for us to purchase. Since coming aboard in
2013, our corporate partners have fixed the balance sheet and transformed the company into a stable, net cash, dividend paying, share repurchasing company.

The new undisclosed Japanese company is a classic Southeastern opportunity of an entire business getting discounted because of potential headwinds at one segment that is of limited importance to the company’s long-term success. The most meaningful segment has 60% global market share in a growing business with barriers to entry and an owner operator at the helm. The uncertainty around NAFTA hit Mexican securities broadly, providing the opportunity to purchase both undisclosed Mexican companies, one of which has unusually strong pricing power around the world and the other with a dominant position within Mexico as well as attractive growth potential.

We exited Yum China (YUMC), the operator of KFC and Pizza Hut restaurants in China. YUMC was spun off from YUM Brands! in November 2016. The timing coincided with Asian markets being rocked by Donald Trump’s election. Because YUMC was not in an index and did not pay dividends, we were able to buy this franchise at a significant discount. Under the leadership of Micky Pant, YUMC delivered strong results in 2017. Total revenue rose 8% year-over-year and operating profits gained 23%. Same store sales recovered to +4% after three years of decline. On the capital allocation front, YUMC initiated a cash dividend, repurchased stock and expanded its buyback program. The gap between share price and our appraisal of the business quickly closed. In our 14 month holding period, Yum China generated a substantial 60% return.

**Outlook**

With the new purchases in the quarter, the Fund’s cash reserves declined to 13%, and we hope to add to several positions plus have a few more of our on-deck prospects qualify. The low-70%s price to value (P/V) also became more attractive with both the addition of companies selling for 30+% discounts to appraisal and the value growth at the businesses we already owned. For the last decade, global equity markets have been paced by USD assets with a growth bias. Today, we believe that a non-U.S., non-USD, concentrated value driven approach is well positioned for attractive risk adjusted returns.

We believe the Fund can outpace the index because of the rigor of our discipline and the flexibility to invest opportunistically, rather than based on momentum-weighted
country or sector allocations. Our local contacts and context should enable us to find attractive investments that we believe can compound at long-term double-digit rates. As the largest shareholder group in the Fund and long-term investors, we welcome the volatility and the investment opportunities it can bring.

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RISKS
The Longleaf Partners International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

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

Capex or Capital expenditure, are funds used by a company to acquire, upgrade, and maintain physical assets such as property, industrial buildings, or equipment.

One basis point is equal to 1/100th of 1%, or 0.01% (0.0001).

Book Value is the value of an asset as carried on a company’s balance sheet.

As of March 31, 2018, the top ten holdings for the Longleaf Partners International Fund: EXOR, 8.3%; LafargeHolcim, 7.2%; Hikma Pharmaceuticals, 6.6%; CK Hutchison, 6.3%; Fairfax, 5.9%; OCI, 5.7%; CK Asset, 5.2%; Ferrovial, 4.6%; Great Eagle, 4.6%; Melco, 4.5%. 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.

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Longleaf Partners International Fund delivered a strong 24.23% return in 2017, meaningfully exceeding our annual absolute goal of inflation plus 10% for the second consecutive year and falling just shy of MSCI EAFE’s 25.03%. The Fund’s sizable cash position, which posed no risk to capital, persisted throughout the year and more than accounted for the 2017 relative performance. The Fund exceeded the index for most of the year until the fourth quarter rally in interest rate sensitive industries, when the Fund declined 0.31% but the index advanced 4.23%. We seek to outperform the benchmark over the long term but were pleased that Longleaf International nearly matched the market in 2017 given high cash, limited exposure to the industries and countries that drove EAFE’s return and a market bias for momentum.

Most companies positively contributed to the Fund’s substantial 2017 results with over half of holdings posting double-digit gains. There was also an absence of notable performance detractors in both the fourth quarter and the full year. Investments that our management partners made in the last few years began to deliver returns. We have written previously about the market’s tendency to discount non-earning assets (NEAs) until cash is flowing. Several companies benefited from NEAs becoming profitable including Melco’s Studio City resort in Macau, EXOR’s purchase of PartnerRe, OCI’s newly producing Iowa nitrogen plant and Fairfax’s investments in Asia. Substantial multi-year cost cutting programs also yielded results, moving margins up at EXOR’s holding, CNH. LafargeHolcim cut substantial costs but still has plenty of potential to optimize further under new CEO, Jan Jenisch, who was a laudable partner at the Fund’s past investee, Sika. Our management partners pursued transactions to further entrench their competitive positions, focus on their core businesses or capture value opportunities that we believe will make the Fund’s cash a major benefit as more companies meet our strict criteria. Higher dispersion helped create a more robust list of potential investment cases worked out, and a number of stocks moved closer to our appraisals. We exited six investments, including one in the fourth quarter. More surprisingly, we bought four new companies, including one in the fourth quarter, as our on-deck list of prospective investments grew even as the market appreciated. Market dispersion benefited our search — only three of the eleven sectors within EAFE returned as much as the overall index, and Information Technology (IT) substantially outperformed all others, gaining just under 40%. Higher dispersion helped create a more robust list of potential opportunities that we believe will make the Fund’s cash a major benefit as more companies meet our strict criteria.

Contributors/Detractors
(2017 Investment return; 2017 Fund contribution; Q4 Investment return; Q4 Fund contribution)

Melco International (+116%, +5.66%, +2% +0.12%), the Macau gaming company, was the top contributor for the year and performed well in the fourth quarter as the industry gross gaming revenues (GGR) accelerated in the second half of 2017. November year-to-date GGR growth of 19.5% was substantially higher than Melco’s mid-to-high single-digit full year GGR.
growth expectation. With major infrastructure projects moving closer to completion, mass visits and spending increasing, and VIPs returning, concerns about potential over-supply from significant capacity additions in Macau turned into confidence that additional hotel and gaming properties will be well absorbed by the market. Melco Resorts is on schedule to open phase 3 (Morpheus) of City of Dreams (COD) in the first half of 2018, which will almost double the number of five star hotel rooms at COD. Upon the completion of Morpheus, we expect free cash flow (FCF) – and distributions to shareholders – to increase significantly with growth in industry GGR and the completion of significant growth capital expenditures (capex). Melco’s price remained below our appraisal, but we reduced the Fund’s exposure as the discount shrunk after the stock more than tripled in the last 18 months.

**EXOR (+44%, +3.35%, -3%, -0.39%),** one of Europe’s leading investment holding companies, was the Fund’s largest position and a strong performer in 2017. The component pieces of our appraisal are Fiat Chrysler Automobiles (FCA) (32%), PartnerRe (26%), CNH Industrial (21%), and Ferrari (16%). FCA’s profits increased substantially, and takeover speculation also pushed its stock up. CNH rose during the year as its agricultural equipment sales and margins grew, and the company received an investment grade rating. Ferrari’s stock reflected its stellar year operationally, if still not living up to hopes on the Formula 1 Circuit. In spite of EXOR’s appreciation, at year end the stock traded at a near 40% discount to the market value of its component pieces. European holding companies that are generally held up as EXOR peers tend to cluster around a 10% net asset value (NAV) discount, whereas some North American ones with substantial track records of value creation trade at NAV or even a premium. We believe EXOR’s extreme discount is unwarranted as CEO John Elkann and his management team can produce additional double-digit value growth on top of the significant value creation over the last decade. Attractive upside optionality remains in the underlying pieces of EXOR.

**Yum China (+54%, +2.80%, +1%, +0.16%),** the operator of KFC and Pizza Hut restaurants in China, was a significant contributor to performance during the year and continued to rise in the fourth quarter. Since its November 2016 spin out from Yum Brands!, YUM China (YUMC) has delivered strong results including KFC’s 7% same store sales growth year-over-year in Q3 2017. The company returned much of its growing FCF to shareholders, initiating a cash dividend of $0.10/share, buying back stock, and expanding its buyback program from $300mm to $550mm. The announcement that COO Joey Wat will become CEO and current CEO Micky Pant will become Vice-Chairman in March 2018 created additional optimism. Wat has been instrumental in KFC’s success, and we believe she will continue to create significant value. With the stock’s rapid appreciation more closely reflecting the company’s worth, we reduced the portfolio weight of YUMC.

**OCI (+44%, +2.54%, +8%, +0.63%),** a leading producer of nitrogen fertilizers and natural gas-based chemicals, added to the Fund’s 2017 and fourth quarter results. The stock’s strong performance last year closed much of the gap between price and our appraisal value, and we reduced the Fund’s stake in the fourth quarter. The company’s earnings grew as its new Iowa plant, a particularly large NEA, ramped production and fertilizer commodity prices recovered from 2016 lows. OCI has six production facilities located in the Netherlands, the United States, Egypt and Algeria, and its new U.S. methanol plant will ramp up in 2018. As its major capex projects come to completion, cash flows should accelerate meaningfully. CEO Nassif Sawiris is aligned with shareholders and remains focused on value creation and recognition.

**CK Asset (+46%, +2.15%, +6%, +0.38%),** the Hong Kong based asset holding company, was among the top contributors for the fourth quarter and year. The company achieved strong volumes of residential property sales in both Hong Kong and mainland China, and in the first half of 2017, sold the highest volume of residential property in Hong Kong. Rather than pay elevated prices for land, CK Asset (CKA) diverted sales proceeds to value accretive share buybacks at prices substantially below our appraisal. CKA spent HK$6.9 billion to buy over 3.3% of its shares, making it one of the top three repurchasers on the Hong Kong stock exchange for the year. To mitigate the cyclical nature of cash flows associated with property development, CKA diversified into stable infrastructure type assets around the globe, including gas pipeline and electric distribution company DUET in Australia, building equipment services provider Reliance Home Comfort in Canada, and fully integrated sub-metering company Ista International GmbH in Germany. To reflect this strategy, the company changed its name from Cheung Kong Property to CK Asset. In November, CKA sold The Center, a prime office building in HK for HK$33,000 per square foot and a capitalization rate of less than 2.5%. This price far exceeded our appraisal of the property and once again confirmed what great partners we have in Li Ka-shing, his son Victor Li and their team.

During the year, most portfolio holdings rose, and the couple of stocks that did not had minimal impact on performance. Similarly, in the fourth quarter, no individual stock declines meaningfully hurt the Fund’s results.

**Portfolio Activity**

It may seem odd that we made purchases given new market highs. We do not require a market correction to find qualifiers, just individual business value mispricing. And while the overall market had strikingly low volatility, a few good businesses’ stocks declined enough to enable us to buy three new investments in the first half and Hikma in the fourth quarter. Hikma, the pharmaceutical company, is an example of how complexity often leads Southeastern to investments. Industry-wide pressure over the last 18 months on the company’s smallest segment, Generics, took the stock to a multiple similar to generics peers. The company’s Injectables and Branded units, however, comprise the bulk of our appraisal. In particular, the complexity and sterility requirements of the Injectables business create high barriers to entry in a global industry expected to grow at double-digit annual rates. Chairman and CEO Said Darwazah and his family own nearly 25% of the company, and the share price
under his leadership has compounded at 13% per year since its 2005 initial public offering. The market’s overemphasis on the Generics industry challenges provided an opportunity to partner with a strong management team focused on growing and realizing value.

We sold six businesses during the year and trimmed some of the Fund’s strongest performers whose discounts to intrinsic value had diminished. Sika, Genting Singapore, and the Cemex bonds reached our appraisal values; Stada was acquired above our appraisal; we sold K Wah with Hong Kong real estate’s strength after our view of management changed; and in the fourth quarter, we sold the Fund’s small stake in Applus as it moved closer to our appraisal.

Outlook
The Fund’s last two years’ 39% cumulative return outperformed the index and substantially beat our absolute goal of real double-digit returns. Holding 20+% cash, which posed no risk of loss, more than accounted for the Fund’s 80 basis point shortfall versus the index in 2017. We are confident we can outperform over the next 5+ years. First, as was true in 2017, what we own – not what drives the index – will produce our returns going forward, and the Fund’s portfolio contains discounted strong businesses with growing values selling at an average P/V in the mid-70s% - a striking contrast to what we believe is an overvalued index increasingly driven by momentum in a narrower group of companies. We expect our differentiation from the index to be a source of strength. Second, the Fund’s cash is temporary until we find qualifiers, and with lower equity market correlations and the prospect of more volatility among stocks, we expect undervaluation opportunities will increase, as they did in late 2017, providing us additional investments that should drive future compounding.

It is our strong view that with most asset classes selling at full prices and many areas within the stock market trading at high multiples, the inflated index is more vulnerable to downside surprises than likely to continue double-digit gains. Ben Graham’s definition of an investment from Security Analysis written in 1934 has never been more relevant: “An investment operation is one which, upon thorough analysis, promises safety of principal and a satisfactory return.” We aim to preserve capital and compound at a real double-digit rate of return by owning a limited number of undervalued, high quality, competitively advantaged businesses where we are engaged with capable and aligned management partners. We have no doubt that we can deliver good performance because of our understanding of the drivers of each company’s value growth versus the associated risks, our ongoing dialogue with management, and our discipline to hold cash when businesses do not meet our stringent criteria.

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 International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

Active Share measures how much an equity portfolio’s holdings differ from those of the benchmark index.

IPO is an initial public offering.

“Margin of Safety” is a reference to the difference between a stock’s market price and Southeastern’s calculated appraisal value. It is not a guarantee of investment performance or returns.

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.

As of December 31, 2017, the top ten holdings for the Longleaf Partners International Fund: EXOR, 9.0%; LafargeHolcim, 7.4%; OCI, 6.9%; CK Hutchison, 6.5%; Fairfax, 6.2%; Hikma Pharmaceuticals, 5.9%; CK Asset, 5.3%; Baidu, 4.8%; Great Eagle, 4.7%; Ferrovial, 4.3%. 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.
Longleaf Partners International Fund gained 5.64% in the third quarter, outperforming our annual absolute goal of inflation plus 10% as well as the MSCI EAFE Index return of 5.41%, in spite of the Fund’s large cash position. The Fund’s substantial year-to-date (YTD) performance of 24.61% surpassed both our absolute goal and the index’s 19.96% return and contributed to the Fund’s relative strength over the last 1, 3, and 5 years.

Almost all of the Fund’s investments posted gains in the quarter, and there were no notable return detractors. The three most substantial contributors were located on different continents and had company-specific drivers. Their common thread was deeply aligned management partners who are pursuing transactions aimed at building value per share.

Over the last three months we added to two of our more discounted investments in Europe but bought no new companies. We sold one of our three Asian gaming related companies and trimmed the other two after strong price appreciation over the last 18 months. We also sold our Cemex bonds. The high cash and lack of new investments mask the activity level of our analyst team. As the year has progressed, in spite of strong broad market performance, our on-deck list of companies that meet our qualitative criteria and are within 10-15% of our required discount has grown. In our bottom up search for new investments, more performance dispersion amid our universe has generated a number of deeper-dive appraisals and prospective opportunities.

The Fund’s long-term potential to outperform will be due largely to our concentrated, bottom-up approach that makes the portfolio dramatically different from the index (as evidenced by the 95% active share). Our flexibility to own companies outside of the index provides opportunity distinct from the benchmark. Two of the Fund’s largest contributors in the quarter - Baidu and Fairfax – and YTD - Melco and Yum China – were not part of EAFE. Likewise, the portfolio is positioned opportunistically with no country or sector exposure requirements. The Fund outperformed in the third quarter without any investments in the four countries - Japan, the United Kingdom, France, and Germany - that made up over 60% of the benchmark’s allocation and performance. The weak dollar was a tailwind for the Fund and EAFE, but because the index had roughly two-thirds of its exposure in Europe versus one-third for the Fund, currency accounted for over 35% of EAFE’s return but only roughly 20% of the Fund’s. We believe the portfolio flexibility and current holdings of the International Fund’s make it much more attractively positioned than EAFE. The Fund’s cash is also an advantage, providing liquidity when we find new qualifiers, but also acting as a buffer in the event that the bull market reverses course.

**Contributors/Detractors**

**Baidu (+38%, +1.54%),** the dominant online search business in China, was also a top contributor. Baidu reported strong second quarter results after stricter regulations requiring more careful vetting of online advertisers and limiting the amount of paid search results that can appear on a web page had affected the search business last year. Growth of its core online marketing services revenue turned positive (+6%) after three consecutive quarters of decline. Operating profits grew 47% YOY with margins expanding to above 20%, the highest in two years, as Baidu reduced subsidies for its online to offline (O2O) business. The approximately 30% like-for-like growth guidance for the third quarter indicates Baidu's confidence in its core business recovery. In August, Baidu disposed of its margin dilutive food delivery business, following its plan to refocus back on its core search business as well as artificial intelligence. News of a potential IPO of iQiyi, Baidu’s video content business with over 30 million paying subscribers, was positive as it would reduce the significant investment that Baidu has been making in content. The demonstrable progress at the company corresponded with the January 2017 arrival of Dr. Qi Lu, Vice Chairman and Group President of Baidu, who has proven an excellent partner. The stock remains well below our appraisal, and we believe management will grow value per share further with the renewed focus on the company’s most profitable businesses.

**EXOR (+17%, +1.38%),** one of Europe’s leading investment holding companies, is the Fund’s largest position and was a strong contributor to third quarter performance. EXOR owns over 30% of Fiat Chrysler Automobiles (FCA) whose share price rose 64%. FCA announced that profits increased over 200% year-over-year (YOY) driven by strength in its Maserati brand and in South America and Europe. Additionally, takeout activity level of our analyst team. As the year has progressed, in spite of strong broad market performance, our on-deck list of companies that meet our qualitative criteria and are within 10-15% of our required discount has grown. In our bottom up search for new investments, more performance dispersion amid our universe has generated a number of deeper-dive appraisals and prospective opportunities.

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speculation persisted with rumors surrounding potential Asian buyers. Our partners at EXOR, Chairman and CEO John Elkann, a member of the founding Agnelli family, and Vice Chairman Sergio Marchionne (also CEO of FCA) first drew us to EXOR and have demonstrated superior capital allocation judgement. In the quarter, they announced plans to separate Magneti Marelli, FCA’s low margin component parts business. Over our five year holding period, the work of our partners has enabled our base EXOR appraisal to grow at an impressive 14% per annum. The company’s composition has changed, most notably with the acquisition of PartnerRe last year. The component pieces of our appraisal today are FCA (32%), PartnerRe (28%), CNH Industrial (19%), Ferrari (16%). The substantial value growth at EXOR has enabled the stock to remain attractively discounted, even following strong returns. We believe management can continue to produce double-digit value growth and that attractive upside optionality remains in the underlying pieces of EXOR, particularly in the investing opportunity at PartnerRE and the margin leverage at CNH Industrial as demand for agricultural equipment rebounds.

Fairfax Financial Holdings (+120%, +1.02%), the Canadian based property and casualty (P&C) insurer and reinsurer, is the Fund’s newest holding and was among the largest performance contributors in the third quarter. Several material corporate actions helped bring clarity to pieces of hidden value that CEO Prem Watsa had built. In India, Fairfax sold a portion of its stake in ICICI Lombard through an IPO and a private market transaction, producing a combined $950 million gain. In Singapore, Fairfax sold its subsidiary, First Capital, to Mitsui Sumitomo, one of Japan’s largest insurers, at a price more than three times book value. This multiple, which was much higher than traditional U.S. P&C companies receive, highlighted the inherent value in some of Fairfax’s international insurance subsidiaries. The First Capital transaction not only generated a $900 million after-tax gain, but also provided Fairfax with a continuing 25% quota share in First Capital’s underwriting and with the potential to participate in the difficult to access Japanese reinsurance market through Mitsui Sumitomo. The proceeds from these transactions will help fund Fairfax’s newly announced share repurchase program and will also replenish capital from recent hurricane losses, putting Fairfax in an excellent capital position to take advantage of a potentially hardening P&C market after these multiple catastrophes.

Portfolio Changes
As mentioned above, we made no new purchases. We added to our newer European investments during the quarter, Ferrovial and Belmond. Over the last twelve months, half of our new investments (Ferrovial, Yum China, and Fairfax) came from “recycled names,” businesses that we previously have owned directly or as part of another company. Our level of conviction in recycled names is usually higher because we know the businesses and management teams more intimately after being owners.

We exited two investments, Cemex bonds and K. Wah. We sold Cemex convertible bonds for a 23% gain two years after buying them. Trading above par and denominated in pesos, there was not enough upside left to keep us involved despite Cemex’s strong U.S. operating results and improved pricing in Mexico. Our Asian gaming investments, Melco, Genting, and Galaxy via our K. Wah position, performed strongly over the last 12-18 months, and we sold K. Wah and trimmed Melco and Genting. K. Wah benefitted from strength in its China and Hong Kong residential real estate business as well as Galaxy’s rebound. Because we had some reservations about management’s allocation of capital towards the company’s expensive land bank in Hong Kong and China, we sold K. Wah to reduce our overall exposure to Asian gaming given higher P/V levels. The investment returned 20% over our three year holding period.

Asian gaming, particularly in Macau, exemplifies how Southeastern uses our time horizon of 3-5+ years as an advantage when short-term fears dominate a stock’s price. In early 2016, Macau gaming was the Fund’s most discounted opportunity. Prices reflected the substantial drop in VIP revenue following China’s anticorruption campaign, but they ignored the longer term increase in much more profitable mass gamblers and the growth in visitors that new properties and infrastructure under construction would bring. Less than two years later, newly opened casinos and hotels have drawn more visitors and mass gaming revenue has grown double digits. Unexpectedly, VIP visitors also have increased from their low levels. The stocks have soared but remain below our appraisals because of the value growth. None of these positives yet reflects the impact of the new bridge to Hong Kong, expected to open in 2018, or other longer term infrastructure improvements.

Outlook
Company-specific results drove the Fund’s outperformance in the quarter and YTD in spite of the 25% cash position. The Fund’s flexibility to look different from the index and our bottom up, valuation driven discipline should allow the International Fund to continue to earn strong long-term returns. The companies we currently own offer additional attractive upside given their P/V in the high-70%s and the value growth that our management partners are capable of delivering. We do not need a market correction to find new qualifiers. Our edge comes in finding the best stock-specific opportunities rather than in investing in broadly discounted markets. Increasing dispersion generally favors our bottom up approach. The research work we have done throughout the year has given us a number of prospective investments simply waiting on prices to move in our buying range, and our liquidity will be an advantage when opportunity strikes. We believe each new investment will provide the Fund additional foundation for successful future compounding.

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As of September 30, 2017, the top ten holdings for the Longleaf Partners International Fund: EXOR, 9.1%, LafargeHolcim, 7.4%, CK Hutchison, 6.5%, OCI, 6.3%, Fairfax, 5.9%, Baidu, 5.3%, CK Asset, 5.2%, Melco International, 4.8%, Great Eagle, 4.7%, Yum China, 4.4%. 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.
Longleaf Partners International Fund Commentary

June 30, 2017

Longleaf Partners International Fund returned 8.42% for the quarter, outperforming the MSCI EAFE Index’s 6.12% gain and meaningfully exceeding our annualized absolute goal of inflation plus 10%. The Fund’s year-to-date (YTD) results were a substantial 17.06% versus 13.81% for the index. Continued strength in our Asian holdings drove much of the Fund’s outperformance, as did the fact that most of the stocks in the portfolio posted gains, and there were no material detractors. The Fund’s large absolute and relative results were driven by very different factors than the index and came in spite of higher-than-normal cash level — a reminder that successful stock selection in a concentrated portfolio with high Active Share can be a winning formula.

Asian markets continued to make notable gains, heavily fueled by the pricey Information Technology sector (particularly in China) that propelled many markets worldwide. EAFE’s largest country contribution came from heavily weighted Japan. The International Fund outperformed with no Japanese investments and minimal exposure to technology. We own a handful of Asian companies whose business results began to confirm our longer term investment cases for Macau gaming, Hong Kong real estate, and the newly spun out Yum China. Asia remains the most discounted market around the world, but stocks are no longer broadly cheap, particularly compared to twelve months ago. We trimmed several core Asian holdings but had limited opportunities to reallocate to in the region.

European equities represent over a 60% weight in EAFE, and this area produced over 75% of the index’s return. The U.S. dollar’s large decline against European currencies meant that over 50% of EAFE’s total return was due to currency conversion. By contrast, the Fund’s one-third weight in Europe and almost one-quarter exposure to Hong Kong, whose currency is pegged to the U.S. dollar, meant that currency translation added approximately 25% to the International Fund’s results. The second largest country contribution to EAFE’s return came from France, where the International Fund had no investments. The country’s performance, appreciation of the Euro, and gains in broader Europe, were influenced in large part by politics, which have had a disproportionate impact on markets over the last year. Going into the first round of French elections on April 23rd, there was considerable angst over the potential impact of a far left or far right candidate taking the presidency of Europe’s second largest economy.

The resounding success of Emmanuel Macron in the first round, and his subsequent election in the second, lifted this cloud. European indices rallied to new twelve month highs. Our European universe became more overvalued, and several companies that were close to qualifying as new investments moved out of price range. In the last several weeks of the quarter, Europe retrenched a bit, which could bode well for new investments in the back half of the year.

Continuing the trend from the first quarter, market strength over the last three months led to more portfolio sales than purchases in a challenging environment in which to deploy capital. We exited two positions that reached fair value and trimmed five stronger performers. We bought one new company and added to Fairfax Financial. This activity resulted in cash at 29%, the highest level since summer of 2004. The normal recycling process was slow as our long on-deck list of potential investments did a lot more price appreciating than depreciating in the quarter.

We are not discouraged by the limited new opportunities and are confident our patience and discipline will pay off. Our on-deck list contains an ample number of companies around the world that meet our qualitative criteria and are not far from qualifying on price. A temporary setback or disappointment at any of these could put their stocks in buying range. Likewise, a more widespread market correction could help us put cash to work. Despite elevated market levels, dispersion remains broad, and we are investigating numerous prospective investments.

Contributors/Detractors
(2Q portfolio return; 2Q Fund contribution)

Melco International (+52%; +2.83%), the Asian casino and resort holding company, was a primary contributor to performance as investors were encouraged by the accelerating recovery pace of industry gross gaming revenue (GGR) in Macau. GGR rose 17% in the first six months with May up 24% and June up 26%. Melco International’s substantial holding company discount to the market value of its 51% stake in Melco Resorts, which operates the casinos, shrank considerably this year, as Melco International consolidated its control over Melco Resorts. The consolidation is an example of the solid stewardship of our partner, CEO Lawrence Ho. Although the

Average Annual Total Returns (6/30/17): Since Inception (10/26/98): 7.81%, Ten Year: 0.88%, Five Year: 9.81%, One Year: 32.35%

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, 2017, the total expense ratio for the Longleaf Partners International Fund is 1.33%. The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.
stock price remains discounted, we trimmed our stake to maintain a more normal portfolio weight.

**Yum China** (+45%, +2.17%), the operator of KFC and Pizza Hut restaurants in China, also helped drive Fund performance. The company reported its first full quarter as a newly spun off independent company, and significantly exceeded expectations for operating margins. In addition to helping current results, this margin strength has ramifications for the future value of stores to be developed. Both the reported results and YUM China’s acquisition of online food delivery service Daojia, helped investors begin to realize that the enormous amount of meal delivery in China could end up being an additive weapon instead of a competitive threat for the company’s store base. With the stock’s significant gains, we reduced YUM China’s portfolio weight, but we believe management will continue to drive attractive value growth.

**Cheung Kong Property** (+19%, +0.87%), the Hong Kong and China real estate company, was another notable contributor. The company achieved strong volumes of residential property sales in both countries. In the first half of 2017, Cheung Kong Property was the largest seller of residential property in Hong Kong. Additionally, the value of Cheung Kong Property’s commercial Hong Kong properties was highlighted with the sale by the government of the comparable Murray Road property across from Cheung Kong Property’s Hutchison House. The transaction fetched a land premium that implied a price of HK$50k per square foot (psf) on a gross floor area (GFA) basis and a cap rate of less than 3%. Our appraisal of Hutchison House is around HK$16k psf, which reflects the 5% cap rate we use to appraise Cheung Kong Property’s office properties in Central, Hong Kong. Cheung Kong Property will begin redevelopment of Hutchison House which will allow the company to substantially increase the plot ratio from the current 22 story building to 38 floors. Managing Director Victor Li built value on two fronts by selling residential properties into a high price/high demand market and aggressively buying in Cheung Kong Property’s undervalued stock. YTD, Cheung Kong Property paid HK$36.9 billion to repurchase ~3.3% of outstanding shares at a substantial discount to our appraisal. In May the company closed its acquisition of Duet in Australia. In the same month, Cheung Kong Property took advantage of the low interest rate environment and issued US$1.5 billion 4.6% guaranteed senior perpetual capital securities, which are being used to repurchase additional shares.

**OCI** (+16%; +0.83%), the global nitrogen fertilizer and methanol producer, contributed positively to results in the quarter. Improved prices and volumes for related commodities led to greatly increased cash flow year-over-year. The company’s Iowa fertilizer plant began operating in April, which showed the market that this formerly non-earning asset is now about to produce significant earnings. OCI also made progress bringing its new methanol plant (“Natgasoline”) closer to its fourth quarter completion date. Late in the quarter, OCI’s stock price responded positively to rumors of private equity interest in the company. We are confident that our proven, aligned partner, Chairman Nassif Sawiris, will navigate any strategic outcome in a way that maximizes shareholder value.

There were no material detractors in the quarter.

**Portfolio Changes**

We bought one new company which is undisclosed as we hope to build a more meaningful stake. We increased the Fund’s position in **Fairfax Financial**, a Canadian based insurance and reinsurance operator that we began buying in the first quarter. The Fund previously owned the company for over a decade with a successful outcome. CEO and Founder Prem Watsa has continued to increase Fairfax’s value since we sold the stock in 2012. Fairfax is underwriting more successfully than when we previously owned it, is about to complete a value-accretive merger with Allied World, and still has the investing prowess of Watsa and his team. Because the merger is on the come and Watsa is holding a large amount of cash that is not producing significant income, near-term reported earnings per share are well below the company’s long run earnings power. We are excited to partner with Watsa at Fairfax again.

We exited STADA Arzneimittel, the German maker of numerous over-the-counter medicine brands as well as generic drugs. Price reached our appraisal when the Board of Directors recommended a purchase offer from a private equity consortium. This investment is a good example of the difference that good partners make. For 20 years STADA was a serial underperformer with entrenched management poorly allocating capital and running the company as a personal fiefdom. We followed the company and liked its strong brands and discounted price but could not get comfortable with the people. In 2016, a German activist group got involved and changed management and most of the board. We started our position in November of 2016; private equity obviously was seeing the same opportunity. The company’s new board and executives oversaw a disciplined, rational process that resulted in a good sale price and a nearly 50% gain for the Fund in less than 6 months. We also sold our stake in Genting Singapore, the casino company with a duopoly in Singapore and controlled by Genting Berhad. The stock reached our appraisal as the company reported a strong quarter. Hold-adjusted earnings before interest, taxes, depreciation and amortization (EBITDA) rose around 45% year-over-year (YOY), beating market expectations by a wide margin. The company gained mass market share. Write-downs on VIP receivables fell over 80% YOY, and management’s statements regarding the balance sheet implied a lower level of bad debt provisions going forward. The company also announced its intention to redeem S$2.3 billion of perpetual securities which would save almost S$1.2 billion in interest costs. In our 19 month holding period, Genting Singapore generated a 52% return.

**Outlook**

The P/V of the Fund in the mid-70s% is higher than usual, as is the 29% cash position. In spite of a more challenging market for investing in undervalued securities, we are confident that the businesses we own have the financial and competitive strength to produce solid results. Our management partners are building values through strong operations, as
well as prudent capital allocation. In addition, our productive research has built an attractive list of high quality prospective investments that we are positioned to buy as the market provides inevitable opportunities. We believe in the Fund's ability to generate long-term outperformance based on what we own and what we will own as a result of Southeastern's time-tested value discipline, deep global research team, and available firepower.

We are pleased to announce that Josh Shores will become a co-manager on the International Fund effective July 10 in recognition of his successful investment contributions during his 10-year Southeastern tenure. Josh has covered investments in Europe, South America, and Asia, and has resided both in Memphis and London. Scott Cobb will step away from co-managing the International Fund to allow him the time and focus required to engage more deeply with corporate managements in his role as Managing Partner on our concentrated, engaged European strategy. Scott will continue to lead our research efforts in Europe, and his work remains an important source of potential investments for Longleaf International.

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**Cap rate (capitalization rate)** is the rate of return on a real estate investment property based on expected income.

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

As of June 30, 2017, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: Melco, 5.0%; Yum China, 4.4%; Cheung Kong, 5.0%; OCI, 6.0%; Fairfax, 5.0%; STADA, 0%; Genting Berhad, 0.9%; Genting Singapore, 0.0%. 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.
Longleaf Partners International Fund returned 8.80% for the quarter, outperforming the MSCI EAFE Index’s 7.25% and meaningfully exceeding our absolute annual goal of inflation plus 10%. This performance extended 2016’s strong absolute results and over 1100 basis points of benchmark outperformance.

A large portion of our return was attributable to our gaming resort investments in Macau, where industry gross gaming revenue accelerated above consensus estimates in the last two months to approximately 18% growth year-over-year. Most stocks in the portfolio rose. The several that declined only had slight impact on the Fund’s performance and created a couple of opportunities to add to our positions at deeper discounts.

Since the U.S. election in November, global markets have levitated. Full valuations in parts of the world have become more extended. Our European universe appears fairly to slightly overvalued, while the Asia Pacific region is more attractive. In other parts of the world we see pockets of prospective opportunity. The chart below illustrates the relative valuations of major stock markets. Our portfolio reflects the regional opportunity set with the portfolio invested 39% in Asia, 35% in Europe, 5% in Latin America, and the remainder elsewhere. Cash is almost 18%.

Overall market levels constitute a challenge for the value oriented investor, but tight capital market correlations of the last eight years have started to break down. The central bank inspired lock-step elevation of risk assets started in the early days of the U.S. Subprime Crisis. Passive investing in index funds and exchange-traded funds rose in popularity as the lack of price dispersion reduced the opportunity for active managers to outperform. We believe this has changed. As the graph below indicates, correlations across global asset classes have dropped back to 2006 levels. Our strong performance in 2016 and through the first quarter of 2017 when correlations were declining from high levels is an indicator of how active management can deliver.

With increased dispersion, our on-deck list has expanded over the last six months even as broader markets have risen. We have bought five new investments over that time, two in the first quarter of 2017. Company-specific investments that require our brand of deep due diligence and owner-oriented engagement translate to increased opportunities for outperformance. Our global network of contacts continues to provide an advantage as these important partners provide investment ideas, insight into companies and managements, and resources to help bring about positive outcomes at our holdings. Our positive result at Sika, the one company we exited in the quarter, was due in part to gaining an understanding from various contacts of the business quality, the legal hurdles, and the interests of the different parties involved in the controlling family’s effort to sell its stake to St. Gobain.
Contributors/Detractors
(1Q portfolio return; 1Q Fund contribution)

MELCO INTERNATIONAL (+30%; +2.02%), the Asian gaming operator, was the primary contributor in the quarter. Investor sentiment towards Macau has improved since August 2016 when industry gaming revenues posted their first year-over-year (Y/Y) growth in 26 months. In the last two months, growth of industry gross gaming revenue accelerated above consensus estimates to about 18% Y/Y. While overall visitation was essentially flat in FY16, overnight visitations grew 10%. Overnight visitors tend to be higher value customers relative to day trippers. The higher margin mass business grew double-digit rates in each of the last three quarters; and, even the VIP business is staging a comeback, supported by junket consolidation and increasing credit availability. The increase in demand has helped absorb new supply. Melco’s City of Dreams maintained its market share even with the opening of the $4 billion Wynn Palace across the street, and Melco’s newest property, Studio City, continued to ramp up, substantially growing earnings before interest, tax, depreciation and amortization (EBITDA). Competition remains rational with all participants focused on margins rather than reducing prices to gain share. We expect the new ferry terminal to open this year, which will bring mass tourists directly to Cotai, where City of Dreams is located. Importantly, Melco re-financed $1.4 billion in Studio City secured credit facilities at attractive rates in late 2016 which removed an overhang on the stock. CEO Lawrence Ho and his team have proven to be strong operators and astute capital allocators. In January, Melco Crown, which Melco controls, declared $1.3 per share in special dividends (implying over 8% yield).

EXOR (+21%; +1.63%), the Netherlands based holding company of the Agnelli family, was another top contributor in the quarter. Investor sentiment towards EXOR is at the early stages of its transformation under the leadership of CEO John Elkann and remains attractively priced at a discount to our appraisal.

LafargeHolcim (+13%; +1.05%), the world’s largest global cement, aggregates, and ready-mix concrete producer, also added to the Fund’s return. The company’s 4Q results demonstrated continued success in pricing, operating cost control, and disciplined capital spending which helped EBITDA grow 15.5% and free cash flow increase 107%. For 2017, CEO Eric Olsen guided to 2-4% volume growth helped by resumed growth in India and Latin America and continued volume growth in the U.S. Improved volumes combined with pricing and cost controls should drive double-digit EBITDA growth and strong free cash flow (FCF) generation. FCF along with divestitures has fortified LafargeHolcim’s balance sheet, and the competitive landscape is positive with few slated capacity additions. We expect dividends and share repurchases to accelerate as cash flow grows.

K. Wah (+43%; +0.95%), the Hong Kong and China real estate company that also owns 3.8% of Macau casino operator Galaxy Entertainment, was another major contributor in the quarter. All three of the company’s value drivers performed strongly. Book value grew 16% and the dividend grew 8% Y/Y. In 2016, the company sustained a second year of elevated sales of Hong Kong residential developments at high margins. K. Wah also achieved strong pre-sales of its Hong Kong K-City residential project at the former Kai Tak airport for prices almost double what it will cost to complete. In China, K. Wah achieved EBITDA margins above 50% on real estate sales due to its low cost land bank and strong price growth in tier 1 cities, where most of its land bank is located. During the quarter, the company’s stake in Galaxy Entertainment appreciated by over 25% as sentiment towards Macau improved (see discussion of Melco above). We took advantage of K. Wah’s gain to trim the position as our case began to rely more heavily on management’s capital allocation, where we have somewhat less confidence in the controlling shareholder’s interest in closing the remaining discount.

There were no material detractors in the quarter.

Portfolio Changes
In addition to K. Wah mentioned above, we reduced three positions and increased our stake in two companies. As noted above, we bought two new holdings and sold one, our successful investment in Sika, the Swiss producer of construction specialty materials and services, following a 50% return over our 16 month holding period. With helpful insights from our network of related contacts, when we purchased the stock, we were confident that the significant margin of safety, top quality operating management, and high quality business more than offset the uncertainty surrounding the efforts by the founding family to sell its controlling stake to a French competitor. Through extraordinary operating results and positive developments in the legal dispute between the parties, the share price exceeded our assessment of intrinsic value in a short period. The independent, non-executive directors on the company’s board, Chairman Paul Haelg, and CEO Jan Jenisch all merit special commendation for fortitude and outstanding performance in a difficult governance situation.

We started buying two new investments in the first quarter. One is a financial services business that we have owned before with a very satisfying outcome. The other is a company we have followed for years. We still are working to purchase full positions, and thus, will wait to discuss the companies more in depth.

Outlook
Our corporate partners have been delivering solid operating results and capital allocation choices. The Fund’s F/V ratio is in the low-70s%, and the competitively advantaged businesses we own and superior management teams running them should be able to grow values per share at above average rates. Disruptions from the geopolitical uncertainty around the world, particularly with elevated market levels in many places, could deliver additional opportunities. Our global research team is already adding strong businesses to the on-
deck list. With our almost 18% cash position, we are positioned to take advantage of the next qualifiers. We believe our proven discipline and robust process mean that our current holdings and prospective investments portend good risk-adjusted returns for the foreseeable future. Thank you for your continued support of Longleaf International.

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RISKS

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MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

“Margin of Safety” is a reference to the difference between a stock’s market price and Southeastern’s calculated appraisal value. It is not a guarantee of investment performance or returns.

Enterprise value (EV) is a company’s market capitalization plus debt, minority interest and preferred shares, and less total cash and cash equivalents.

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

EV/EBITDA is a ratio comparing a company’s enterprise value and its earnings before interest, taxes, depreciation and amortization.

Price-to-book value (P/B) is the ratio of market price of a company’s shares over the value of a company’s assets as carried on the balance sheet.

As of March 31, 2017, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: Sika, 0%; Melco, 7.9%; EXOR, 8.2%; LafargeHolcim, 8.4%; K. Wah, 2.2%. 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.
Longleaf Partners International Fund returned 12.20% for the year, meaningfully outperforming the MSCI EAFE Index’s 1.00% return and beating our absolute goal of inflation plus 10%. In the fourth quarter, the Fund fared better than the index, falling -0.31% versus the index’s -0.71% decline.

In two distinct environments, the Fund outperformed with minimal exposure to the areas that periodically drove market returns. In the first nine months, perceived “safe” stocks dominated. The fourth quarter reversed, with cyclical gains and defensive and minimum volatility stocks declining rapidly to end the full year among the worst performing areas. Global markets had significant quarterly price volatility across geographies. For example, Hong Kong markets suffered declines in the first and fourth quarters amid China concerns, with the fourth quarter further complicated by fears of higher U.S. interest rates and impacts of a Trump presidency on global trade. Our Hong Kong exposure added positively to 2016 results despite these fears. In Europe, markets rebounded quickly in the third quarter after a negative first half overshadowed by Brexit and European terrorist attacks.

The International Fund’s successful performance had little to do with the index’s return. 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 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)**

**adidas** (+70%, +3.58%), the German-based global sportswear and equipment brand, was the Fund’s top contributor for the year. We sold our stake in the third quarter as the price approached our appraisal value. We engaged in a productive dialogue with the company when necessary since initializing the position in August 2014. Over that time, adidas re-focused on its core brand, grew revenues, sold or sought buyers for non-core segments including Rockport and golf, repurchased just over five percent of the company at substantially discounted prices, replaced the CEO, and added two highly qualified owners to the Supervisory Board, one of whom we proposed. In the Fund’s two year holding period, adidas returned 122% (in U.S. dollar) and 166% in local currency (euro).

**Great Eagle** (+60%, +3.06%), a diversified property holding company based in Hong Kong also added to the Fund’s 2016 return. Great Eagle announced a $2 per share special dividend in the second quarter after monetizing commercial real estate in San Francisco at a sub 4% net operating income cap rate. The company also successfully completed the acquisition of a prime hotel site in Roppongi, Tokyo, expected to be operational by the 2020 Tokyo Olympics. In addition to the Langham Hotels owned and operated across global capital cities, Great Eagle owns Hong Kong-listed Champion Real Estate Investment Trust (REIT) and Langham Hotel REIT. The company is led by Dr. Lo Ka Shui who owns 59% of Great Eagle and has an exceptional record of savvy acquisitions and divestitures, as well as value growth.

**CEMEX** (+41%, +1.94%), the global cement, ready-mix concrete, and aggregates company, performed well, reflecting improved fundamentals. The convertible bonds that we own have an attractive risk/reward profile, with asset coverage over twice the debt. Our long-term upside beyond par value, plus the 3.75% annual coupon, will depend on where the equity price trades relative to the conversion price. Our appraisal of CEMEX grew during the year, and we expect further appreciation since its core markets of Mexico and the U.S. are improving. Tonnage prices are rising, with cement plant capacity utilization in the U.S. at approximately 95% in the fourth quarter. On the capital allocation front, the company divested non-core assets. Proceeds from asset sales, as well as free cash flow, continue to reduce debt.

**Sika** (+35%, +1.77%), the Swiss provider of specialty materials and services for the construction industry was another major contributor in the Fund for the year. Since we initiated

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**Average Annual Total Returns (12/31/16): Since Inception (10/26/98): 7.05%, Ten Year: 0.62%, Five Year: 6.47%, One Year: 12.20%**

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 International Fund is 1.28%. The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.
the position, the company has consistently reported strong quarterly results, with increased revenues and improved margins across all regions. Prior to our investment, the founding Burkard family made an agreement to sell its 16% stake to French company Saint-Gobain at an 80% premium without a concurrent offer to others shareholders. We have taken a public stand against the proposed deal, as we believe that all owners should be treated equitably. In late October, Sika's share price rallied after an initial corporate governance win in the two year battle against the Saint-Gobain takeover. The Swiss court ruled that Sika could limit the voting rights of the Burkard family to 5%, essentially blocking the proposed deal. We trimmed the position after strong performance, and we remain optimistic about value growth and the outlook from today.

**BR Properties (+25%, 1.55%)**, one of the main commercial real estate investment companies in Brazil, also stood out as a strong performer in 2016. We sold the holding in the second quarter on the strength of a recovery in the company’s earnings, in addition to an offer by GP Investments, a Bermuda-based investment company, to acquire 70% of BR Properties’ outstanding shares.

**OCI (-29%, -1.52%)**, a global fertilizer and chemical producer, was the largest detractor in the Fund for the year, even after a rebound of 18% in the fourth quarter. The two main pressures on the share price were weakness in nitrogen fertilizer prices and the cancellation of the CF Industries merger as a result of the U.S. government crackdown on tax inversions. Despite depressed fertilizer prices, nitrogen remains an essential part of global food production, and global demand is growing by around 2%, which will help deplete the current excess supply by 2018. Given the high cost and long lead time of building a new plant, it is unlikely that new capacity will be built in the medium term. OCI owns the newest and most efficient nitrogen fertilizer plants in the industry, with its large, new Iowa plant now producing. Its Texas Greenfield methanol plant comes online in late 2017. OCI recently initiated a cost savings plan over $100 million, $65 million of which is executed, and the company has completed the majority of its large capital expenditures. We expect significant earnings production in the coming two years, and CEO Nassef Sawiris and his team are working diligently to grow value per share. In early December, the company announced a 25% premium offer to acquire all publicly held shares of OCI Partners in exchange for OCI shares. The acquisition should allow for operating synergies between methanol assets and incremental free cash flow with a positive impact on the combined balance sheet in 2017.

**CK Hutchison** (-14%, -1.24%), a global conglomerate comprised of five core businesses (retail, telecommunications, infrastructure, ports, and energy), was the only other noteworthy detractor in the Fund for 2016. 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. In recognition of the steep discount at which CK Hutchison trades to value, the company initiated its first share repurchase in the fourth quarter.

**Annual Portfolio Changes**

We took advantage of the market volatility and individual company performance throughout the year. We exited several core holdings in the first half, including ALS, Mineral Resources, and BR Properties, as well as Philips, SoftBank, and adidas in the third quarter on the back of share price strength. We exited our small position in Vivendi in the fourth quarter. Currency translation to U.S. dollars dampened the return on our investment in this euro-denominated business. In the Fund’s two year holding period, Vivendi returned -5% in USD but added 21% in local currency.

We bought a small position in **Applius** in the second quarter, and we added three new purchases in the fourth quarter. We bought two European-based businesses. One of these we owned during the Eurozone crisis in 2011, and it remains undisclosed while we build the position. The other is **STADA Arzneimittel**, a leading European pharmaceutical company based in Germany. Approximately 60% of this business is generic drugs, and 40% is the over-the-counter branded drugs business that is high margin and better growing. STADA historically traded at a depressed value due to questionable governance and management under its prior executive team. The former CEO used a German “restricted transferability of shares” rule that acted as a poison pill, allowing management to block daily trading of public shares. A local German activist investor, Active Ownership Capital (AOC), took a large stake in the company early in 2016 and made substantial governance improvements, including replacing the CEO with an interim executive, replacing the Chairman, replacing five of six supervisory board members, and abolishing the restricted transferability of shares. New Chairman Ferdinand Oezer is focused on hiring the executive committee and ensuring alignment through ownership incentives at the executive and board level. There is significant room for operational improvement at the business. We also added **Yum China**, which recently spun out of Yum! Brands, a company our team knows well from the Fund’s successful multi-year prior investment. Yum China has exclusive rights to KFC, China’s leading quick-service restaurant concept, Pizza Hut, a leading casual dining brand, and Taco Bell, with expansion plans in China. Yum China has over 7,300 restaurants and more than 400,000 employees in 1,100+ cities in China with additional expansion opportunity in urban centers. Yum China’s brand and scale are unique advantages and fit the desires of a rapidly growing middle class, where eating outside the home is becoming more commonplace.
Outlook
In 2016 we delivered substantial absolute performance, and the Fund far outpaced the index, even with a larger-than-average cash balance. The International Fund’s price-to-value remains attractive in the high-60s%. We believe that uncertainty over the future of the Eurozone in the wake of Brexit and pending elections in France and Germany, as well as world trade under a Trump administration, is likely to lead to further volatility and opportunity. Weakness in emerging markets and China macro fears are creating further opportunity in Asia to buy world class businesses like Yum China that are trading at meaningful discounts to our appraisal of intrinsic value. The Americas have several near-qualifying opportunities on deck. We believe we have a portfolio of competitively advantaged businesses that are financially strong with management partners who can go on offense in times of uncertainty. Our on-deck list has expanded in the last few months with new prospective investments around the world. Our 18% cash will allow us to invest in high quality businesses with strong management partners. We believe our existing companies and management teams will continue to deliver both organic and transaction-driven value growth that should benefit our future results, as they did in 2016.

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**RISKS**

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**REIT** is a real estate investment trust.

**EBIT** is earnings before interest and taxes.

**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 International Fund: Great Eagle, 6.0%; Cemex, 5.1%; Sika, 2.7%; OCI, 5.7%; CK Hutchison, 7.0%; Applus, 1.1%; STADA, 2.5%; Yum China, 4.5%. 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.
Longleaf Partners International Fund meaningfully outperformed the index in the third quarter with a return of 12.55%, nearly double the 6.43% return of the MSCI EAFE. Year-to-date, the Fund has risen 12.55%, far surpassing MSCI EAFE's 1.73% return in the same period.

The sustained environment of slow global economic growth and low interest rates has reduced capital costs associated with acquisitions and spurred consolidation that can increase not only revenues but margins. Most of our companies were positive contributors this quarter. Actual or anticipated successful integration of mergers and acquisitions, along with transactions that strengthened balance sheets, helped drive our strong performance. Melco International benefitted from consolidating Melco Crown’s results in its financial reporting, after increasing its ownership stake in the second quarter. LafargeHolcim reduced debt through asset sales and captured synergies from last year’s merger. CK Hutchison gained approval for a merger that will create the largest mobile phone operator in Italy. Additional smart management action, including EXOR’s moving its headquarters from Italy to the Netherlands, has also been rewarded by the market.

Capable management partners deserve particular credit for achieving returns of this magnitude when economic growth rates are not powering earnings. We take a long-term ownership mindset to investing, and we consistently engage with our management teams to encourage them to take advantage of the environment to build value per share. Our strong performance this year highlights the benefits of partnering with aligned management teams that are focused on growing value, and we believe our partners will continue to drive strong performance in this uncertain environment. Our partners at Hong Kong real estate companies have a particularly compelling opportunity today, as historic low interest rates have resulted in record high prices of Hong Kong real estate. The spread between cap rates implied in the stock and physical properties transact has rarely been as wide as it is in Hong Kong, and we are encouraging our management partners to take advantage of this once in a lifetime opportunity to sell property at these levels.

The historically low interest rate environment has impacted our portfolio positioning and future opportunity set. We trimmed or sold several positive performers, and our cash balance has grown as a result. Cash was the only significant detractor from relative performance in the quarter. However, we believe this heightened cash level is temporary, as we have a solid on-deck list of potential qualifying investments in Europe and Asia where we could quickly put capital to work. Despite posting a strong quarter of performance, Hong Kong, Japan, and other Asian markets remain attractively discounted on an absolute and relative basis. European markets are less broadly discounted than Asia, but we are working on a number of businesses that are discounted for company-specific reasons, rather than broad market cheapness. Continued uncertainty of what Brexit will mean for European markets over the longer term should lead to further volatility and create opportunities to buy high quality businesses at a discount.

Contributors/Detractors

Melco International (+42%; 2.4%), the Macau casino and hotel operator, was the Fund’s top contributor in the quarter. After Melco International (Melco) increased its ownership of Melco Crown (MPEL) to 38% last quarter, Melco’s subsequent consolidation of MPEL’s results in its financial reporting nearly doubled book value per share. Melco’s share price also benefitted from an easing of headwinds in Macau, as industry gross gaming revenues hit an inflection point in August and grew (+1.1% year-over-year) for the first time in 26 months. The industry continues its transition from VIP to mass gaming focus, and Melco, with CEO Lawrence Ho as our partner, is well-positioned as a leader in the higher margin, fast growing mass gaming business. The stock remains among our more discounted in the portfolio.

LafargeHolcim (+31%, +2.1%), the world’s largest global cement, aggregates, and ready-mix concrete producer, was also a top contributor. During the quarter, CEO Eric Olsen and his management team made progress with respect to divestitures, merger synergies, and pricing. The company sold assets in India, Sri Lanka, and Vietnam at attractive prices. These sales, coupled with previously announced transactions in South Korea, Saudi Arabia and China, got the company to its 2016 Swiss Franc (CHF)3.5 billion divestiture goal ahead of schedule and helped LafargeHolcim reduce its debt from CHF18 billion to 13 billion in 2016. An announced CHF1.5 billion of additional divestitures are targeted for 2017, which will move the balance sheet to investment grade quality and...
allow management to return free cash flow to shareholders. Expected synergies from last year’s merger between Lafarge and Holcim have come through on target with an expected CHF450 million this year. Industry cement pricing is moving in the right direction. During the quarter, prices increased 2.2% sequentially versus 1.2% in Q1 2016 and -1.6% in 4Q 2015. LafargeHolcim now has higher prices in almost 70% of its markets versus 2015 levels. Even though volumes did not grow in all markets, higher prices and large cost savings resulted in strong earnings before interest, taxes, depreciation, and amortization (EBITDA). Despite the stock’s rise, the company remains one of the more undervalued securities in the portfolio.

CK Hutchison (+18%; 1.2%), the Hong Kong-based global conglomerate, was another top performer in the quarter. Following the initial shock of Brexit in late June, the company’s limited impact from a weaker pound became more apparent. After regulators rejected the company’s proposed acquisition of O2 by its UK mobile phone business Three UK, CK Hutchison received approval in September for the merger of Three Italia with Wind in a 50/50 joint venture between CK Hutchison and VimpelCom. This combination will create the largest mobile operator in Italy with approximately 37% market share versus the two remaining primary competitors. CK Hutchison expects at least 5 billion euros of synergies from this merger, with most to be delivered within three years of the transaction closing in the fourth quarter of 2016. These projected synergies exclude any upside from selling assets and spectrum, utilizing tax losses, or refinancing expensive debt. CK Hutchison’s European businesses grew nicely, and the company expects to see solid global growth, particularly in its telecom and retail segments. Li Ka-shing and his son, Victor, continue to build value for shareholders.

Portfolio Changes
We exited three successful holdings during the quarter. Currency translation to U.S. dollars dampened the return on our investment in euro-denominated businesses Philips and adidas. We sold health and wellness company Philips. Although we applaud actions management has taken over time to address the conglomerate discount, including the recent partial initial public offering of its lighting business, the execution has taken longer than expected and reduced our confidence in the case. Philips added 76% in local currency (euro) and 40% in U.S. dollar terms in the same period. We also exited SoftBank, the Japan-based diversified telecom and technology company. In June, President and heir-apparent Nikesh Arora unexpectedly resigned after CEO Masayoshi Son announced his intention to remain CEO for the next 10 years. We viewed Arora as important to SoftBank’s capital discipline. Not long after his departure, the company announced the purchase of U.K.-based microchip business ARM Holdings for $32 billion or 44 times earnings. The change in leadership combined with the transformative acquisition of a business with a competitive advantage that we find difficult to assess over the long term led us to sell the position. SoftBank added 19% since we bought it in March 2015.

Outlook
The International Fund sells for a price-to-value in the mid-60s%, and appraisals grew for several of our businesses in the quarter. Cash levels grew to 27% as we sold and trimmed strong performers, but we believe we will continue to find new qualifiers in Europe and Asia. We delivered strong double-digit returns, even with the larger than average cash balance. Our future returns are not dependent on higher interest rates or economic growth. The qualitative and financial strength of our companies, along with continued value-additive action from our capable management partners, should drive our long-term performance.

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

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Funds distributed by ALPS Distributors, Inc.
Longleaf Partners International Fund Commentary

June 30, 2016

Longleaf Partners International Fund outperformed the MSCI EAFE Index in the first half of 2016, with a 0.00% return compared to the index’s loss of -4.42%. In the recent quarter, the Fund fell -2.76% while the index lost -1.46%.

Over the last three months, we saw various benefits of Southeastern’s distinct approach—intelligent, concentrated, engaged, long-term, partnership investing. Among our largest positive contributors, including adidas, Great Eagle, BR Properties, and SoftBank, returns were enhanced by the productive activity of our management partners with whom we have engaged constructively over time. While the cancellation of acquisitions at OCI and CK Hutchison weighed on those stocks, our heavily-aligned management partners pursued the interests of shareholders.

Intelligent, long-term investing also was relevant in the fearful environment that developed following the Brexit vote. In the short-term aftermath, a strengthened dollar detracted from our performance as local returns of our European-domiciled companies held up better than U.S. dollar based returns. Our businesses have small direct exposure to the United Kingdom, but we saw knock on effects from the decision in stocks with ties to weaker European Union countries such as Italy and Spain. Given our time horizon and valuation discipline, we view the U.K. and EU uncertainty as prospective opportunity for both our companies and our portfolio. The strength of our businesses with European exposure should help them weather the eventual changes from Brexit, and our management partners have the skills, incentives, and balance sheets to take advantage of the upheaval. We were prepared with a target list of companies in the unexpected event that Brexit passed, but in the end, few of the quality businesses we targeted became discounted enough. We did initiate one new investment, however, and our target list still could become amply discounted as countries determine how to move forward.

To us intelligent investing is also about holding cash in the absence of qualifying long-term investments. Our cash position benefitted the Fund’s relative results, as did our disciplined focus on business strength which generally keeps us out of financial institutions. The Financials sector was the index’s biggest detractor with the heavily weighted banks suffering, whereas it was the Fund’s largest positive sector because our holdings classified as such consist of less risky holding companies and real estate firms.

In addition to our one new purchase, we added to two of our more discounted stocks, sold three investments, and trimmed several stocks whose prices and portfolio weights had grown.

**Contributors/Detractors**

(+23%;+1.2%), the German-based global sportswear and equipment brand, remained the Fund’s largest contributor as the company reported stronger-than-expected results. Overall revenues rose 22%, operating profits gained 35%, and net income was up 38%. Earnings per share (EPS) grew 50%, helped by buyback activity during the quarter. The company increased its 2016 organic revenue growth outlook to 15% from the previous 10-12% range. During the quarter the company announced it was actively seeking a buyer for its golf segment, including the TaylorMade, Ashworth, and Adams brands. Additionally, two highly qualified investors, one of whom we proposed, joined the company’s board.

Also a positive contributor for the quarter was **Great Eagle** (20%; 1.0%), a Hong Kong real estate company that invests in and manages high quality office, retail, residential and hotel properties around the world. In addition to an over 60% stake in publicly listed Champion REIT, Great Eagle also owns hotels branded under the Langham name, the Eaton hotels in Hong Kong and Shanghai, and Chelsea Hotel in Toronto and trades at a significant discount to intrinsic value. With a strong net cash position, the company announced a 2 Hong Kong Dollar per share special dividend which, combined with the regular dividend, equated to an almost 10% dividend yield. In June, the company announced the sale of its 28 story office building in San Francisco at a 3% net operating income (NOI) cap rate. Our partners, the Lo family, own 60% of the company and bought more stock during the quarter.

Ending the quarter as the Fund’s largest detractor was **M Melco International** (-33%; -2.7%), the Macau casino and hotel operator. Although the company’s $3.2 billion Studio City project (relative to Melco’s market cap of $9 billion) opened in late 2015 and is now generating positive cash flow, construction activity near the property has adversely affected customer traffic flow in the short term. As the construction ends later this year, we anticipate that Studio City’s location and non-gaming attractions will draw more highly profitable mass visitors. Shuttle service to Studio City from other Macau casinos began in June and should boost revenue. In May,
Melco Crown Entertainment, the joint venture that owns Melco International’s Macau properties, purchased $800 million of its shares from James Packer at a steep discount, increasing Melco International’s ownership of Melco Crown to 38% and placing Melco International CEO Lawrence Ho firmly in control of the Macau properties. The stock market value of Melco International’s stake in Melco Crown is worth more than 150% of Melco International’s market cap. Ho again increased his personal stake in Melco International.

OCI (-31%; -1.4%), a global fertilizer and chemical producer, also detracted from second quarter results. The two main pressures over the last three months were weakness in urea commodity prices (a key nitrogen fertilizer) and uncertainty around the CF Industries merger. Despite attractive strategic rationale for the combination of CF and OCI, the increased crackdown on tax inversions in the U.S. made the deal untenable. OCI’s European domicile further pressured the stock in the last week of the quarter, even though the Brexit vote should not impact fertilizer demand and could create some currency translation benefits to OCI. Globally, nitrogen fertilizer demand increased, helping to deplete excess supply. OCI’s plants have an advantage by being located near low-cost natural gas, a primary feedstock in fertilizer. Our investment case incorporates demand for nitrogen fertilizer continuing to grow at a couple of percent annually and supply tightening. Beyond 2016, no major additional plant capacity will be added for at least five years. Despite the current decline in nitrogen fertilizer prices, the company is generating significant free cash flow. CEO Nassef Sawiris and his team are working to grow value per share and are exhibiting a disciplined approach to monetizing assets at prices that reflect longer term intrinsic values.

Among other noted detractors for the quarter was CK Hutchison (-14%; -1.1%), a global conglomerate comprised of five core businesses (retail, telecommunications, infrastructure, ports, and energy). CK Hutchison’s plan for its Three mobile phone network to acquire U.K. telecom company O2 was denied by the European regulator. While CK Hutchison is Hong Kong-based, the stock also fell with the Brexit vote because of fears of the impact on its European and U.K. operations which generated over half of its pre-tax earnings last year. However, Chairman Li Ka-shing and his son, Victor, have demonstrated a compelling long-term record of building businesses, compounding net asset value at double-digit rates, and buying and selling assets at attractive prices, and their history includes intelligent capital allocation during previous market dislocations. We are confident our management partners will continue to grow and unlock value.

**Outlook**

The International Fund sells for an attractive price-to-value ratio in the low-60s%. We own companies whose leaders are building long-term value and pursuing ways to drive prices closer to intrinsic worth. While cash stands at 17%, we believe we will continue to find new qualifiers. Our wish list includes companies with strong underlying businesses that may become overly discounted as the futures of the EU and Great Britain get sorted out, questions continue about China’s growth prospects, and Japan struggles with its economy and currency. Over the long run, we and our fellow shareholders have been rewarded for adhering to our investment discipline, and we believe our distinct, advantaged approach will continue to deliver strong results, especially from this point in a world of uncertainty.

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RISKS

The Longleaf Partners International 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. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. An index cannot be invested in directly.

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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.

Earnings per share (EPS) is the portion of a company’s net income allocated to each share of common stock.

REIT stands for real estate investment trust.

Net operating income (NOI) is a profitability formula that is often used in real estate to measure a commercial property’s profit potential and financial health by calculating the income after operating expenses are deducted.

Dividend yield is a stock’s dividend as a percentage of the stock price.

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

As of June 30, 2016, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: adidas, 4.3%; Great Eagle, 5.9%; SoftBank, 5.3%; OCI, 4.5%; CK Hutchison, 7.0%; Melco, 5.8%; K.Wah, 5.6%; EXOR, 8.5%; Undisclosed, 1.1%. 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.
Longleaf Partners International Fund Commentary

Longleaf Partners International Fund advanced a notable 2.83% in the first quarter, far surpassing the MSCI EAFE Index’s -3.01% decline. A number of our stocks had double-digit gains, including several of our most undervalued businesses coming out of 2015. Most of our companies generated solid operating results, and management activity helped drive higher appraisals. Not only were our absolute returns in line with our absolute goal of inflation plus 10%, but our relative results also benefited from our lack of exposure to health care, which was among the top performing index sectors in 2015 but was among the MSCI EAFE’s worst performing sectors in the quarter.

Stock prices in the first quarter embodied Ben Graham’s description of “Mr. Market,” whose manic short-term swings are driven by investor emotions. The MSCI EAFE fell by -13% at its February 12 low point, but then rallied over 11% by the end of March, a 2440 basis point swing. While broad economic and political uncertainties fostered stock volatility, our appraisals proved much more stable, highlighting the importance of anchoring investment decisions to the long-term cash flows and underlying asset values of each company.

The volatility provided opportunistic points to buy one new business, add to one of our more undervalued companies, sell three holdings, and trim several positive performers as they became overweight and traded closer to our appraisal values. Our on-deck list of new qualifiers was more robust in Asia than elsewhere which is reflected in our 45% portfolio exposure in the region.

Contributors/Detractors
(gross return of the stock for 1Q; impact to Fund return for 1Q)

**adidas** (+20%; +1.8%), the German-based global sportswear and equipment brand, reported better-than-expected earnings, with 16% revenue growth for the core brand, and increased its 2016 expectations to 10-12% organic revenue growth. We have been engaged in productive conversations with adidas over the last year and were pleased with several governance announcements. Kasper Rorsted was named the successor to CEO Herbert Hainer. Rorsted had a strong record at Henkel AG, and we believe he will successfully address costs and increase adidas margins, which are at half the level of key competitors. The company also nominated shareholders Nassef Sawiris and Ian Gallienne to join the Supervisory Board. After the stock’s strong 12-month performance, we trimmed our overweight position, but the company remains discounted relative to both our appraisal and its peers.

**Genting Berhad** (+97%; +1.3%), the Malaysian holding company with gaming, property, plantation, pharmaceutical, and oil and gas assets, benefited from progress at several businesses and a rebound of the Malaysian ringgit. There was news of a potential initial public offering of Alzheimer’s drug maker TauRx Pharmaceuticals, which is 20.7% owned by Genting. The Singapore casino business steadied, with the core mass gaming and non-gaming business revenues expected to grow. The duopoly position in the stable Singapore jurisdiction represents a significant competitive advantage. Genting Singapore also began construction on its Jeju project in Korea, which offers potential upside for our appraisal and the stock. Despite the strong quarter, Genting trades at a significant discount to the sum of its parts, but we did trim our stake to reduce the overweight.

**Mineral Resources** (+61%; +1.2%), the Australian-based mining services company, surprised the investment community with stable operating results in its crushing business and lower mining costs. Additionally, higher iron ore prices and a stronger Australian dollar were favorable for the stock. Although ore prices did not benefit Mineral Resources’ crushing and processing business since the company is paid a fixed fee per ton, they did help the mining operation produce higher earnings before interest, taxes, depreciation and amortization (EBITDA) per ton. Management indicated the company is unlikely to move forward with the ambitious elevated transport system without a more attractive long-term iron ore pricing environment. The company began to buy back shares, and founder and managing director, Chris Ellison, purchased more shares personally. We trimmed our position.

**EXOR** (-21%; -2.3%), the Italian holding company, detracted from the Fund’s results as its share price closely correlated with underlying holding Fiat Chrysler Auto (FCA) despite FCA comprising less than half of our total EXOR appraisal. Most auto stocks declined with concerns about peak demand, easy credit, and the longer term implications of driverless cars. Additionally, the Volkswagen emission test scandal weighed on European car makers. These current industry challenges are likely to delay CEO Sergio Marchionne’s pursuit of a merger for FCA. Additionally, the broader Italian market had...
the worst performance in Europe, which impacted EXOR's share price despite the value overwhelmingly coming from outside of Italy. EXOR completed its acquisition of Bermuda reinsurer PartnerRe in the quarter, providing another outlet for Chairman and CEO John Elkann to build value. We believe there are ample strategic and value building levers still to be pulled at EXOR and see the current price weakness as unjustified.

OCI (-21%; -1.2%), a global fertilizer and chemical producer, fell early in the quarter in line with a decline in the underlying urea commodity price, which recovered somewhat by quarter-end. Global excess supply should diminish as nitrogen fertilizer demand grows approximately 2% per year while no additional plant capacity is scheduled for at least five years out. Uncertainty around OCI's planned sale of its U.S. and European assets to CF Industries also weighed on the stock. A major hurdle to the deal was removed in mid-March, when OCI announced that Consolidated Energy Limited would jointly invest in the methanol plant, Natgasoline, which would fall outside of the scope of the assets going to CF. OCI is trading at a steep discount to our appraisal and even more cheaply assuming the CF deal closes in the second quarter of 2016 as planned.

Portfolio changes
We sold three companies in the quarter and initiated a small position in nitrogen fertilizer manufacturer and distributor CF Industries, which offered a more discounted way to increase our stake in OCI post deal. CF CEO Tony Will is buying back discounted shares, and OCI CEO Nassef Sawiris will be the largest CF shareholder and join the board when the deal closes.

We sold Australian-based testing, inspection, and certification company ALS Limited at a loss after owning it for just over a year. The company announced a rights issue, which we thought was unnecessary, at a steep discount to market price. This decreased both our appraisal and confidence in management’s capital allocation skill.

We exited our small position in British power systems company Rolls-Royce after its price rallied in the first half of the quarter. The business has long-term upside, but the thesis will take longer to play out than we originally expected. We invested our proceeds in higher return opportunities.

We completed the sale of Orascom Construction, which OCI spun out in 2015.

Outlook
We believe the strong absolute and relative returns we posted in the first quarter should be indicative of our expectations going forward. Many of our top performers rallied from unsustainably low levels to a more normal discount range and have substantial additional upside. The portfolio price-to-value (P/V) in the low-60s% offers an attractive buffer between our conservative appraisals and our companies' underlying stock prices, especially in a market where we are finding limited new opportunities. Volatility could increase in Europe, coupled with increasing political risks from the migrant crisis and terrorism, as well as Britain's potential exit from the Eurozone. Asia remains more undervalued, given persistent uncertainty over China's future growth rate and additional currency weakness. The Fund’s 7% cash level should enable us to take advantage of the next opportunity wherever it emerges. At many of the companies we own, management teams are pursuing operational improvements as well as strategic alternatives that can build material value.

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

A basis point is one hundredth of one percent (0.01%).

As of March 31, 2016, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: adidas, 6.2%; Genting Berhad, 1.8%; Mineral Resources, 1.9%; EXOR, 7.8%; OCI, 4.3%; CF Industries, 0.6%; ALS, 0.0%; Rolls-Royce, 0.0%; Orascom, 0.0%. 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.

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Positive performance at a number of holdings was overshadowed by double-digit declines in our companies with the highest exposure to emerging markets (EMs). While we have limited direct investments in companies based in emerging markets, top line exposure to these regions impacted several of our businesses. Look-through emerging market revenue is over 40%. Chinese economic fears, amplified by the collapse in the China A-share market and renminbi devaluation in the second half, broadly impacted our companies with direct or indirect exposure. EM currency weakness relative to the strong U.S. dollar (USD) exacerbated results, as currency translation into USD turned an otherwise positive portfolio return for the year negative. Swiss-based LafargeHolcim, which suffered as its emerging markets revenues were translated into stronger Swiss francs, was the largest detractor in the year, as the stock’s translation into USD further hurt returns. Returns at Malaysian-based gaming and energy company Genting Berhad and our two Australian businesses that service the natural resources sector were also worsened by the ringgit’s and Australian dollar’s decline. BR Properties appreciated in local currency, but the weak Brazilian real made the company a substantial detractor in USD. Despite a strong rebound across our Macau gaming companies in the fourth quarter, Melco International remained a top detractor for the year. While we believe these portfolio exposures offer more substantial discounts and greater potential upside than the index, the negative performance masked the positive progress across the majority of our businesses in the year. Weak currencies and stocks that are substantially discounted can change direction quickly, and we believe these investments will ultimately provide solid returns.

As mentioned above, Macau casino and hotel operator Melco gained 22% in the fourth quarter but remained among the Fund’s largest detractors for the year, down 31%. The stock benefited from improved sentiment regarding Macau during the quarter among indications that the higher margin mass market is stabilizing. In addition to relaxation of transit visa, the Macau government softened its stance on the smoking ban on the gaming floors. While Beijing will continue its anti-corruption campaign (which has hurt VIP business in Macau), the mass-focused infrastructure spending (high speed trains, ferry terminal, bridge from the HK airport, light rail) continues unabated. More than 90% of Melco Crown’s earnings before interest, taxes, depreciation and amortization (EBITDA) comes from mass business, where margins are 4X that of VIP business. Melco Crown opened its new mass-focused casino Studio City in late October, which helped increase market share in the all-important mass segment. This $3.2 billion project (relative to Melco’s market cap of $9 billion) has just started generating cash flow. We expect Studio City to receive an additional 50 table allocation in early 2016 in addition to its initial 200 table allocation. With a strong balance sheet, increasing EBITDA, and declining capital expenditure profile, the company is well positioned to buy back shares or buy out minority owners of Studio City. Melco International CEO, Lawrence Ho, bought about $25 million worth of shares in the fourth quarter.

After announcing another strong quarter of double-digit organic growth for its core adidas brand, German-based global sportswear and equipment brand adidas returned 22% in the quarter and 43% for the full year. The brand’s strong positions in Europe, China, and Latin America drove growth. The company expects 2016 operating income margins to meet or exceed 2015 levels and overall sales to increase at high, single-digit rates in the next year. Despite the stock’s strong performance, we believe adidas remains discounted due to strong value growth and has significant additional upside. As discussed in previous quarters, we have had constructive engagement with management and the supervisory board and have seen many positive developments. In addition to authorizing a 10% share repurchase program, the company made managerial changes in the U.S. business, sold its non-core Rockport brand at a price above our appraisal value, and announced it is exploring strategic options for its golfing brands and hockey division.

Baidu was added to the portfolio in the second half during the China market panic, and the strong fourth quarter rebound, up 38%, resulted in the stock also being one of the strongest contributors for 2015. Baidu is the dominant internet search
provider in China with 71% market share of PC and mobile search page view and revenue share over 80%. Its online search business grows at 30% per year with 50% operating margins and sells at a single-digit FCF (free cash flow) multiple. The company only focuses on Chinese language search, mastering the subtleties of its domestic market. During the fourth quarter, in the large and fast-growing online travel space, Baidu swapped its 45% stake in Qunar for a 25% stake in Ctrip. Together with Ctrip’s 37.6% stake in eLong, Ctrip will control 80% of online domestic travel booking revenues, which should lead to more rational competition and improved economics. Through this transaction, Baidu vastly improved its position to become the largest o2o (online to offline) travel platform in China. Furthermore, Baidu will de-consolidate loss making Qunar and provide more clarity to the underlying economics of the core search business. Separately, Alibaba’s offer to privatize online video company Youku Tudou during the quarter helped validate the conservatism in our appraisal of Baidu’s 80% stake in online video business iQiyi.

Colt Group, the British-based provider of business communications and information technology solutions to companies primarily in Europe, was up 40% for the year, making it among the Fund’s largest contributors. We sold the position when the company was acquired by Fidelity Investments in the third quarter. Our investment in Colt, beginning in the second quarter of 2014, produced a 27% annualized return for the International Fund.

Another top performer, CK Hutchison, a conglomerate comprised of the non-real estate businesses from the June merger between Cheung Kong and its subsidiary, Hutchison Whampoa, returned 22% during 2015 when combined with Cheung Kong Property. The corporate transaction helped remove holding company discounts and clarify business line exposures by splitting the property business (Cheung Kong Property Holdings) from the non-property business (CK Hutchison Holdings). The transaction is likely to be viewed as a seminal event leading to improved governance and structure for other complex conglomerates in Asia. In the fourth quarter, Cheung Kong Property was a modest detractor, down 10%, as poor sentiment towards real estate and China lowered real estate prices in Hong Kong. Hong Kong property stocks remained sharply discounted versus the physical property market. Cheung Kong, among the largest property companies in China and Hong Kong, has a large, low cost land bank in China and a strong balance sheet, positioning the company to exploit short-term market disruptions for the benefit of long-term investors. Chairman Li Ka-shing and his son, Victor Li, have demonstrated a track record of building businesses, compounding NAV at double-digit rates, and buying and selling assets at compelling values.

Also contributing to performance, Italian holding company EXOR appreciated 5% in the quarter, taking full year returns to 12%. Over the course of the year, Chairman and CEO John Elkann, together with Fiat Chrysler Auto (FCA) CEO Sergio Marchionne, took numerous steps to drive value growth. The company sold or spun assets at a strong price, including an $893 million initial public offering (IPO) of Ferrari—well above expected value, the sale of Cushman and Wakefield to DTX for $2 billion—a more than 30% premium to our carrying value for the business, and the recently announced sale of its 17% stake in Banijay for €60.1 million—a €25 million premium to book value. Management reinvested proceeds into high quality assets at a fair price. In the second half, EXOR announced the acquisition of Bermuda reinsurer PartnerRe to be completed in the first quarter of 2016 and increased its long-held stake in The Economist. At FCA, Sergio Marchionne publicly called for auto industry consolidation, potentially positioning EXOR for discussions to merge FCA with another key player.

Among detractors to the Fund’s performance, ALS declined 12% in the quarter, taking full year returns to -34%, after announcing a rights issue at a discount to the market price. Given the balance sheet strength and expected earnings growth in the next two years, we believe the rights issue was unnecessary, and it negatively impacted our appraisal. Despite management’s poor capital decision, the competitively entrenched Life Science business remains attractive.

Our position in the convertible bonds of CEMEX declined 12% in the quarter and 21% since we bought the position in the third quarter. The price declined due to weak Latin American currencies, challenged trends in some emerging markets, and a general sell-off across the entire non-investment grade bond sector. We believe CEMEX’s assets are worth roughly twice the debt, which provides generous asset coverage. In addition, we receive a yield component and the opportunity of longer-term upside over par value through the convertible feature as EBITDA growth and debt reduction drive the underlying equity value higher.

Global cement, aggregates, and ready-mix concrete producer LafargeHolcim declined 2% in the quarter and over the year. During the quarter, CEO Eric Olsen presented his three year operating plan with an intense focus on free cash flow generation, internal growth, and returning cash to shareholders. The plan should enable debt to return to investment grade and a dividend payout ratio near 50%. With only modest volume and pricing assumptions, combined with realizing synergies from the LafargeHolcim merger, we believe the plan is achievable. We are excited to own a company with a collection of geographically advantaged assets at less than approximately 8x normalized FCF earnings power and strong cash generation that should be allocated to maximize value per share.

Genting Berhad was one of the largest detractors for the year, declining 53%. Malaysia macro/FX was a big headwind, and the company’s development of its sizable oil and gas assets is likely to be delayed given the weakness in energy prices. The company’s Singapore duopoly casino, publicly listed Genting Singapore, is led by CEO Hee Teck Tan and was down after reporting four quarters of unusually poor hold (2.0%–2.5%) in its gaming business, as well as some equity investment write-downs. Since opening the casino, the cumulative win rate at Genting Singapore has been close to the theoretical average of 2.85%, and we believe win rates should normalize over time. In the quarter we added Genting Singapore in addition to our
Genting Berhad position. The stock’s deep discount was largely due to a slowdown in Chinese VIP visitors as a result of the Chinese anti-corruption campaign. Genting’s core mass market business has been steady and more than justifies our appraisal. The duopoly position in the stable Singapore jurisdiction represents a significant sustainable competitive advantage. The simple P/E multiple misses the sizable cash and investment portfolio on the balance sheet and minimal maintenance capex requirement (capex is much lower than depreciation). The company engaged in a value-accractive share buyback in recent months.

Mineral Resources returned -51% during 2015 driven largely by the collapse of iron ore prices. The crushing services business maintained steady volumes and strong margins but was not enough to appease market concerns of continued iron ore price declines. The company surprised the market with its ability to reduce costs in the iron ore mining business at a pace that maintained positive cash flow margins. During the fourth quarter, the company announced a A$30 million stock buyback, (4% of outstanding shares), higher EBITDA guidance, and a new EPC (engineering, procurement, and construction) contract for a crushing plant for Rio Tinto’s Nammuldi mine. The company continued to take costs out of its mining operations to ensure that every ton of iron ore produced is sold at positive cash flow margins.

Over the year, we took advantage of increased market volatility to upgrade the portfolio. We sold four positive performers that reached our appraisals in the first nine months. In the fourth quarter, we sold our small stake in DSM to fund more discounted positions. New purchases were more heavily weighted to Asia, which provided more discounted investments, but we also found interesting company-specific opportunities in Europe. In addition to Genting Singapore mentioned above, we bought British power systems company Rolls-Royce.

Although 2015 performance was disappointing, we believe the International Fund is well positioned for a strong rebound. The broader currency pressures as well as EM weakness that impacted results could reverse course quickly. Additionally, the Fund’s price-to-value (P/V) ratio is in the low-60s%. The four largest detractors are highly discounted selling below 57% of value, and the four largest positions, which were among top contributors for the year, remain discounted with solid value growth prospects. Beyond these discounts, the high quality of our businesses and the caliber of our management partners, who are pursuing available avenues to drive value recognition, make us confident in future results. We appreciate your continued partnership. We are confident that the Fund should reward your patience and ours with strong future performance.

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Price / Earnings (P/E) is the ratio of a company’s share price compared to its earnings per share.

Capital Expenditure (capex) is the amount spent to acquire or upgrade productive assets in order to increase the capacity or efficiency of a company for more than one accounting period.

Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management, and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested.

As of December 31, 2015, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: LafargeHolcim, 6.9%; Genting Berhad, 0.6% (5.3% adjusted for close of warrants and purchase of underlying stock); ALS, 3.0%; Mineral Resources, 1.6%; BR Properties, 3.3%; Melco, 8.0%; adidas, 8.1%; Baidu, 4.9%; CK Hutchison, 7.4%; EXOR, 9.1%; CEMEX, 4.7%; Genting Singapore, 2.0%; Rolls-Royce, 2.6%. 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.

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China economic fears broadly impacted our companies with direct or indirect exposure. The slowing Chinese economy, collapse in the China A-share market, and an unexpected Renminbi devaluation created a ripple effect of angst across countries with economic ties to China, including many emerging markets (EM), where local stocks were down but currencies also suffered. LafargeHolcim, one of the highest quality names we have ever owned with large economic emerging markets exposure, suffered for that exposure as its EM revenues were translated into strong Swiss francs. Our Macau gaming companies stock declined with pressure of lower revenue comparisons and a variety of other negative news. Our Hong Kong based companies declined as well, in part because they became a source of liquidity for investors unable to sell their China-A shares. Our two Australian holdings, which have businesses that serve mining and natural resources, were meaningful detractors as their stocks declined in the Australian market, and the currency translation into USD further hurt returns. BR Properties appreciated in Brazil, but the weak Real hurt performance in USD. Likewise, Genting Berhad suffered as a proxy for Malaysian economic weakness and even more due to, the ringgit’s decline. In total, the currency translation impact from our holdings in these three countries cost our performance close to 2%.

Despite our frustration over recent returns, the China related stock price volatility among our businesses was not indicative of a decline in the long-term positive fundamentals that we believe will be reflected in our companies’ prices. Following previous periods when broad macro pressures weighed heavily on our absolute returns, we posted strong returns when macro fears subsided. At each of the low points, our portfolios had similar characteristics to today including price-to-values (P/V) below 65%, an expansive on-deck list, and solid value growth prospects. Our concentrated, bottom-up approach has historically produced strong, long-term results. The total expense ratio for the Longleaf Partners International Fund is 1.25%. The Funds’ expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.

As the largest contributor, German-based global sportswear and equipment brand adidas returned 5% after reporting a strong quarter of organic growth for its core adidas brand. This growth is being driven by adidas’ incredibly strong positions in Europe, China, and Latin America. We have had ongoing constructive engagement with management and believe the managerial changes in the U.S. business will lead to the brand regaining market share there over time. The company has spent €750 million repurchasing nearly 5% of shares this year and is authorized to repurchase another €750 million over the coming year. After selling its non-core Rockport brand at a price above our appraisal value earlier this year, adidas recently announced that it is exploring strategic options for its golfing brands, including TaylorMade.

After announcing board and shareholder approval of a planned merger with Brazilian offshore shipping company ASGAARD, Brazilian iron ore company Manabi appreciated 7%. As part of the merger, approximately 60% of the Manabi value will be distributed to shareholders as cash, while the remaining portion will be held as common stock in the newly formed company, with a simplified shareholder structure potentially allowing for greater liquidity in the future.

During the quarter, all conditions of the merger between cement makers Lafarge and Holcim were met, and the transaction was completed. Eric Olsen now serves as CEO of LafargeHolcim, and Wolfgang Reitzle and Bruno Lafont serve as Co-Chairmen of the Board. The stock price of the newly combined entity declined 25% in the quarter due mainly to volume and currency weakness in its emerging market and Europe. North America was strong. Olsen called out Indonesia, India, Brazil, and Egypt as markets where targeted cost reduction programs will commence as well as sixteen markets where pricing, along with lower costs, will be a focus. Management has set a total synergy goal of €1.2 billion to be realized over the next three years for the newly combined entity. Each geographic region will have accountability to margin of safety between the stock price and corporate worth to deliver attractive returns from this point.

September 30, 2015

Longleaf Partners International Fund Commentary

Longleaf Partners International Fund declined 13.62% in the third quarter and 11.30% for the year-to-date (YTD). The Fund underperformed the MSCI EAFE Index’s declines of 10.24% for the quarter and 5.28% YTD. Over the life of the Fund, it has outperformed the index.
meet the cost saving targets. Additionally, management has signaled that the company is open to further non-strategic asset divestitures if selling can create the most value for shareholders.

K. Wah International, a Hong Kong real estate company and 3.8% owner of Macau casino company Galaxy, was down 23%, largely due to Galaxy’s weakness and market volatility in China’s domestic stock market. The sharp China A-share correction and subsequent government intervention measures left Hong Kong listed stocks as a primary source of liquidity. K.Wah’s real estate transactions are on a record pace with 2015 volumes projected to be four times as high as 2014. Operationally, K. Wah delivered strong results, and there was also strong insider buying at the company.

The news flow out of Macau continued to be negative in the quarter, impacting Melco International’s price, which was down 21%. Headlines about junkets and arrests continued to depress global sentiment about Macau, yet almost exclusively relate to the VIP business, not the mass business which should almost entirely drive Macau’s long-term economic future. Melco Crown’s mass volumes, which represent over 90% of EBITDA, remained solid. The new $3.2 billion Studio City casino is on track to open in late October. Negative sentiment and broader economic concerns in China are allowing us to own this competitively entrenched, long-term growth business at very attractive free cash flow (FCF) multiples.

Another top detractor, Mineral Resources declined -43% despite a recovery in iron ore prices—particularly as measured in Australian dollars—and greater-than-expected fiscal year 2015 results. The crushing services business maintained steady volumes and strong margins and happily surprised by reducing costs in the iron ore mining segment at a pace that maintained positive cash flow margins. The stock price does not reflect company fundamentals, and Mineral Resources has a strong history of building value during down cycles.

Australian-based testing, inspection, and certification company ALS Limited also declined in the third quarter, by 27%. After a strong first half, ALS’s share price was punished by AUD weakness and pressure on natural resource prices. ALS’s Minerals business provides services to miners but has minimal direct exposure to iron ore. The majority of the company’s value lies in its competitively entrenched and growing Life Services and other non-commodity related businesses which remain strong. CEO and Chairman Greg Kilmister is making progress in effectively managing costs.

During the quarter, we added four new positions in the Fund, including one in CEMEX convertible bonds. CEMEX is one of the global leaders in the building materials industry, manufacturing and distributing cement, ready-mix concrete, and aggregates in more than 50 countries. We have owned the company in the past, and the converts became attractive again on weakness in emerging markets. Buying the converts versus straight equity allows for an advantageous risk/reward scenario. We believe risk is limited given that asset values at CEMEX more than cover outstanding company debts, as validated by comparable transactions. Upside will be dictated by the company’s value growth going forward as it capitalizes on primary end market exposure to both Mexico’s infrastructure spending and continued growth in the U.S.

We also bought Sika, a Swiss provider of specialty materials and services for the construction industry. Sika is an innovative leader in its industry with global scale and a strong reputation for trustworthiness. In his five years as CEO, Jan Jenisch has improved returns on invested capital, enhanced operating margins, and reinvested back into the business for future growth. Prior to our investment, the founding family made an agreement to sell its 16% stake to Saint-Gobain at an 80% premium without a concurrent offer to others shareholders. We have taken a public stand that all owners should be treated equally, but whether or not the deal proceeds in its current form, we believe Sika is a most compelling investment.

Another new investment in the Fund, Baidu is the dominant internet search provider in China with over 70% market share in search page views and 80% of revenues. Baidu’s dominance strengthened after Google exited China in 2010. Baidu only focuses on Chinese language search, mastering the subtleties of that market. The recent panic in China’s stock market offered a window for us to pay a single-digit FCF multiple for Baidu search, which is growing at 30% per year with 50% operating margins. The company took advantage of weakness in the stock price and initiated a $1 billion stock buyback.

Lastly, we purchased Irish drinks company C&C for the second time. CEO Stephen Glancey and CFO Kenny Neison have been shareholder-oriented management partners who navigated the company through a challenging economic environment in the core markets of the U.K. and Ireland. We are pleased to have the opportunity to own this market leader with top notch cider and beer brands.

We exited two positions in the Fund during the third quarter. Colt Group, a British company that provides business communications and information technology solutions to companies primarily in Europe, was acquired by Fidelity Investments in the quarter. Our investment in Colt beginning in the second quarter of 2014 produced a 27% annualized return for the International Fund.

We sold one of our most fully valued companies, Christian Dior, to fund more deeply discounted new positions. French luxury goods business and holding company for LVMH Moët Hennessy Louis Vuitton (LVMH), Christian Dior added 17% since we initiated the position in the first quarter of last year. Owner-operator Bernard Arnault drove the strong outcome by distributing LVMH’s shares in Hermès to Christian Dior shareholders and focusing on improving results in its core LVMH business. The investment approached its appraisal value more quickly than our average five year holding period, driven by value accretive capital action by its management team.

The Fund has two categories of companies that we see driving returns. Approximately 60% of the portfolio is a collection of what we feel are industry leading businesses that have the...
competitive strength and management leadership to compound value per share at a potentially high rate. Based on our appraisals, as a group this category of holdings sells for below 65 cents on the dollar and, on average, less than 12X after-tax free cash flow (real cash P/E). Prospects for these holdings' value growth, especially as a diversified basket, are greatly enhanced due to their combinations of pricing power and gross profit royalty status. Their managements' track records and ownership alignment suggest strongly that these steadily growing FCF streams should be reinvested to build even more corporate value.

In our opinion, among the holdings in this group are the most value-generating holding company in the world since the Global Financial Crisis in EXOR (thanks to its leaders Sergio Marchionne and John Elkann), one of the world's two best sports brands in adidas, the most dominant worldwide cement oligopolist in LafargeHolcim, the highest-quality global conglomerate in CK Hutchison, the world's most compelling real estate company in Cheung Kong Property, and China's best internet search engine in Baidu. These companies are among those that offer a combination of competitive advantages, balance sheet strength, and glaring undervaluation that gets lost in the focus on the pressures that have hurt recent results. As the largest portion of the portfolio, however, it is this group of holdings that we look to as the primary long-term driver of potential future outperformance.

The second category of holdings includes companies being led through transitions by strong management partners who are focused on growing and unlocking values by highlighting their competitive business segments and/or reinvesting substantial cash in high-return opportunities. OCI is merging most of its assets into CF Industries; Philips is heading toward becoming a leading healthcare company; ALS Limited owns a highly valuable life sciences business temporarily obscured by a depressed energy segment; BR Properties is basically liquidating, having sold or contracted to sell more than half its assets; Great Eagle holds net cash and securities totaling more than its stock price in addition to many hotels and other valuable properties; DSM is far down the road in slimming itself into a purer-play nutritionals company; and Vivendi holds the world's largest music company, dominant French media assets, and significant cash to deploy. This group comprises almost 40% of the portfolio and we feel should drive performance when the gap between price and value closes as our management partners lead these transitions.

Not only do these two categories of companies create the possibility of future outperformance, but within the groups, the specific stocks that hurt most this quarter are compelling longer term in part because of the same factors that drove down recent results. Broadly speaking, management teams in Hong Kong and Singapore are buying back undervalued shares at record rates in response to the recent steep price declines. Many of our partners also are making large insider purchases. More specifically, Macau will prosper long-term based on its mass gaming appeal, regardless of all the well-chronicled issues around higher profile but far lower margin VIP gaming. Our Australian businesses offer large growth and competitive advantage having nothing to do with iron ore or energy prices, even though those drove their stocks this quarter. Emerging markets' long-term population and economic growth make cement critical to these areas over time with LafargeHolcim as a beneficiary. Our Hong Kong stocks had short-term correlations with the Chinese and Hong Kong markets, but their business segments and geographies are far better diversified than recent high correlations imply.

Although we cannot predict short-term prices, we believe the International Fund has reached an attractive level for long-term investors to add capital. The Fund's P/V ratio is in the high-50s%, and the sharp uptick in global market volatility, which has now reached its highest level since 2011, has been a precursor to strong Fund returns in the past. While a useful data point, the historic performance is not the basis for our confidence in returns going forward. The competitiveness of our businesses our extremely capable management partners, and the attractive margin of safety in our companies’ stock prices makes us highly confident that the companies we own can perform well and reward your patience and ours.

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.

MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

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

**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.

**Price / Earnings (P/E)** is the ratio of a company’s share price compared to its earnings per share.

Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management, and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested.

As of September 30, 2015, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: EXOR, 8.4%; adidas, 8.3%; LafargeHolcim, 6.9%; CK Hutchison, 6.9%; Melco International, 6.3%; K. Wah, 5.7%; OCI, 5.4%; Cheung Kong Property, 5.1%; CEMEX, 5.0%; Philips, 4.9%; ALS, 4.7%; BR Properties, 4.3%; Great Eagle, 3.6%; Baidu, 3.6%; Sika, 3.2%; Genting Berhad, 2.9%; Mineral Resources, 2.1%; DSM, 2.0%; C&C, 1.7%; Manabi, 1.3%. 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._
Longleaf Partners International Fund gained 3.13% in the second quarter, outpacing the MSCI EAFE Index’s return of 0.62%. Year-to-date the Fund returned 2.68% and trailed the index’s 5.53% return. Over the last 15 years, the International Fund’s cumulative returns have more than doubled the index.

In the second quarter, the majority of our businesses made positive progress, as our management partners took smart actions to drive long-term value growth. Double-digit returns at top performers Colt and CK Hutchison (formerly Cheung Kong) demonstrated how quickly share prices can respond to productive corporate activity. Although most of our investments were positive performers in the quarter, much of our partners’ value-building effort at the businesses we own is not being fully reflected in the Fund’s returns. Our Asian gaming-related companies remained the top absolute and relative detractor, faced with the Chinese government’s anti-corruption crackdown.

Colt Group, the British based company that provides business communications and information technology solutions to companies primarily in Europe, was the fund’s biggest contributor in the quarter. The stock gained 49% with Fidelity’s offer to buy roughly 37% of shares outstanding it does not already own. We invested in Colt in the second quarter of 2014, and the offer price represents a 35% premium to our average cost.

Also a large contributor to the fund’s performance in the quarter, CK Hutchison, merged with its 50% owned subsidiary, Hutchison Whampoa, and spun off their combined real estate businesses into Cheung Kong Property. With the stock’s move from HK$125 prior to the restructuring announcement in January to HK$196 for the combined pieces after the spin in June, this corporate restructuring succeeded in reducing two persistent discounts the market applied to CK Hutchison. First, the complexity of the corporate structure and diversified set of businesses within two layers of holding companies made valuing the company difficult. Second, market concerns related to property exposure in Hong Kong and China has weighed heavily on the stock. CK Hutchison was the largest constituent of the Hang Seng Property Index, yet many property investors could not own the stock given its significant non-property businesses. The restructuring creates a pure play property company – Cheung Kong Property – and moves CK Hutchison from the Hang Seng Property Index to the Hang Seng Conglomerates Index.

Australian-based testing, inspection, and certification company ALS Limited gained 19% in the quarter. We bought ALS late last year, when the company become overly discounted, as iron ore prices declined 49% in 2014. Its minerals business provides services to miners, but ALS has minimal direct exposure to iron ore. The majority of the company’s value lies in its competitively entrenched and growing life sciences and other non-commodity related businesses. In the recent quarter, life sciences reported revenues above expectations and further expansion of its South American business. The minerals and energy segments maintained healthy double-digit operating margins, despite revenue declines, highlighting impressive cost flexibility in the hands of disciplined CEO and Chairman Greg Kilmister.

Several stocks detracted from performance in the quarter. Genting Berhad, the Malaysian holding company with gaming, property, plantation, and oil and gas assets, fell 12% during the quarter with weak demand in the Singapore casino duopoly. While China’s anti-corruption campaign has caused VIP investors to avoid Macau and frequent other regional destinations, Singapore’s rules preventing junket participation has muted demand growth in that jurisdiction. Analyst coverage of Genting largely focuses on the gaming business. We believe the company’s limited disclosure on its oil and gas assets has led to significant undervaluation. Genting recently announced that its Indonesian Kasuri block, which is adjacent a BP liquefied natural gas facility, has proven oil and gas reserves.
Also negatively impacting the Fund’s second quarter results, BR Properties, Brazil’s largest commercial office real estate investment company, was down 16%. A strengthening U.S. dollar coupled with political uncertainty after last year’s election and overall economic decline in Brazil hurt BR Properties’ performance this year. In the second quarter, Brazil’s central bank raised interest rates again to 13.75%, the highest level since 2009. In the first quarter, BTG Pactual filed an initial takeover offer at a price below our appraisal. In early July, subsequent to quarter-end, BTG withdrew its offer following much shareholder resistance, including our own, to the low price. BR Properties has a strong balance sheet, a high quality office portfolio in prime locations, and blue chip tenants with high switching costs to exit leases. Although same-store rents rose year-over-year, they are flat-to-marginal down when adjusting for inflation. Financial vacancy rates are up year-to-date, but down over twelve months. CEO Claudio Bruni and his team historically have sold assets at good prices and returned cash to shareholders in the form of dividends and buybacks.

With continued pressure on the Macau gaming industry, Melco International declined. We see early signs of revenue stabilization. In spite of industry challenges, Melco gained market share during the recently reported quarter and was quicker than peers in reducing costs. The new, mass market-oriented Studio City casino is on track to open by October and advances the government’s efforts to broaden tourism beyond gaming. CEO Lawrence Ho is a large owner and is building value by buying back deeply discounted shares, investing in high-return projects to increase visitor traffic, further shifting their mix towards higher margin mass and premium mass business, diversifying into non-gaming revenue sources that the government supports, refinancing debt at attractive rates, securing long-term credit lines to increase financial flexibility, and exploring ways to maximize returns on a limited supply of baccarat tables. We believe growth in the higher margin mass market will drive a bright future for Macau gaming and Melco. New casinos with diverse non-gaming attractions and much-needed hotel room supply, as well as ongoing government investments in infrastructure, will facilitate more mass visitors. The reversal of the transit visa restriction announced on June 30 is the first sign of supportive regulatory policy to improve economic conditions in Macau. This should be positive for VIP and premium mass volumes.

During the quarter, we bought no new positions in the fund. We sold our successful investment in Orkla, the Norwegian consumer goods company, as price reached our appraisal. Orkla Chairman Stein Erik Hagen has been a fantastic partner, growing value by monetizing assets at attractive prices and focusing the company on its core branded consumer goods business.

We believe the International Fund is well positioned for strong absolute and relative performance. The price-to-value ratio (P/V) is in the high-60s%. Many international markets are priced with little margin of safety, with global mergers, acquisitions, initial public offerings (IPOs) near 2007 peak levels and at multiples well above our appraisals. We remain focused on owning discounted, strong businesses that can generate organic value growth and that have good managements who are pursuing opportunities to build and monetize value per share. We are engaged to varying degrees with our management partners and believe their near-term steps to close the gap in price will reward us.

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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.

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Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management, and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested.

As of June 30, 2015, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: CK Hutchison, 6.2%; CK Property, 3.7%; Colt Group, 6.7%; ALS, 4.2%; Genting Berhad, 3.0%; BR Properties, 4.0%; Melco International 6.4%. 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.
International Fund Management Discussion

Longleaf Partners International Fund declined 0.43% in the first quarter, underperforming the MSCI EAFE Index, which added 4.88%. The Fund’s disappointing results over the last year have negatively impacted our longer term absolute and relative performance. Large swings in returns are not unusual in our concentrated portfolio, and past positive performance bursts account for our strong 15-year and since inception cumulative results, which are more than double the index.

Cumulative Returns at March 31, 2015

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>1Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>232.63%</td>
<td>140.33%</td>
<td>32.37%</td>
<td>17.06%</td>
<td>-17.61%</td>
<td>-0.43%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>112.04</td>
<td>53.00</td>
<td>62.09</td>
<td>34.84</td>
<td>-0.92</td>
<td>4.88</td>
</tr>
</tbody>
</table>

Average Annual Returns at March 31, 2015

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>7.59%</td>
<td>6.02%</td>
<td>2.84%</td>
<td>3.20%</td>
<td>-17.61%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>4.69</td>
<td>2.88</td>
<td>4.95</td>
<td>6.16</td>
<td>-0.92</td>
</tr>
</tbody>
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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.

The total expense ratio for the International Fund is 1.25%. The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.

In the first three months of 2015, our businesses had solid operating performance, coupled with value-accretive actions taken by our management partners. The majority of names were positive performers, with double-digit returns at many. Despite positive progress across the portfolio, the persistence of three broad headwinds – U.S. dollar strength, the Chinese government anti-corruption crackdown, and a supply/demand imbalance in iron ore – weighed on returns. Priced in local currencies, the Fund rose 7%, but the translation into U.S. dollars wiped away all the gains and had the largest negative impact on performance. Our Asian gaming holdings continued to suffer as revenues further declined. Additionally, iron ore prices fell another 17% and pressured our two mining related stocks.

The Fund’s largest positive contributor, CK Hutchison (formerly Cheung Kong), announced its intention to merge with subsidiary Hutchison Whampoa and spin out the combined property company. This latest savvy move by founder and CEO Li Ka-shing should lessen the holding company discount on the stock as underlying business exposures are clarified and the spin off highlights the value of the combined property business. The stock gained 22% during the quarter. An independent valuer recently appraised CK Hutchison’s property business 48% higher than stated book.(1) The company’s high profile dramatic restructuring of a blue chip Asia conglomerate has the potential to unleash similar restructurings in the region. Italian holding company EXOR appreciated 10% in the quarter.

In the quarter we purchased three new positions based in Japan, Hong Kong, and the Netherlands. Additionally, after EXOR’s underlying holding Fiat Chrysler Automobiles (FCA) announced plans to spin out the Ferrari brand late last year, in the first quarter FCA CEO Sergio Marchionne publicly called for industry consolidation, potentially positioning EXOR for discussions to merge FCA with another key player. German-based global sportswear and equipment brand adidas added 13% in the quarter following several important announcements. The company sold its Rockport brand for £246 million, or almost twice our appraisal value. The board began its search for a successor to CEO Herbert Hainer. Revenue was up 6% (ex-currency impact) for the year and 5% in the fourth quarter as the core soccer segment and core geographies of Europe and Latin America generated solid growth. adidas gave better-than-expected 2015 guidance of currency-neutral revenue growth in the mid-single digits. The company plans to repurchase up to £300 million in additional shares in the second tranche of its buyback plan.

The Fund’s largest detractor, Macau gaming company Melco International, declined 23% and suffered along with its peer group from an unprecedented anti-corruption crackdown imposed by Beijing. In this environment of anti-extravagance, VIP customers are avoiding Macau and contributing to high VIP growth rates in jurisdictions far away from scrutiny in places like Australia, Korea, and the UK. Mass market visitors, however, continue to increase, rising 14% in 2014. Our Melco appraisal reflects the severe slowdown in VIP revenues, but more than 80% of earnings before interest, taxes, depreciation and amortization (EBITDA) comes from mass business, which should increase further when the company’s new mass market oriented Studio City casino opens in the third quarter. The long-term investment case remains compelling with high barriers to entry, massive new infrastructure in queue to secure Macau’s role as Asia’s permanent entertainment and gaming capital, and over 70% in additional hotel capacity by 2018 to address pent-up demand amid current 90+% occupancy.

Our position in Brazilian iron ore company Manabi declined 46% in the quarter, reflecting lower offer prices and comparable transactions data. Our carrying value is only slightly above the company’s cash position. Malaysian based conglomerate Genting reported in line with expectations as strength in the Property and Oil & Gas divisions offset weak Leisure & Hospitality results. The company’s monopoly Malaysian casino and duopoly Singapore casino both traded down along with the gaming sector in the region. The company is reevaluating its Las Vegas project given the lackluster gaming revenue in the VIP segment. CEO Lim Kok Thay’s family owns 39% and has a record of consistently building intrinsic value per share. The company is buying back shares at the Genting Singapore level.

In the quarter we purchased three new positions based in Japan, Hong Kong, and the Netherlands. We added Softbank, the Japanese telecom and internet conglomerate. The company’s 34% stake in Chinese e-commerce giant Alibaba is greater than Softbank’s entire market cap. We essentially get the Japanese mobile business that will generate $5 billion/year in EBITDA plus stakes in publicly traded Yahoo Japan and Sprint, as well as a portfolio of internet companies for free. In addition, Masayoshi Son, the founder and CEO, has demonstrated an exceptional track record building businesses and allocating capital. Great Eagle Holdings is a Hong Kong based real estate company whose market cap is less than the combined value of its cash and stakes in publicly traded REITs, Champion and Langham Hospitality Trust. In addition to the listed assets, the company owns hotels worldwide under the Langham brand and investment properties in Hong Kong and San Francisco. The market’s strong aversion to Hong Kong and China real estate has created the opportunity to accumulate this holding at significantly less than the sum of its parts. We bought Dutch science-based conglomerate DSM. CEO and Chairman Feike Sijbesma is an owner-operator who has divested lower margin, lower return businesses to transform DSM into a more profitable pure-play nutrition company with solid growth prospects.
We sold Spanish based transportation infrastructure company Ferrovial when its price reached our appraisal. We bought Ferrovial during the Eurozone crisis in 2011, when the company was perceived as a highly levered Spanish construction company in spite of most of its debt being non-recourse against stable assets and its primary value being a Toronto toll road and Heathrow airport. Chairman and 45% owner Rafael del Pino consistently added value by monetizing assets at high prices and returning capital to shareholders. This investment added 144% over our holding period.

We believe the Fund is well positioned for strong future performance. The price-to-value (P/V) ratio is in the low-70s%. We believe the portfolio is invested in high quality businesses with greater FCF yields and stronger future growth potential than the MSCI EAFE Index. Our management partners are taking actions to drive strong value growth and, in many cases, creating catalysts for value recognition.

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 International 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 invest 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 Funds may be more volatile than those of larger companies. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

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

Free Cash Flow Yield (FCF Yield) equals a company’s free cash flow per share divided by the current market price per share.

As of March 31, 2015, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: CK Hutchison, 9.5%; adidas, 6.5%; EXOR 7.6%; Melco, 6.9%; Manabi, 1.2%; Genting Berhad, 3.9%; Softbank, 2.5%; DSM, 2.7%. 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.
International Fund Management Discussion

Longleaf Partners International Fund declined 6.59% in the fourth quarter and 14.76% for the full year, underperforming the MSCI EAFE Index’s decline of 3.57% and 4.90% for the two periods. The Fund’s relative performance divergence occurred primarily in the second half of the year. At the end of the first quarter, the International Fund was ahead of the Index for trailing one and five year periods, but relative returns reversed with the steep decline over the last six months. We are disappointed in the recent performance and its impact on our longer term numbers, but we remain highly confident in the quality of our businesses and management partners. Over the 16+ years since its start, Longleaf International has doubled the cumulative performance of the MSCI EAFE Index. We believe the portfolio is positioned to outperform from its current discounted level over the next several years.

Cumulative Returns at December 31, 2014

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>4Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>234.08%</td>
<td>146.40%</td>
<td>36.02%</td>
<td>19.98%</td>
<td>-14.76%</td>
<td>-6.59%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>102.18</td>
<td>45.73</td>
<td>54.29</td>
<td>29.68</td>
<td>-4.90</td>
<td>-3.57</td>
</tr>
</tbody>
</table>

Average Annual Returns at December 31, 2014

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>7.74%</td>
<td>6.20%</td>
<td>3.12%</td>
<td>3.71%</td>
<td>-14.76%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>4.45%</td>
<td>2.54%</td>
<td>4.43%</td>
<td>5.33%</td>
<td>-4.90</td>
</tr>
</tbody>
</table>

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.

The December 31, 2014 and 2013 total expense ratios for the International Fund are 1.25% and 1.27%, respectively. The expense ratios are subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.

Positive performance at a number of holdings was overshadowed by declines across the majority of our companies due primarily to the combination of a strong U.S. dollar and tighter regulation and economic controls in China. More than half of the Fund’s negative return for the year was attributable to currency translation into the U.S. dollar (USD). USD strength against the euro, which was the base currency for a dozen of our holdings over the year, meant that positive local returns at many of our European holdings translated into negative USD returns. These currency conversions did not reflect the underlying operating performance of our businesses and did not impact our long-term appraisals nearly as much as they impacted prices. The USD/euro disparity may continue given current fears of a Greek exit from the Eurozone as well as slower economic growth in Europe. Most of our European holdings are global market leaders with strong balance sheets, and much of their underlying revenue exposure is
outside of Europe. Most short-term currency dislocations will self correct over time, and our outlook for our companies’ fundamentals remains strong. The stock return figures cited below are shown in USD; most local returns were higher.

Hong Kong based conglomerate Cheung Kong was the largest contributor for the year, gaining 15%. Over the course of 2014, results at most of the company’s operating divisions were strong. Additionally, management made several value-enhancing asset sales across multiple business lines at low cap rates and used proceeds to opportunistically reinvest in discounted infrastructure deals outside of Asia with double-digit IRRs (internal rates of return). Management also returned proceeds to shareholders in the form of dividends. Most recently, in a joint venture with Mitsubishi Corp, Cheung Kong bought an airplane leasing portfolio. With its strong balance sheet, Cheung Kong can take advantage of Hong Kong land banking opportunities if prices correct.

Canadian property and casualty insurance company Fairfax Financial added 15% for the year before we sold it in the fourth quarter. We first purchased Fairfax in January 2000, and it returned approximately 11% annualized over our holding period. CEO Prem Watsa steered the company through challenges in the early 2000s and improved insurance operations over time. He also regularly grew book value, with particularly strong investment returns in the Global Financial Crisis of 2008/2009 when he made substantial gains on credit default swaps.

French luxury goods business Christian Dior (CDI), which we bought early in the year, was the largest performance contributor for the quarter, adding 17%, and ending the year up 13%. Christian Dior is the holding company for LVMH Moët Hennessy-Louis Vuitton (LVMH) and Dior Couture, the world’s most prominent collection of luxury brands. Given its holding company structure, CDI has historically traded at a discount to LVMH ranging from 7% to 40%. Gaining LVMH economic exposure through CDI aligns our interests with owner-operator Bernard Arnault. After nearly tripling shareholder capital on LVMH’s 24% stake in Hermès, Arnault distributed the Hermès stake to LVMH shareholders, and CDI’s board decided to distribute its pro-rata share of the Hermès stake. We sold the Hermès shares above our appraisal. The transaction realized a 13% yield on our average cost for CDI. Arnault’s opportunistic purchase of Hermès in the Global Financial Crisis and subsequent decision to distribute the fully-valued shares illustrate his financial discipline and intense focus on shareholder value creation.

Global fertilizer and chemical producer OCI also had a strong fourth quarter, adding 13% after positive news on various fronts. Egyptian natural gas shortages that had negatively impacted OCI’s plant utilization rates stabilized; the company won an Egyptian tax case related to the 2007 sale of its cement unit; and the EPA issued its final construction permit for the greenfield Beaumont, Texas plant that will be the largest methanol facility in the U.S. and is scheduled to begin production in 2016. CEO Nassef Sawiris’ decision in the third quarter to spin out the legacy construction business should help the market properly value OCI as a pure-play nitrogen company. Sawiris opportunistically bought shares personally throughout the year to take advantage of the price discount.

Those names that most hurt performance in the year were among the large detractors in the fourth quarter. Increased regulatory and economic controls in China directly or indirectly impacted stock prices. Chinese VIP gamblers reduced their visits to Macau, and lower Chinese demand for natural resources pressured many commodity prices as well as stocks and currencies in countries that produce resources. Some of our businesses and many of our stocks felt the impact, but the longer term fundamentals of our holdings are intact. This broad economic pressure is reminiscent of late 2011 when any stocks directly or indirectly associated with Europe were under pressure. Price declines lasted through the first half of 2012, but those discounted names set the stage for our strong outperformance in 2013.

We believe our current Asian holdings are similarly well-positioned for a strong recovery.
Increased government scrutiny and regulation in China hurt all Macau gaming companies indiscriminately and made our stakes in Melco and Galaxy via K.Wah primary performance detractors for the year with Melco down 39% and K.Wah, bolstered by its Hong Kong real estate, down 19%. At Melco, less than 15% of EBITDA (earnings before interest, taxes, depreciation, and amortization) is tied to lower margin VIP visitors who have been most severely impacted by China’s anti-corruption scrutiny and increased regulation. Melco grew its mass gaming business at a higher rate than the overall market. The company bought back 15.8 million shares, approximately 1%, over the last four months, and CEO Lawrence Ho bought an approximate $HK600 million personally in 2014. K.Wah owns 3.9% of Galaxy Entertainment, which caters more to Macau’s VIP business. Galaxy significantly outperformed the broader VIP market, and has an advantage with its planned opening in mid-2015 of the next major casino expansion on the Cotai Peninsula. Excluding the discounted market value of its stake in Galaxy, K.Wah’s remaining property business trades at less than \( \frac{1}{3} \) of book value. Management opportunistically bought urban Hong Kong land at a discount to subsequent auctions in the same area. The planned launch of large scale projects in Tseung Kwan O should increase 2015 sales. Even in the storm of worry that labeled 2014 a disastrous year for Macau gaming, overall revenues fell less than 3%, the number of visitors rose, and mass revenues grew double-digits. The Chinese government has demonstrated its long-term support of Macau with massive infrastructure projects, and efforts to crack down on corruption and attract more legitimate visitors ultimately will benefit our holdings. We are excited to own these businesses as increased accessibility and additional room supply should enable revenues to rise at healthy levels.

Lower demand from China, increased supply from major industry players, and adverse movements in resource-rich currencies and stock markets depressed iron ore prices by 49% for the year, reaching their lowest level since June 2009. Our position in Brazilian iron ore company Manabi declined 45% in the fourth quarter and 60% in the year. Manabi’s lower price reflects the current commodity environment and delays in implementing the company’s operating plan. Iron ore pressure also hurt Australian based mining services company Mineral Resources (MIN RE), which we bought in the first quarter, with returns down 32% in the year after a 15% fourth quarter decline. Because MIN RE owns some mines, it traded with the iron ore industry. Its core business of iron ore crushing and services, however, depends on volume of work rather than commodity price. Because MIN RE provides crushing services at less than half the cost that miners can achieve themselves, the company benefits as large Australian miners turn to lower-cost outsourcing when ore prices fall. Businesses unrelated to its mines produce $250 million in EBITDA, meaning the company trades at just over 4x EV/EBITDA (enterprise value/earnings before interest, taxes, depreciation, and amortization). Management is using its financial flexibility to invest in crushing and processing capacity at this opportunistic time.

We bought BR Properties, Brazil’s largest manager of commercial office buildings, in the first quarter. Brazilian stocks and currency declined following the recent re-election of President Dilma Rousseff, who has doubled the pace of interest rate increases in an effort to slow inflation. Our stake in BR Properties fell 27% in the fourth quarter and 29% over our holding period. As lending rates increased to 11.75% and the Brazilian real fell to a nine-year low in December, the entire Brazilian real estate sector declined. BR Properties successfully navigated the political environment under Dilma over the past four years, and the long-term business value of its properties is much more stable than either these rate changes or currency moves. The company continued to lease its new buildings, sold non-core assets, and bought back shares at a steep discount.

Broad pressure on the Norwegian economy and stock market following the price slide in oil hurt our return in consumer goods company Orkla, as did the kroner’s decline to its lowest level since 2009. Orkla lost 25% in the fourth quarter, offsetting earlier gains and ending the year down 9%. Management moved to focus on the branded
consumer goods business following the IPO (initial public offering) of its aluminum business, Granges. This listing strengthened Orkla’s balance sheet by deconsolidating the company’s debt.

Throughout the year we bought nine new positions as dislocations around the world and at individual companies gave us more attractive opportunities than usual. In addition to the first quarter purchases of CDI, MIN RE, and BR Properties discussed above, we added Vopak. In the second quarter, we bought lida and Colt, and in the third quarter, adidas and Vivendi. In the last three months, we bought Australian-based testing, inspection, and certification company ALS Limited. The same previously described mining pressures impacted ALS, which is associated with Australian mining even though the company has minimal exposure to iron ore.

We exited an unusually high number of businesses because some approached our appraisals and others presented the opportunity to sell more fully valued and/or lesser quality names to position the portfolio in businesses with a larger margin of safety and higher expected value growth. In the most recent quarter, we sold Fairfax and the Hermès distribution from CDI as described above. We exited Vopak, a first quarter purchase, lida, a second quarter purchase, and NewsCorp after our investment cases changed.

We thank our fellow shareholders for your continued partnership in a year when short-term performance did not reflect our long-term value proposition. As the Fund’s largest owners, we are not pleased with our recent performance. The return, however, does not adequately reflect the underlying progress our companies made during the year. We are confident in the collection of high quality, industry-leading companies in the portfolio as well as in our management partners who are taking action to build shareholder value.

As we would expect from shareholder-oriented managements with meaningfully discounted shares, we saw buybacks at most companies and personal share purchases by many of our partners. As you would expect from your investment management partners, we have been adding to our personal holdings in the International Fund, which currently trades at a mid-60s% price-to-value ratio (P/V).

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RISKS

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Internal rate of return (IRR) is the interest rate at which the net present value of all the cash flows from an investment equal zero.

EV/EBITDA is a ratio comparing a company's enterprise value and its earnings before interest, taxes, depreciation and amortization.

As of December 31, 2014, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: Cheung Kong, 7.7%; Christian Dior, 5.2%; OCI, 6.1%; Melco, 7.4%; K Wah, 5.8%; Manabi, 2.1%; Mineral Resources, 4.1%; BR Properties, 4.6%; Orkla, 3.7%; Colt, 4.7%, adidas, 4.9%; and Vivendi, 4.9%. 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.
International Fund Management Discussion

Longleaf Partners International Fund declined 10.3% in the third quarter and 8.8% for the year-to-date (YTD). The Fund underperformed the MSCI EAFE Index’s decline of 5.9% for the quarter and 1.4% YTD. Over the 15+ years since its start, Longleaf International has more than doubled the cumulative performance of the EAFE Index.

Cumulative Returns at September 30, 2014

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>YTD</th>
<th>3Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>257.63%</td>
<td>162.91%</td>
<td>58.34%</td>
<td>30.35%</td>
<td>-2.46%</td>
<td>-8.75%</td>
<td>-10.25%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>109.67</td>
<td>76.80</td>
<td>84.52</td>
<td>37.41</td>
<td>4.25</td>
<td>-1.38</td>
<td>-5.88</td>
</tr>
</tbody>
</table>

Average Annual Returns at September 30, 2014

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>8.33%</td>
<td>6.66%</td>
<td>4.70%</td>
<td>5.44%</td>
<td>-2.46%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>4.76</td>
<td>3.87</td>
<td>6.32</td>
<td>6.56</td>
<td>4.25</td>
</tr>
</tbody>
</table>

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.

The December 31, 2013 total expense ratio for the International Fund is 1.27%. The expense ratios is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.

Only a handful of names appreciated in a quarter when prices decoupled from values, as macro pressures and uncertainty weighed on many of our holdings. One factor that heavily impacted short-term performance of both the Fund and Index was the U.S. Dollar (USD) strengthening. Most currencies moved meaningfully lower against the USD, causing the translation of stock returns from local currencies into USD to negatively impact most of our holdings and accounting for approximately half of the Fund’s decline. These short-term movements did not reflect the underlying operating performance of our businesses and did not impact our long-term appraisals. (The stock return figures cited below are shown in USD; local returns were higher.)

Vopak, the global leader in independent oil and chemical tank storage, added 11% in the period, making it the largest contributor in the quarter. This Netherlands-based company rebounded after reporting results in line with expectations and providing higher EBITDA (earnings before interest, taxes, depreciation, and amortization) guidance. One reason we were able to buy Vopak at a discount last year was that crude oil had been in an unusual period of backwardation, meaning the front end of the futures price curve was higher than the back end. In this environment, traders exit the market, and oil storage declines. In August, the oil futures’ price curve returned to an upward slope or “contango,” meaning the longer dated price is again higher than the front end price. Vopak benefited from an uptick in traders storing oil for future profit.

After a 2% gain in the quarter, Norwegian consumer goods company Orkla became the largest contributor YTD, adding 21%. The company’s results beat sell side expectations with...
positive organic revenue growth from product innovation and marketing efforts. To offset rising raw material costs, Orkla increased prices in its food segment, highlighting the business’ pricing power. The company is reorganizing its Confectionary and Snacks business under new management, and the recently announced bolt-on acquisition of NP Foods will double its presence in the Baltics and increase scale, pricing power, and negotiating ability. Management’s disposal of non-core assets progressed with the initial public offering (IPO) of Granges aluminum just after quarter end.

Although Cheung Kong declined 7% in the third quarter, its 13% YTD return made this Hong Kong-based conglomerate a large contributor for the year. In the first half, Hong Kong property sales were strong, and management made several value-enhancing asset sales across multiple business lines as well as returned capital to shareholders. More recently, Cheung Kong’s price was penalized amid protests and labor strikes in Hong Kong. Our appraisal remained intact. We are partnered with strong capital allocators who have not bought overpriced assets in China or Hong Kong. Cheung Kong’s strong balance sheet positions management to buy discounted land in the event of a real estate correction.

Most holdings declined in the quarter. While we have limited direct exposure to companies based in emerging markets, top line exposure to developing regions impacted a number of our names. Our companies with exposure to China demand, whether directly as with Macau gaming or indirectly as with natural resources and luxury goods, came under more pressure with the Chinese government crackdown on corruption causing wealthier people to keep a lower profile away from Macau, slower Chinese economic growth hurting property sales that boosted gambler credit, and liquidity challenges faced by junket operators who organize VIP visits and extend credit to them. Other pressures impacting the stocks are difficult to quantify, such as tighter transit visa requirements, wage inflation and labor unrest, UnionPay credit card restrictions, and a smoking ban starting in October. We met with all of Macau’s casino operators in September. Our confidence in Macau’s long-term attractiveness, and particularly Melco, remains high in spite of the negative news flow. Our appraisal already incorporated lower growth in both VIP and mass revenues than most sell-side analysts had previously assumed for the year. Over 80% of Melco’s EBITDA comes from the mass, non-VIP segment that is still growing gross gaming revenue at 15%. This important mass market has margins several times higher than the margins on VIPs whose revenues are split with junket operators. 100% hotel occupancy also has limited growth this year, but new hotel inventory, projected to increase over 50% in the next three years, should expand visitation, as should the new Hong Kong–Macau bridge that will allow passengers at the Hong Kong airport to arrive in Macau in half an hour. Melco has a near-term supply advantage with its Studio City casino and hotel opening in 3Q 2015. Despite analyst downgrades on Macau gaming stocks, Melco is estimated to have high EBITDA growth in 2015 and 2016. The company began repurchasing shares in Melco Crown in September, and our partner, CEO Lawrence Ho, has bought more stock personally in the last five months.

Cement maker Lafarge declined 16% in the quarter following weak emerging market results, due in part to currency moves. Additionally, the stock pulled back after its initial surge on the announcement of the Holcim merger. The company’s geographic diversity and our already conservative growth assumptions helped our appraisal remain steady. Slower volume growth in a few markets, such as Latin America, Western Europe, and Eastern Europe, was offset by solid demand in North America, Asia, and the U.K., as well as strong
Quarterly Report 3Q 2014

International Fund Management Discussion

pricing in most markets. The planned merger with Holcim should be completed in 2015, providing upside opportunity through over €1 billion in cost savings and synergies. CEO Bruno Lafont has enhanced the company’s value by divesting a number of plants at attractive prices as he moves to meet anticipated antitrust requirements.

The Hong Kong property company K. Wah International declined 18% in the quarter, erasing earlier gains and taking the YTD return to a 15% decline. The Macau gaming concerns that affected Melco also negatively impacted K. Wah because of its 3.9% stake in Galaxy Entertainment, one of the six operators licensed in Macau. Slower sales of K. Wah’s luxury China properties driven by the government-imposed slowdown were somewhat offset by mass market property sales in Hong Kong. Management opportunistically bought attractively priced land in urban Hong Kong at a discount to subsequent land auctions in the same area.

Global fertilizer and chemical producer OCI declined 21% in the third quarter and 32% for the year. Natural gas is the primary component in nitrogen fertilizer production, and during the quarter, gas supply interruptions impacted OCI’s two Egyptian plants, weighing on the short term stock price. Management anticipates that plant utilization will improve over the next year with several factors increasing gas supply: Egypt has begun to import liquid natural gas for the power sector, the cement industry is switching from natural gas to petroleum coke, and the major producers have begun to return to Egypt to ramp up exploration in the wake of a more stabilized government. We assume a continued low utilization rate of 50% in our appraisal, but even at this rate, the plants are cash flow positive. OCI’s other plants around the world are operating at or near full capacity and benefitting from low cost gas and higher prices for Ammonia and Urea, two primary outputs. The long-term case for OCI remains compelling as the company is a low cost industry leader in nitrogen fertilizer, essential for world food production. In the next 12-18 months the company will have higher production and lower capex with the opening of a greenfield plant in Iowa and the completion of the Beaumont, Texas extension. The company is also building the largest methanol plant in the country in Texas. CEO Nassef Sawiris has built and monetized substantial value historically; specifically, he has added enormous value for our partners in the International Fund through his work at Lafarge. Most recently, he announced that in early 2015 OCI will separate the fertilizer and construction businesses to remove the conglomerate discount in the stock price.

In the quarter we bought two new businesses, adidas and Vivendi, and added to several discounted positions. German-based adidas is among the top global sportswear and sports equipment brands. Short-term currency moves, concerns over its business in Russia, and management’s postponing 2015 margin targets gave us the opportunity to buy this world class brand at a discount. Management recently announced plans to repurchase up to €1.5 billion – over 10% of shares – and to return capital via a dividend. French company Vivendi consists of two key businesses – Universal Music Group, the world’s largest record label, and Canal+ Group, France’s biggest pay-TV operator. The recent sale of Vivendi’s Brazilian broadband business, GVT (Global Village Telecom), highlights Chairman and 5% owner Vincent Bolloré’s focus on creating value for shareholders. Southeastern has invested in Vivendi successfully twice before, and the company’s focus, asset quality, and management team has grown even stronger.

To fund our purchases, we trimmed several appreciated stocks and sold Guinness Peat, Hochtief, and Vodafone in the quarter. These exits highlight our long-held investment discipline of selling more fully valued and/or lesser quality names to position the portfolio in businesses with a larger margin of safety and higher expected value growth.

As the Fund’s largest shareholders, we feel the discomfort of our recent performance. However, our competitively positioned businesses, strong balance sheets, and capable management partners give us confidence in the longer-term prospects for the portfolio. The Fund ended the quarter with a price-to-value ratio (P/V) in the high-60s%, and we have a robust on-deck list of potential new qualifiers around the world.

See following page for important disclosures.
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RISKS

The Longleaf Partners International 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 invest 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 Funds may be more volatile than those of larger companies. Investing in non-U.S. securities may entail risk due to non-US economic and political developments, exposure to non-US currencies, and different accounting and financial standards. These risks may be higher when investing in emerging markets.

MSCI EAFE Index (Europe, Australasia, Far East) is a broad based, unmanaged equity market index designed to measure the equity market performance of 22 developed markets, excluding the US & Canada. 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.

As of September 30, 2014, the holdings discussed represented the following percentages of the Longleaf Partners International Fund: Vopak, 4.1%; Orkla, 4.4%; Cheung Kong, 6.7%; Melco International, 6.6%; Lafarge, 7.2%; K Wah, 5.4%; OCI, 4.5%; adidas, 4.7%; and Vivendi, 4.5%. 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.
International Fund Management Discussion

Longleaf Partners International Fund declined 1.3% in the second quarter, taking the year-to-date (YTD) return to 1.7%. The Fund underperformed the MSCI EAFE Index’s 4.1% in the quarter and finished the first half below the Index’s 4.8%. In spite of the weak quarter, the Fund’s one year return remained well above our absolute goal of inflation plus 10% but dipped below the benchmark. Over the 15+ years since its start, Longleaf International has nearly doubled the performance of the EAFE Index.

Cumulative Returns at June 30, 2014

<table>
<thead>
<tr>
<th>Fund</th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>YTD</th>
<th>2Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>298.48%</td>
<td>198.21%</td>
<td>68.19%</td>
<td>67.66%</td>
<td>22.76%</td>
<td>1.67%</td>
<td>-1.30</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>122.76</td>
<td>96.08</td>
<td>95.49</td>
<td>74.41</td>
<td>23.57</td>
<td>4.78</td>
<td>4.09</td>
</tr>
</tbody>
</table>

Average Annual Returns at June 30, 2014

<table>
<thead>
<tr>
<th>Fund</th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>9.22%</td>
<td>7.56%</td>
<td>5.34%</td>
<td>10.89%</td>
<td>22.76%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>5.25</td>
<td>4.59</td>
<td>6.93</td>
<td>11.77</td>
<td>23.57</td>
</tr>
</tbody>
</table>

The index is unmanaged. 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.

The December 31, 2013 total expense ratio for the Fund is 1.27%. The expense ratio is subject to fee waiver to the extent normal annual operating expenses exceed 1.75% of average annual net assets.

The Fund’s top performers over the last three months also posted gains in the first quarter, thereby making them the largest YTD contributors. Cheung Kong, the Hong Kong based conglomerate with businesses around the world, returned 15% in the second quarter, pushing the YTD return to 21%. In the first half of 2014, management made value-enhancing asset sales across multiple business lines. In the first quarter, Cheung Kong Infrastructure spun off and listed Hong Kong Electric. Additionally, 50% owned affiliate Hutchison Whampoa sold 25% of A.S. Watson Group, the world’s largest health and beauty retailer. In the second quarter, the company paid a HK$7 special dividend with the proceeds of the Watson sale. Hong Kong residential property sales accelerated after the government relaxed some stamp duty regulations. With high land valuations, our partners exercised the discipline we have come to expect – abstaining from any land purchases in Hong Kong or China for over a year.

Global cement producer Lafarge added 11% in the quarter and 16% in the half. The company announced a merger with Holcim that will create economies of scale for cost savings and combine Lafarge’s innovation strength with Holcim’s plant efficiency. The merger plan includes divestitures, largely in Europe, where low cost financing and economic recovery are generating buyer interest. If approved, the merger should close in the
second half of 2015. Although foreign currency headwinds negatively impacted results in the second quarter, underlying revenues and operating cash flow grew nicely due to increases in volumes and pricing as well as cost containment. Lafarge also sold its Ecuador operations for a per ton price higher than what we used in our appraisal.

Norwegian branded food company Orkla contributed 9% in the quarter and 19% YTD. Orkla reported two solid consecutive quarters with improved working capital and net debt. New CEO Peter Ruzicka has been on the board of Orkla since 2006 and is focused on maximizing the branded consumer goods business by driving organic growth and minimizing costs. The company announced that it is considering an initial public offering (IPO) of Granges, its rolled aluminum business – an example of management’s focus on branded consumer goods and commitment to value realization of non-core businesses.

Though a number of names retreated in the quarter, the two primary detractors, Manabi and OCI, also weighed on YTD results, as did the first quarter’s lowest performer, Melco. As an illiquid security, Brazilian iron ore company Manabi is priced using input from a third party appraisal firm that examines various factors, including comparable publicly traded iron ore mining stocks and Manabi’s progress, to produce a valuation range. Due to a more difficult environment for mining companies, including Manabi, we reduced the price 23%, to the low end of the valuation range.

Global fertilizer and chemical producer OCI fell 14% over the last three months, offsetting the first quarter gain and creating a YTD decline of 13%. The company announced that no dividend would be paid on 2013 earnings due to pre-funding $1 billion in capital investment for 2014. We view substituting growth capital expenditure for the dividend as a solid capital allocation move by CEO Nassef Sawiris, who has generated solid returns over time through greenfield expansions and financial investments. In addition to eliminating the dividend, several short-term pressures impacted the stock. OCI’s Algerian fertilizer plant, Sorfert, had shipments delayed in 2013 after the Algerian government required new export license agreements. As of April 2014, the plant had returned to 100% utilization, and management expects this utilization to continue for the rest of the year. The company also reported weak utilization at its Egyptian plants due to gas curtailments, which we already accounted for in our appraisal.

Macau gaming company Melco International was down 18% YTD after a 9% second quarter decline. The price fell amid broader Macau gaming industry concerns, but Melco’s business was impacted very little by much of the negative news which included lower VIP gaming revenues, junket defaults, removal of illegal mobile credit card terminals from the gaming floor, restrictions on transit visas, and a smoking ban on the mass floor starting in October. Melco’s profits are heavily weighted to the mass market, with approximately 75% of EBITDA (earnings before interest, taxes, depreciation and amortization) now coming from non-VIP business. The industry revenue decline and junket issues were related to VIP guests and had little impact on Melco. Mass gaming continued to grow over 30% without any other issues appearing to affect traffic. CEO Lawrence Ho personally bought $21 million (HK$165mm) worth of stock in the second quarter, adding for the first time since September 2011 when we first initiated our Melco position. We also increased our ownership during the quarter.

In the quarter we began buying Iida and Colt Group, bringing to six the number of new holdings this year. We also increased our stakes in Genting, Melco, and Philips over the last three months. We are currently seeing the most opportunity in companies that are based in – or impacted by – macroeconomic factors in the Asia Pacific region. Broad macro fears of reduced Chinese consumer demand, as well as worries of a potential Chinese real estate bubble, have impacted companies as far ranging as Hong Kong real estate, Macau gaming, European luxury consumer goods, and Australian mining services. What separates the companies we have bought from others impacted by China fears are our
management partners, most of whom are significant owner-operators with track records of value creation. The quality of and discounts in our Asian holdings today remind us of those in our European investments coming out of 2011 that subsequently rebounded and drove much of the Fund’s strong performance over the last two years. With Europe’s bounce back, we sold ACS in the first quarter and TNT Express in the second, when we also trimmed Ferrovial, Hochtief, and Lafarge. Following the 2013 Japan rally, we sold Nitori early this year. We also sold our small position in UGL over the last three months. We swapped the direct position in agricultural equipment and commercial truck company CNH Industrial for parent company EXOR.

The portfolio ended the quarter with a price-to-value ratio (P/V) in the high-60s% and cash at 9%. The P/V ratio became more attractive (lower) with our portfolio transactions and value growth across most holdings. We remain highly confident in the qualitative position of our strong businesses and management partners, and the current cash position gives us the flexibility to move quickly as we identify new qualifiers.

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As of 6/30/14, the top 10 holdings in Longleaf Partners International Fund – Lafarge (7.7%), Cheung Kong (7.6%), EXOR (6.6%), Melco (6.4%), K Wah (5.9%), Orkla (5.3%), OCI (5.1%), News Corp (4.8%), Philips (4.8%), Genting (4.4%). 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.

Expires October 15, 2014
Longleaf Partners International Fund gained 3.0% in the first quarter, strongly outpacing the MSCI EAFE Index’s return of 0.7%. The Fund nearly doubled the performance of EAFE since inception and beat the Index in most trailing periods as indicated below.

**Cumulative Returns at March 31, 2014**

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>1Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>303.72%</td>
<td>249.64%</td>
<td>70.06%</td>
<td>110.71%</td>
<td>23.13%</td>
<td>3.01%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>114.01</td>
<td>93.17</td>
<td>88.22</td>
<td>110.17</td>
<td>17.56</td>
<td>0.66</td>
</tr>
</tbody>
</table>

**Average Annual Returns at March 31, 2014**

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>9.47%</td>
<td>8.70%</td>
<td>5.45%</td>
<td>16.07%</td>
<td>23.13%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>5.06</td>
<td>4.49</td>
<td>6.53</td>
<td>16.02</td>
<td>17.56</td>
</tr>
</tbody>
</table>

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.

The total expense ratio for the Longleaf Partners International Fund is 1.29%. The expense ratio is subject to a fee waiver to the extent the Fund’s normal annual operating expenses exceed 1.75% of average annual net assets.

Italian holding company Exor was the largest contributor for the quarter, adding 12%. Exor owns Fiat Chrysler Auto, which had strong performance after Fiat merged with Chrysler in the period. Exor also benefitted from a strong rebound in Italian stock markets in response to political progress and broad enthusiasm about the direction of the Italian economy and government. Another Exor holding, agriculture equipment and truck company CNH Industrial, remained on track with the integration of its recently combined pieces, Fiat Industrial and CNH. Exor Chairman and CEO John Elkann, who has an excellent investing track record, has net cash available to provide liquidity when compelling investment opportunities arise. We swapped the Fund’s direct holding in CNH Industrial for an increased weight in Exor in the quarter.

Norwegian branded food company Orkla returned 10%. Orkla reported a solid quarter, with improved working capital and net debt. The company announced a new CEO, Peter Ruzicka, who has a long track record in branded consumer goods and has been on the Orkla board since 2008. He is committed to Chairman Stein Erik Hagen’s plan to transform the company by selling noncore assets and focusing on consumer branded goods.

Infrastructure company Ferrovial added 12% in the quarter, driven by solid results from the ETR-407 toll road in Toronto and London’s Heathrow airport along with higher than expected cash balances after collecting cash owed from regional governments in Spain. Ferrovial has €1.7 billion in net cash at the holding company. Management recently announced a €0.30/share complementary dividend will be paid in May. Special dividends have consistently been paid in previous periods when management could not find suitable investment opportunities that met their demanding internal return hurdle. Because the Texas toll roads that Ferrovial is building are on schedule and nearing completion, and because the company’s other world-class infrastructure assets continue to grow in value, we expect free cash flow to increase meaningfully in the coming years.

Fairfax Financial, the property/casualty insurer, was up 11% in the quarter. Andy Barnard has successfully managed the insurance operations with solid underwriting and integration of acquisitions done in years past. A low number of catastrophes also helped recent results. CEO Prem Watsa’s investment returns have been held back by high cash and equity hedges over the last year, but he is off to a good start this quarter.

Macau gaming company Melco lost 9% making it the Fund’s largest detractor in the quarter. Market concerns over short-term weak January gaming growth, driven primarily by the timing of Chinese New Year, impacted the stock, as did stories about Macau shortening license renewal periods. The
company later reported record growth in February with fiscal year (FY) 2013 luck-adjusted EBITDA (earnings before interest, taxes, and amortization) up 44% and revenues up 27% year-over-year. Melco announced a special dividend of $191 million.

Hong Kong property company K Wah International declined 1%. Through its 3.9% stake in Macau gaming company Galaxy Entertainment, K Wah was negatively impacted by the same short-term market concerns as Melco. K Wah’s property business benefitted in the quarter from sale proceeds of both an investment property in Singapore and residential property in China. K Wah is slowing its land acquisition activity and is currently focused on selling its high-end Shanghai residential project. Galaxy Entertainment comprised over 75% of K Wah’s market capitalization at quarter end, meaning the remaining property business is trading at 0.2x book. Meanwhile, Galaxy, like Melco, is growing value per share extremely quickly.

We sold Nitori and ACS as each reached our appraisals. We bought four new businesses in the quarter. Unlike in 2011-2012, when we saw broad macroeconomic “themes” driving pockets of geographic (i.e. Europe) and/or sector (i.e. industrials, materials, insurance) cheapness, we are finding new ideas today across a broad range of sectors and geographies, based on more idiosyncratic, stock-specific factors.

The portfolio P/V (price-to-value ratio) is in the mid-70s%, and cash is just over 12%. After strong performance in global markets in the past two years, we remain highly alert to how potential macro risks may impact the overall portfolio. We believe the quality of what we own will help protect and grow intrinsic values, even if market prices slide. We believe our businesses are:

- Financially strong (many with net cash) and well-positioned to take advantage of market dislocations to buy in shares, make smart acquisitions, or sell assets at attractive prices;
- Led by management teams with track records of value creation, as evidenced by what they have done in previous times of crisis; and
- Industry leaders that have pricing power to protect against deflationary or inflationary scenarios.
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As of 3/31/14, the top 10 holdings in Longleaf Partners International Fund – EXOR (7.0%), Cheung Kong (6.9%), Lafarge (6.8%), OCI (5.8%), K Wah (5.6%), Philips (5.0%), Orkla (4.9%), Ferrovial (4.6%), News Corp (4.5%), Melco (4.5%). 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 Rafferty Capital Markets, LLC. As of May 1, 2014, Funds distributed by ALPS Distributors, Inc.
Longleaf Partners International Fund produced strong results for the fourth quarter and the year, gaining 6.9% and 28.1%, respectively. These results outpaced the EAFE Index’s 5.7% and 22.8% returns for the same periods and far exceeded our absolute annual goal of inflation plus 10%. The Fund also outperformed the benchmark for the 15+ years since inception.

Cumulative Returns at December 31, 2013

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>15 Year</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>4Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>291.93%</td>
<td>259.51%</td>
<td>75.86%</td>
<td>73.38%</td>
<td>28.14%</td>
<td>6.89%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EAFE Index</td>
<td>112.60</td>
<td>94.57</td>
<td>95.09</td>
<td>79.69</td>
<td>22.78</td>
<td>5.71</td>
</tr>
</tbody>
</table>

See page 18 for additional performance information.

Melco International gained 219% for the year after rising 37% in the fourth quarter. Through its joint venture in Macau casino operator Melco Crown, the company benefitted from the limited supply and large demand for Macau gaming. In the quarter, the company reported a 24% increase in overall revenue and a luck-adjusted 50% increase in year-over-year EBITDA (earnings before interest, taxes, depreciation, amortization). CEO Lawrence Ho, who is Melco’s largest shareholder, has focused the business on mass-market gamblers, a much more profitable segment than VIPs whose revenues are shared with junket operators. He is using capital to benefit from the acceleration in visitor arrivals and length of stays over the coming years by building Studio City and adding to City of Dreams. While Macau does seven times more gaming volume than Las Vegas, it currently has one-eighth the hotel rooms. The opening of the Macau-Hong Kong Bridge in 2016 will allow easy access to the Hong Kong Airport and provide travelers from Chinese cities on the eastern side of the Pearl River Delta a much quicker route to Macau, bringing more customers. Despite the strong price appreciation during the year, the stock remains below our appraisal, because revenues grew significantly ahead of our expectations. We did trim the position to maintain a normal weight as the price rose.

OCI gained 33% in the fourth quarter, bringing its appreciation to 41% since we purchased the stock in the third quarter. OCI is one of the world’s leading nitrogen fertilizer producers with capacity of nearly 7 million tons. The company also operates one of the leading engineering and construction firms in the Middle East and North Africa specializing in complex infrastructure projects. Chairman and CEO Nassef Sawiris controls 54% of the stock and has a strong operating and capital allocation record. He sold Orascom Cement in 2007, just before the financial crisis, and successfully listed 22% of OCI Partners in October 2013. OCI Partners, which is 78% owned by OCI, is up nearly 50% from the IPO price. He has built OCI into one of the industry’s lowest cost fertilizer producers through long-dated natural gas contracts at low prices (a primary ingredient in fertilizer) and newer, more efficient plants that are strategically located next to either main export hubs or major agricultural centers.

Global telecommunications giant Vodafone ended 2013 with a 55% gain after a 7% rise in the fourth quarter. Mid-year, CEO Vittorio Calao negotiated a compelling price to sell the company’s 45% ownership of Verizon Wireless to Verizon. He has committed to return much of the proceeds to shareholders. In the fourth quarter, speculation that AT&T would make an offer for Vodafone helped push the stock higher. With or without a deal, management is growing value for shareholders not only through capital allocation, but also through successfully adjusting to the evolving telecom landscape in Europe, Africa, and India.

Hochtief, one of the world’s leading infrastructure construction firms, was a significant contributor...
for the year with a 50% return. CEO Marcelino Fernandez Verdes spent his first year selling non-core assets including the company’s airports and services business at prices above our carrying values while refocusing the company on its historical core capabilities. With the proceeds from the asset sales, he paid down some debt, repurchased 10% of shares, increased the dividend, and opportunistically bought more of 56%-owned Leighton at a steep discount to value. He has net cash to take advantage of additional opportunities or return it to shareholders, and, just after the New Year, the company announced that it had sold an office building in Germany, the first step in the eventual sale of all of the non-core real estate assets.

Philips CEO Frans Van Houten and CFO Ron Wirahadiraksa completed a €2bn stock buyback at discounted prices, as well as delivered higher margins as planned. Philips’ management team is pursuing additional cost reductions and believes the company has strong revenue and margin potential over the next two to three years in all three primary businesses: medical, lighting, and consumer lifestyle. They signaled their confidence in the future value growth of the business by announcing another €1.5bn share buyback.

Brazilian iron ore company Manabi was the primary detractor for the quarter and the year, down 10% and 31%, respectively. While currency moves played a part in lowering our carrying value, broad industry dynamics, transactions, and a reduction in our mine life assumptions also caused adjustments to the price. Recent reports confirmed the quantity and quality of the iron ore reserves, and the company is moving forward to get the licenses and infrastructure in place to begin mining. We sold Brazilian oil and gas exploration company HRT early in the fourth quarter. Unsuccessful drilling results in Brazil and Namibia combined with management hubris made this a disappointing investment. Our takeaway lesson was that we will not buy an E&P company in the future if it does not have current production to provide a floor to the value. We also sold our Henderson Land position, which was down for the year after a 5% decline in the fourth quarter. Worries over higher interest rates and the Hong Kong government’s housing policy regulations weighed on the price. While the company’s Hong Kong real estate remained undervalued, management’s decision to buy overvalued shares of Hong Kong China & Gas from its Chairman, rather than using the capital to buy its own shares at a deep discount, changed our view of our partners, and we eliminated our position.

During the year, we bought new positions in eight companies. Three of these were in the fourth quarter, including Guinness Peat, an investment holding company, Orkla, a Nordic consumer foods business, and K Wah, a real estate and casino company primarily in Shanghai and Macau. We eliminated eight positions in 2013, mostly after the gaps between prices and our appraisals closed. In addition to those previously mentioned, we sold Accor, C&C Group, and Willis Holdings in the first quarter and NIDEC and Cemex in the third quarter.

We added the building blocks for our strong results in 2013 over the last few years when many investors were avoiding the short-term uncertainty of Europe and Asia. Even though a number of our holdings have experienced solid double-digit value growth, strong performance has pushed the Fund’s P/V into the high-70s%, and cash is 20% (although adjusted for swaps is more like 17%). We believe that our current holdings have much upside opportunity not captured in our conservative appraisals. We have a number of interesting names on-deck but will maintain our deep discount discipline.
International Fund Management Discussion

Longleaf Partners International Fund gained 13.0% for the third quarter and 19.9% year-to-date (YTD), outpacing the EAFE Index’s 11.6% and 16.1% returns for the same periods, and far surpassing of our annual absolute return goal of inflation plus 10%. Over the last year, the Fund was up almost 30%. Since inception almost 15 years ago, the International Fund has returned more than two-and-one-half times the Index.

Cumulative Returns at September 30, 2013

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>YTD</th>
<th>3Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>266.65%</td>
<td>82.06%</td>
<td>32.56%</td>
<td>29.83%</td>
<td>19.87%</td>
<td>12.95%</td>
</tr>
<tr>
<td>(Inception 10/26/98)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EAFE Index</td>
<td>101.11</td>
<td>116.07</td>
<td>36.06</td>
<td>23.77</td>
<td>16.14</td>
<td>11.56</td>
</tr>
</tbody>
</table>

See page 20 for additional performance information.

Macau gaming company Melco International was the largest contributor in the third quarter and YTD, up 42% and 132% respectively. Double-digit visitation increases from Mainland China drove industry gross gaming revenue growth to the high-teens/low 20% range. Margins at the company rose as the more profitable mass market business grew faster than the VIP business (where margins are much lower because revenues are shared with junket operators). The company is exploring opportunities in new gaming markets, and earlier this year completed an IPO of its Philippine business. The value of the company grew, and we added to our position in the quarter.

German-based construction and engineering firm Hochtief rose 34% in the quarter and 53% YTD, making it the second largest contributor for both periods. Since CEO Marcelino Fernandez Verdes took over late last year, the company has sold its airport assets and services business at prices above our carrying value, repurchased 10% of shares, and opportunistically bought an additional 3% of Leighton at a steep discount to value. Management has embarked on a turnaround of the European construction business and improved risk controls at its 55%-owned Leighton subsidiary, which should lead to improved margins and free cash flow in both of these segments. Hochtief is working to sell its non-core real estate assets to complete its transformation into one of the world’s leading infrastructure construction firms. ACS, the Spanish-based global construction and engineering company that owns 52.5% of Hochtief, also appreciated with the positive news, adding 28% in the third quarter and 34% YTD.

Our Dell options position, which we closed out, gained 38% YTD. Michael Dell put his personal gain above other shareholders’ interests and eventually won approval of a management buyout well below the value of Dell’s free cash flow and assets. We recognized our errors in assessing Michael Dell as a partner, but we believed that fighting for our clients’ interests against the first MBO in our 38 year history would generate a better outcome than his initial offer, and it did. Our collective opposition with other institutional owners forced the board to postpone the vote three times to avoid defeat, change the record date, alter voting rules, and secure a higher offer to gain approval of the deal. Southeastern infrequently becomes an activist, but when we do, we cover all expenses incurred out of our own pockets – not the Longleaf Funds’ assets. Importantly, fighting for shareholders usually has delivered a superior result.

The Fund’s position in Brazilian oil and gas exploration company HRT was minimal, but the stock was among the few decliners over the last three months and YTD. Shares fell in the quarter following unsuccessful drilling results in Namibia. Over the last year, we worked to
improve governance via new board members and a management change. The company is exploring all options to extract the remaining value, but given the time it will take and the inconsequential impact it would have on the Fund’s results, we sold the position subsequent to quarter-end.

Brazilian iron ore company Manabi’s stock moved little in the quarter, but remained a YTD detractor after we lowered our carrying value in the second quarter. The price change reflected a variety of external factors but did not indicate any fundamental changes to our investment case. Manabi’s Tier One assets have a concentration of the highest quality iron ore, and management is making progress in securing the necessary infrastructure to bring this iron ore to market.

Despite the run-up in the market, we were able to buy one new position, OCI. We filled out our News Corp position and added to TNT Express and UGL, all of which we initiated earlier in the year. We increased our Vodafone position after CEO Vittorio Colao announced the company would sell its 45% stake in Verizon Wireless to Verizon for $130 billion in cash and stock and return much of the proceeds to shareholders. Through a swap, we hedged out the Verizon shares we would own in the deal and gained larger exposure to Vodafone. We also added to Exor, the Agnelli family holding company run by John Elkann. Exor, which owns 27% of CNH (previously named Fiat Industrial), was a more discounted way to own this global agriculture equipment company. During the quarter, through Vodafone’s sale of Verizon Wireless and Exor’s sale of SGS Testing, our management partners created and realized substantial value by striking deals well above our appraisal values.

In addition to closing out the Dell options, we fully exited Nidec when the stock approached our appraisal after a major restructuring helped the company achieve sales and margin targets. We sold our Cemex convertible bonds as they appreciated significantly. We trimmed some of our stronger performers during the quarter, including ACS, Hochtief, and Philips.

The strong quarter increased the Fund’s P/V to the low-70s%. While the market appreciation has made it harder to find new qualifying ideas, macro factors, such as low economic expectations in Europe and concern over a hard landing in China, have created some discounts. We have identified several interesting investment opportunities but are maintaining our discount discipline as we patiently wait for prices to cooperate.

Market appreciation has made it harder to find new qualifying ideas.
Longleaf Partners International Fund declined 1.0% in the quarter, in line with the EAFE Index’s -1.0% return. The Fund’s year-to-date (YTD), one and five year results outpaced the Index. Since inception, Longleaf International more than doubled EAFE’s return. For the last twelve months the Fund has also outpaced our annual absolute goal of inflation plus 10%.

Cumulative Returns at June 30, 2013

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>Five Year</th>
<th>One Year</th>
<th>YTD</th>
<th>2Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>224.61%</td>
<td>-0.42%</td>
<td>27.26%</td>
<td>6.13%</td>
<td>-1.00%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>80.27</td>
<td>-3.12</td>
<td>18.62</td>
<td>4.10</td>
<td>-0.98</td>
</tr>
</tbody>
</table>

See page 22 for additional performance information.

Macau gaming company Melco International was the top contributor to performance in the second quarter and for the first half, returning 10% and 50% respectively. Melco had strong visitor growth and increased margins in its Macau casinos as the more profitable mass market continued to outgrow VIP guests. The company completed the successful IPO of its Philippines business in the quarter. We trimmed the position as price appreciated, but the stock remains well below our appraisal.

While our Dell options detracted from second quarter performance, the position remained a top contributor for the first half, with the underlying stock appreciating 33%. In the recent quarter, the stock fell as uncertainty increased over the outcome of the proposed management buyout. We continued to work with Carl Icahn to propose a better alternative for shareholders. Given his structure, flexibility, and capital, Icahn was in the best position to lead the development of an outcome that provided an attractive payout but allowed shareholders to remain owners and benefit from the company’s transformation. Subsequent to quarter-end, the Dell Board has extended the vote on the buyout offer three times as it became obvious that shareholders would not approve the deal. Prior to the third postponement, Michael Dell and Silver Lake increased their offer to $13.75 and included a special dividend of 13 cents plus the normal third quarter 8 cent dividend. Southeastern continues to oppose the offer and will work with Icahn Enterprises to ensure that Dell has the right leadership who will focus the company on its profitable and growing enterprise business while allowing long-term shareholders to participate in its long-term success.

Global cement company Cemex added to results as our convertible bonds returned 22% in the first half. Toward the end of the second quarter, we repurchased a small position in Cemex convertible bonds, which we sold earlier in the year after tightening spreads and a rising equity price pushed the price to our appraisal. More recently, the converts became attractive when investors broadly fled emerging markets, the peso weakened, and the Mexican government paused infrastructure spending. Longer term, we believe Mexico public improvements will increase, and Cemex also will benefit from recovery in the U.S.

Hochtief was another top performer in the first half, adding 14%. The company announced the sale of its airport assets and services business for prices significantly higher than our appraisals of the assets. Management announced its intention to repurchase 6% of the company and to increase Hochtief’s stake in publicly listed Leighton, the Australian construction firm. ACS, the Spanish construction and engineering company, benefitted from the positive news at its Hochtief subsidiary, and appreciated 13% in the second quarter. We trimmed the position as the stock moved higher.
Brazilian iron ore company Manabi was the largest detractor over both the quarter and first half. We lowered our carrying value after evaluating a variety of factors, including a small ownership stake sold by an investor at our original cost. Management is working to secure the infrastructure needed to enable the company to monetize its high quality iron ore.

Our positions in both Hong Kong and China real estate developer Henderson Land and Hong Kong-based conglomerate Cheung Kong were among the detractors for the first half, declining 4% and 9% respectively. As discussed in last quarter’s letter, these stocks declined due to worries over Chinese and Hong Kong real estate prices, particularly with government efforts to cool property markets with new taxes and regulations. Both companies have an extremely low cost basis in the real estate they own, and only a small portion of their values come from their undeveloped land banks. In early July, the Hong Kong government announced plans to develop agricultural farmland, a move that could greatly increase the long-term value of Henderson, which is a primary land owner in the area. Cheung Kong owns developed real estate, ports, health and beauty retailers, energy and infrastructure assets, and telecommunications businesses around the world. Both we and Chairman Li Ka-Shing bought more Cheung Kong in the quarter.

We took advantage of increased market volatility late in the second quarter by purchasing three new positions and adding to two existing holdings. As discussed above, we bought Cemex Converts. We purchased News Corp, another company we have owned previously. As the company split out the U.S. Fox entertainment business, we had the opportunity to own the remaining strongly financed, premier media assets around the world at an attractive discount. We also bought UGL, which trades at multiples similar to engineering construction businesses. The primary value of this Australian company, however, is in its property services business, DTZ.

We trimmed a number of positive performers in the quarter, including Melco, ACS, Ferrovial, and Nidec, which we fully exited after quarter-end as the stock approached our appraisal. Our small position in this Japanese maker of electric motors rallied 17% in the quarter after management confirmed sales and margin targets following a major restructuring.

Recent volatility has both reduced the Fund’s P/V to the mid-60s% and provided the opportunity to invest in new qualifiers and fill out a few positions. Although the stated cash position appears high at 24%, almost half of the cash offsets leverage inherent in the options and swaps we own, and approximately 5% is set aside for a new name we are buying. We believe the companies we own can outperform over time given the strength of their businesses and their capable management teams. We will take advantage of any additional volatility to enhance our positions, while remaining disciplined on pricing.

YTD, one and five year results outpaced the Index.
Longleaf Partners International Fund produced strong relative and absolute performance in the first quarter, returning 7.2% vs. the EAFE Index’s 5.1%. The Fund’s cumulative returns since inception have almost tripled EAFE returns.

Cumulative Returns at March 31, 2013

<table>
<thead>
<tr>
<th></th>
<th>Since Inception 10/26/98</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>One Year</th>
<th>1Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>227.88%</td>
<td>136.16%</td>
<td>-1.03%</td>
<td>16.53%</td>
<td>7.19%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>82.05</td>
<td>152.23</td>
<td>-4.36</td>
<td>11.25</td>
<td>5.13</td>
</tr>
</tbody>
</table>

See page 18 for additional performance information.

Most holdings had positive performance in the first quarter, with many producing double-digit returns. Macau gaming company Melco International was the top contributor, adding 37% in the quarter. Subsidiary Melco Crown completed an IPO of its Philippine project, Belle Grande Manila Bay, with an implied value of US$1.5 billion – over twice our carrying value of US$700 million. We have partnered with a proven owner-operator in CEO Lawrence Ho, who owns 49% of Melco International.

Dell stock was up 42% as Michael Dell and private equity firm Silver Lake proposed to take the company private. To see more on the reasons we are fighting the buyout offer, please see the Partners Fund discussion on page 4.

Philips gained 13% as the company grew revenues and margins in its three core businesses of Healthcare, Lighting, and Consumer. Philips sold its consumer electronics business and is dropping “Electronics” from the corporate name to better reflect its lighting, healthcare, and well being focus.

Global cement company Cemex returned 13%, and we sold our converts which we exchanged for our equity stake last year. These convertible bonds benefitted from both tightening spreads and a rising equity price, which rose to over $12 in the quarter from its low of under $3 eighteen months prior. While our appraisal took a hit in the economic crisis, Lorenzo Zambrano and his team did admirable work in restructuring the company to manage its debt and reduce costs in response to demand levels at half of peak.

Hochtief, the construction and engineering company, rose 13% in the quarter. Management conservatively lowered guidance and stated that the focus for this year will be on asset disposals, with profitability improvements in the core businesses coming through in 2014. Leighton, in which Hochtief holds a 54% stake, announced the sale of the bulk of its telecommunications business at an attractive price.

Only a few names were detractors in the quarter, with most down only slightly. Our positions in Hong Kong and China real estate developer Henderson Land and Hong Kong-based conglomerate Cheung Kong both declined 4%. Broad fears over Chinese and Hong Kong real estate prices impacted each company. Both Henderson and Cheung Kong have minimal financial leverage, and despite heavy government crackdown on prices, including increased mortgage rates and stamp duties, each company has low cost inventory that will enable them to profit even at much lower real estate prices. Cheung Kong actually raised its sales targets, expecting to sell 30% more Hong Kong residential property than last year. Cheung Kong Chairman KS Li and Henderson Chairman Lee Shau Kee are personally buying shares at their respective companies.

Spanish construction and engineering firm ACS fell 7% in the quarter, as negative macro sentiment in Spain overshadowed company improvement, and the market waited for planned non-core asset sales, which will further deleverage the company. ACS sold its
transmission lines. Core operations continued to generate free cash flow. HRT, the Brazilian oil and gas exploration and production company, declined 29% in the first quarter. We have actively worked to improve governance at HRT over the past year, but the stock price is unlikely to rebound significantly without successful drilling results or signing a major partner. After quarter-end, John Willott from Exxon was elected the new independent Chairman at the Annual General Meeting.

After a period of strong performance, we sold four positions and trimmed an additional four. We exited Irish drinks company C&C Group as its price reached our appraisal. Our management partners – first CEO John Dunsmore and later CEO Stephen Glancey and CFO Kenny Neisen – created and realized intrinsic value by successfully managing through a challenging economic environment in the core markets of the UK and Ireland and deftly pursuing key acquisitions. Our results at C&C highlight the benefits of partnering with shareholder-oriented management teams who think and act like owners.

We also sold Accor as its price neared appraisal value. As discussed above, we sold the Cemex converts, and we sold Willis as its price rose. We initiated a new position in European shipping logistics company, TNT Express. We also added to EXOR and Fairfax.

With a price-to-value ratio in the mid-60%, the International Fund portfolio remains attractively discounted. Recent price appreciation has limited our ability to find new qualifiers and fill out some of our positions. Cash rose during the quarter, but the reported 26% level is higher than what we have to invest given our participation in the pending Orascom offering. General market volatility or individual company disappointments will eventually provide opportunities that meet our criteria. As we wait, values across our 20 existing holdings should grow given their strong market positions and financial strength, as well as management partners who are large insider owners.
International Fund Management Discussion

Longleaf Partners International Fund ended 2012 on a strong note, returning 8.3% in the quarter and 21.2% for the full year. The Fund outperformed the MSCI EAFE Index over both periods, which returned 6.6% in the quarter and 17.3% in the year. The Fund’s returns since inception have more than doubled EAFE returns.

Cumulative Returns at December 31, 2012

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>One Year</th>
<th>4Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund (Inception 10/26/98)</td>
<td>205.87%</td>
<td>21.23%</td>
<td>8.31%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>73.16</td>
<td>17.32</td>
<td>6.57</td>
</tr>
</tbody>
</table>

See page 18 for additional performance information.

Most holdings positively performed in the quarter and for the year, with some of the strongest returns from those companies that became most heavily discounted and hurt Fund performance in 2011. Our cement and aggregates holdings – Lafarge and Cemex – were the top performers for the year and among those in the fourth quarter. When macro fears about global growth and sovereign debt caused stocks to tumble in the third quarter of 2011, Lafarge and Cemex fell as the timing of a construction rebound grew more uncertain. While we did not know when infrastructure, housing, and commercial building investment would turn, we felt confident that over five years, our companies’ unit sales and pricing would improve. We took the opportunity to buy more stock near the lows, and in 2012, Lafarge added 82% and Cemex added 80%. Both companies benefitted from positive company-specific results, as well as increased pricing trends and more positive sentiment regarding U.S. housing, infrastructure spending, and global construction. Lafarge plans to accelerate the company’s cost savings and to sell additional assets in 2013. Cemex management successfully reduced and renegotiated debt terms without diluting shareholders, continued to cut costs, and IPO’d part of the growing Latin American business. We trimmed both holdings in the quarter, but they remain discounted with significant potential for value growth.

As the result of a second round of financing at a price higher than our carrying value, Manabi returned 84% in the year, making it a top contributor. This Brazilian iron ore company has tier one assets with a concentration in the highest quality resources. CEO Ricardo Antunes is an owner with a team of experienced operators and independent board members. C&C Group, the Irish cider company, returned 30% in the quarter and 68% for the year after reporting strong cider performance outside of Ireland and solid sales and margin growth from Tennent’s beer. C&C acquired Vermont Hard Cider, the largest cider maker in the U.S. We trimmed C&C as price appreciated over the last three months. We sold Ingersoll-Rand, the global industrial firm, early in the fourth quarter after it rose 52% as management paid down debt and returned capital to shareholders through buybacks and dividends. Macau gaming company Melco International returned 30% in the quarter and 57% in 2012, as subsidiary Melco Crown’s mass market operations, particularly at the City of Dreams property, drove growth in revenues and profitability. Because casinos must share VIP revenues with junket operators, the mass market has higher margins. This customer base now comprises two-thirds of Melco Crown’s EBITDA and should continue to increase. Melco has an attractive pipeline of gaming projects in Studio City (Macau) and Belle Grande Manila Bay (Philippines).

Several of our European holdings that declined earlier in the year rebounded in the fourth quarter. Infrastructure company Ferrovial returned 22% in the recent period and 35% for the year after reporting revenue and traffic growth at the Canadian ETR-407 toll road and at Heathrow Airport Holdings. Ferrovial sold an additional 10.62% of Heathrow to Qatar Holding for a price that supports our appraisal. The company also announced two new public-private infrastructure deals in the U.S., a Texas highway and a Virginia toll road. Management returned capital to shareholders with a special dividend in December. We trimmed the position in the quarter. ACS, the Spanish construction and engineering firm,
rebounded 22% in the quarter following positive developments at Hochtief, the German construction company in which ACS holds just over 50%. Hochtief reported solid results and announced the promotion to CEO of COO Marcelino Fernandez, former CEO of ACS’s Dragados construction arm. Hochtief benefitted as public holding Leighton completed its unprofitable Victorian desalination project, easing fears of further cost overruns. Leighton also sold its waste management business and is auctioning its telecom business. After adding to ACS near its low in the first half, we trimmed the position in the fourth quarter following its rebound.

While most holdings rose in 2012, a few companies detracted from performance in spite of fourth quarter gains. Our Dell options added 2% in the final quarter but fell 53% for the year. We wrote at length in the third quarter report about the End User Computing (EUC) segment’s decline as PC and notebook sales fell. Even though the higher margin Enterprise Solutions and Services (ESS) business grew, overall top line declined as EUC was a larger percent of Dell’s revenues. Over time these two divisions will trade places in terms of revenue importance, reaping higher margins and stronger long-term growth for Dell. Post year-end, the stock is up significantly following an offer to take the company private. Brazilian-based oil and gas exploration and production company HRT returned 5% in the fourth quarter, but remained a top detractor for the year after declining 62%. Positive developments in the second half included a letter of intent with Petrobras to monetize Solimoes Basin gas, a farm in deal for 14% of Namibian assets, and the appointment of a majority of new independent board members. This progress, however, was not enough to overcome the dearth of oil discoveries.

During the fourth quarter several names detracted from the Fund’s strong results. Japanese home furniture and fashion company Nitori declined 21% in the quarter and for the year after reporting disappointing same store sales. The home furnishings industry in Japan experienced similar sales declines on the back of unusually hot weather and depressed housing starts. Nitori’s same store sales rebounded late in the quarter, and management reiterated its operating income forecast for the 2013 fiscal year.

In a year of strong performance, we sold seven holdings and trimmed an additional twelve. We bought six new positions, three in the most recent quarter, and added to six existing names in 2012. Exor, the Agnelli family holding company led by Chairman and CEO John Elkann, owns public stakes in competitively positioned businesses, including Fiat Industrial, Fiat Auto, and SGS. Management has opportunistically bought in shares at a discount and is focused on driving value creation at Exor’s underlying businesses. Elkann sits on the boards of Fiat Auto and Fiat Industrial and appointed Sergio Marchionne to oversee the restructuring of these two businesses. We also bought Fiat Industrial, a global leader in agriculture machinery and commercial truck manufacturing. Over 60% of profits come from North and South America through its 88% stake in agricultural equipment business CNH Global. CNH has a comprehensive product offering with a strong distribution network in an oligopolistic industry with pricing power. Fiat Industrial is in the process of merging with the remainder of CNH Global and plans to list the company on the NYSE and move from Italy to the Netherlands to lower its cost of capital and reduce taxes. After we initiated our position in Fiat Industrial, CNH became a cheaper entry point to purchase the same assets. We bought a 1% position in CNH, which we view as a single position with Fiat Industrial. We also initiated a partial position in Nidec, a leader in brushless motor technology that is more energy efficient, quieter, and smaller than conventional motors. This Japanese company serves the commercial, industrial, and auto space, and has over 70% market share in global brushless spindle motors for hard disk drives. We are partnering with the founder and largest shareholder, CEO Nagamori, who has a track record of building shareholder value.

Even after the gains in 2012, the portfolio trades at a price-to-value ratio in the mid-60%, offering attractive upside. Although we do not know when values will be recognized, we believe that – like at Cemex and Lafarge in 2011 – we own undervalued strong market leaders, with many in depressed industries positioned for recovery, and we expect to see continued value growth across our companies. Thank you for your continued partnership.
Longleaf Partners International Fund returned 10.7% in the third quarter, taking year-to-date (YTD) returns to 11.9% and beating the EAFE Index, which returned 6.9% and 10.1% over the same periods. The Fund’s results outpaced our absolute goal of inflation plus 10%. Although the last three years have reflected a substantial bias against value oriented stocks (EAFE Growth Index up 14.7% versus EAFE Value Index up 1.4%), the Fund’s since inception returns have more than doubled EAFE returns.

Cumulative Returns at September 30, 2012

<table>
<thead>
<tr>
<th></th>
<th>Since Inception</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>Three Year</th>
<th>One Year</th>
<th>YTD</th>
<th>3Q</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>182.42%</td>
<td>89.88%</td>
<td>-24.98%</td>
<td>2.94%</td>
<td>12.55%</td>
<td>11.93%</td>
<td>10.72%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>62.48</td>
<td>119.97</td>
<td>-23.60</td>
<td>6.48</td>
<td>13.75</td>
<td>10.08</td>
<td>6.92</td>
</tr>
</tbody>
</table>

See page 24 for additional performance information.

Most holdings rose in the quarter, with many producing double-digit returns, as we saw substantial progress at our companies. Brazilian iron ore producer Manabi closed a second round of funding of $300 million at a price 70% higher than our carrying value. Marking this private company up to reflect the transaction lifted the price 61% in the quarter, making it the strongest performer in the period and YTD. Manabi’s Tier One assets have a concentration of the highest quality iron ore, and the company is progressing on getting the infrastructure in place to get the assets to market. The Fund’s cement and aggregates holdings—Lafarge and Cemex—were again among top performers. Positive sentiment regarding U.S. housing, infrastructure spending, and global construction, as well as upward worldwide pricing trends helped these stocks. Our management partners at both companies took steps to build value and close the discount in their stocks’ prices. Lafarge opportunistically issued €675 million of long-dated debt at rates under 6%. The company also announced the sale of 1.6 million tons of U.S. cement capacity at a price of over $240 per ton, 20% above our carrying value of these assets. Management remained focused on cutting costs and improving margins. We trimmed our position, but even after the price rallied 22% in the quarter and 55% YTD, Lafarge trades at a significant discount to its growing value and offers attractive upside. Cemex gained 61% YTD and 24% in the recent quarter. Management successfully refinanced the company’s bank debt, extending maturities and relaxing covenants, without diluting shareholders. Cemex also announced plans to IPO a portion of its Latin American business. With the stock’s large gains, we trimmed our position by selling the remaining equity and some of the convertible bonds.

Henderson Land was another top contributor for the third quarter and for the first nine months this year. Henderson reported a strong half, with 14% rental income growth in Hong Kong and 33% growth in China. China residential sales rose 82% year-over-year. In September, Henderson launched Double Cove, the first of its large scale mass residential developments in Hong Kong, and received government approval to launch the second development, The Reach, in October. Chairman Lee Shau-Kee purchased over $10 million and took his ownership stake to over 62%. We trimmed the position after strong performance. Cheung Kong also contributed in the quarter after reporting solid results across all segments. The Chinese property development business had 51% margins and sold 2.5 million square feet at HK$2000 per square foot in the last half, highlighting Cheung Kong’s premium brand and low land cost in China. The Chinese residential property sale business is growing rapidly, despite pessimism about China. Additionally, Hong Kong property met targeted sales for the half with operating margins above target. At Cheung Kong holding Hutchison Whampoa, revenues and EBITDA grew in every segment, including those in Europe. Retail had organic revenue and margin growth; ports grew EBITDA 8%, reflecting good operating leverage and cost controls; investment properties and hotels saw year-over-year gains; European telecom increased EBIT by 66% in the half with an improved mix of customers, larger share of smart-phones, and strict cost controls. Cheung Kong Infrastructure revenues and profits grew, primarily due to the Northumbrian acquisition last year. The primary takeaway about Cheung Kong is that in spite of good reports from its broad base of businesses, the stock remains discounted because most investors focus only on the macro concerns around its Chinese real estate. Ingersoll-Rand had another positive quarter and was among top performers for the year, up 50%. Management repurchased approximately 6% of shares YTD.
The price-to-value of the portfolio remains attractive in the high-50%s.

A handful of companies declined in the third quarter. Dell fell 21% over the last three months, and the stock’s 33% retreat in 2012 made it the primary detractor to the Fund’s performance for both periods. The primary challenge over the last two quarters was a larger-than-expected decline in End User Computing (EUC) revenue due to several pressures. Tablets and other mobility devices displaced notebooks more rapidly than anticipated; demand in India and China shrunk, and Lenovo aggressively priced to take share in these geographies; and commercial purchases slowed because of general economic weakness and the anticipated release of Windows 8. In spite of the decline in notebooks and PCs, margins held up in EUC, a testament to the company’s successful cost cutting and variable cost structure. Far more importantly, the growing, higher margin Enterprise Solutions and Services (ESS) business had strong networking and server growth with servers gaining market share. While ESS represents about one-third of revenues, it constitutes over half of profits and a far higher share of our appraisal. The company’s transformation to a solutions-based company is well underway and leverages Dell’s direct distribution advantage of over 20,000 employees responsible for customer relationships with small and mid-size businesses. Interestingly, IBM successfully refocused its business over a ten year period starting in the early 1990’s from mainframe hardware to multifaceted technology solutions for large-scale customers. The head of IBM’s mergers and acquisitions was Dave Johnson, who joined Dell in 2009 to lead its strategy to enhance solutions offerings and has purchased a number of companies and products that have grown through Dell’s expansive distribution. If we assume that EUC continues its rapid decline and has no value, we appraise the remaining ESS business at over twice the current stock price. With adjusted cash earnings of $2.00/share and an enterprise value of less than $3.50/share (share price minus net cash and DFS), the stock trades at less than a 2X adjusted P/E for a growing business (ESS) with good margins and an owner/operator as CEO who is focused on growing value per share.

Brazilian-based oil and gas exploration and production company HRT fell 29% in the third quarter and 64% in the year. As discussed in last quarter’s report, HRT has faced a perfect storm of pressures – both macro and company specific. The primary reason for the decline this quarter was competitor Chariot’s reported dry well in Namibia, which is geologically distinct from HRT’s potential reserves. We became more active at HRT and worked with management to expand the board from nine to eleven members and add seven new directors. We believe the new majority independent board will take the necessary steps to improve operating costs, increase the probability of drilling success, and realize value of the leasehold positions in Namibia and Solimoes. Anglo American declined in the quarter with lower commodity prices. After management bought a bigger stake in iron ore miner Kumba at a large premium to our appraised value, we sold the position.

ACS declined 4% in the quarter and lost 13% for the year, making it one of the largest YTD detractors. ACS fell 26% in the month of July amid uncertainty around the Spanish government’s plans to tax all power generating assets, calling into question ACS’s ability to sell its thermal and solar wind parks. ACS also faced questions around its stake in Iberdrola (IBE), which we discussed in the second quarter report. The stock rebounded after management refinanced the loans on IBE shares, freeing the cash collateral and capping downside risk in the IBE share price. Additionally, the Spanish government quantified the energy production taxes at less onerous rates than feared, making near-term sales of ACS renewable assets more feasible.

As discussed in last quarter’s report, we sold Carrefour, among the top detractors for the year, after our case changed. We also sold our small stake in Vivendi as price rose following the board’s decision to sell segments and after the company’s inability to sell its Activision games stake caused us to lower our appraisal based on this business’ market price. We trimmed six names to manage position sizes after positive price performance. We added to heavily discounted Asian gaming companies, Genting and Melco.
International Fund Management Discussion

Even after a period of strong performance, the price-to-value of the portfolio remains attractive in the high-50% s. We believe the companies we own are well positioned to outperform, even in a challenged economic environment. In many cases, prices do not reflect positive fundamental progress and smart decisions by management because macro worries overshadow the market’s short-term outlook. We are confident that our capable management partners will build and highlight value to the market over time. We continue to find opportunities and have a number of vetted on-deck ideas. We will remain disciplined on price.
Longleaf Partners International Fund declined 9.3% in the second quarter, but remains positive year-to-date with total a return of 1.1%. The EAFE Index fell 7.1% over the last three months and is up 3.0% in 2012. Recent returns have weighed on our medium-to-longer-term relative and absolute performance, but the Fund has almost tripled the return of the benchmark since inception.

**Cumulative Returns at June 30, 2012**

<table>
<thead>
<tr>
<th></th>
<th>Inception</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>Three Year</th>
<th>One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>155.06%</td>
<td>37.90%</td>
<td>-31.65%</td>
<td>7.32%</td>
<td>-22.31%</td>
</tr>
</tbody>
</table>

See page 24 for additional performance information.

Broad market declines as well as a handful of short-term, company-specific disappointments generated negative performance in the quarter. Companies with exposure – perceived or real – to Europe, cyclical industries, and/or commodity prices were negatively impacted as fear of global economic challenges and political uncertainty drove stock prices. The first two quarters of 2012 illustrate the volatile “risk on, risk off” nature of markets today. In the first quarter a burst of risk appetite helped many of our most heavily punished holdings from 2011 rebound significantly. Just as quickly, fear reclaimed investors, and those stocks lost ground. Each of the Fund’s top five contributors this year had strong first quarter returns, but four gave back a portion over the last three months. Despite the rapid price movements, most of our appraisals held steady or grew because our models assumed slow growth over the next few years and revenue declines in Europe through 2014.

Ingersoll-Rand, up 40% year-to-date, was the top contributor in the half after a strong first quarter. Unlike many of its industrial peers, Ingersoll-Rand made gains in the quarter. The company reported order growth, solid revenues, and good margins in its most important segments. Additionally, Trian took a 7% stake in the company with intentions to drive value recognition. Given the stock’s strength and portfolio overweight, we trimmed our stake. After a 13% decline over the last three months, Cemex has gained 30% in 2012. The peso’s recent weakness impacts the translation of Mexican earnings into dollars. Aside from currency fluctuations, results have been strong this year with increased volumes in the U.S. and South America and solid pricing in Mexico. The U.S. has turned EBITDA (earnings before interest, taxes, depreciation, amortization) positive for the first time since 2008, and the recent two year federal road bill extension will unlock needed funds for highway projects. Additionally, Cemex and the banks that comprise half of its debt were renegotiating and extending terms at quarter end. We exchanged some of our equity for convertible bonds to take advantage of the opportunity to move up the capital structure at an attractive yield to maturity and conversion price. We maintain a large percentage of Cemex’s upside while dramatically decreasing downside risk.

LaFarge added 27% in the first half after cement volume and price gains in all regions except for Western Europe, which was flat. Margins are growing as management focuses on higher capacity utilization and cost reductions. We sold short-term covered calls that pay an attractive premium for selling shares at a price where we would trim the position anyway given recent appreciation and portfolio weighting.

Accor gave back 8% of its first quarter gains in the last three months but added 29% for the YTD. As Europe’s largest hotel operator, Accor has the highest exposure to the European consumer in the
Given its dominant position in the economy hotel space, Accor has attracted travelers trading to lower end brands and demonstrated the strength of its moat with strong results during the 2008-2009 downturn. We trimmed the position early in the quarter and realized an attractive premium in selling the related covered calls.

Henderson Land, which we began acquiring late in the first quarter, is one of Hong Kong’s largest property developers and was the top contributor to the Fund’s second quarter performance. Chairman Shau Kee Lee’s family owns 61% of the company, and he personally has bought over HK$750 million in shares this year and HK$13.6 billion (US$1.7 billion) in 2011. Henderson Land’s 40% stake in publicly listed utility Hong Kong & China Gas accounts for about 54% of the stock price of Henderson Land, creating a significant discount in the price of the company’s residential and commercial property investments in Hong Kong and China. While Henderson sells at a discount due to general fear over Chinese real estate, HK & China Gas trades above fair value, benefitting from the flight to stability found in utilities. To isolate the value of the undervalued property business, we shorted out our exposure to Hong Kong and China Gas. In the quarter we added to this paired trade which we own via a swap with cheap financing through a single counterparty.

ACS, the Spanish infrastructure and construction company, rallied 32% from its low on May 16 but remained the largest detractor from year-to-date performance, down 26%. Spain’s main index, the IBEX 35 where ACS is listed, contains 35 companies, many with low free float. As a result, ACS has become a proxy for shorting Spain and faces macro-related headwinds. In the second quarter, the company’s energy related assets weighed on the stock when the Spanish government announced plans to levy taxes on all power generating assets but offered no specifics. The media has suggested that onerous taxes will be placed on both nuclear power and renewables. Until the government provides clarification on renewables taxes, ACS is unlikely to close sales of its remaining thermal solar and wind parks.

Additionally, the uncertainty provoked an intense selloff in all Spanish energy companies, including Iberdrola (IBE) where ACS is the largest shareholder. IBE’s decline created concern that banks would call in the loans ACS held against its IBE stake. To reduce the threat, in April ACS sold just under 4% of Iberdrola at €3.60/share. The sale, however, exacerbated worries that the company would have to sell its remaining 15% in IBE at a discount. After quarter end, ACS announced that it refinanced the loans on its IBE stake, freeing the cash that was held as collateral and capping any further downside risk in the IBE share price below €3.00 per share. Eliminating IBE price risk and limiting upside was preferable to selling the position at a severely discounted market price. While ACS management’s overall capital allocation record has rewarded long-term shareholders, IBE has been a costly mistake. ACS’ other equity holding, Hochtief (HOT), fell 20% in the quarter and impacted both ACS’ price as well as the Fund’s results since we own a direct position in HOT. In addition to concerns over whether ACS could become a forced seller of its 50% stake in the company. Hochtief management has yet to deliver on its promise to focus on core operations and sell stakes in six airports and non-core real estate assets. The company sold its Chilean toll road at an attractive price in the second quarter. After deducting the market value of HOT’s 55% stake in publicly traded Leighton (the Australian contract mining and engineering company) from HOT’s price, the company’s remaining assets sell for €4.50/share, a fraction of the combined worth of its airport stakes, concession assets, real estate, and core operations. We took advantage of the market’s irrational undervaluation to increase our stake.

Brazilian-based oil and gas exploration and production company HRT fell 55% in the second quarter under a comprehensive storm of pressures – first, the Brazilian stock market dropped 24% (in U.S. dollar terms); second, the price of oil fell 19%; third, drilling results on HRT’s 6th Brazilian well showed oil that is uneconomic to procure; and fourth, another firm drilled a dry hole in Namibia, albeit in a different basin from HRT’s blocks without direct read
International Fund Management Discussion

across. However, production is several years away, and current oil prices are above the marginal cost of production. HRT’s acreage includes land that is already producing oil for Petrobras, and the $1 billion that TNK-BP paid for a 45% stake in the Brazilian assets indicates the longer term demand for these reserves. In Namibia, majors are showing increasing interest, and the geological data is promising. The severely discounted stock trades for its net cash, giving investors the Brazilian wells and Namibian leases free.

Dell fell 25% in the quarter making its 2012 return -15%. Disappointing earnings were primarily driven by a steeper decline than anticipated in notebook revenues. We lowered our appraisal to reflect slower notebook revenues and adjusted margin growth in the enterprise business to account for a larger sales force and the time lag to fully integrate acquired products. Our new appraisal equates to the company’s value a year ago. Results in the quarter supported the overall case for Dell transforming from low margin, declining hardware to growing, higher margin solutions. Enterprise grew 5% and represented over half of adjusted operating income. The broader migration to mobile and cloud computing will accelerate the transition pace. Michael Dell is one of the most vested and engaged CEOs we have as a partner. The company repurchased shares at a 4% annualized rate. Dell trades at less than 4.5 times free cash flow adjusting for the net cash.

Carrefour declined 23% in the quarter. The company’s core French and European business continued to suffer under economic headwinds and increased competitive challenges. New CEO Georges Plassat brings an impressive pedigree to the task of turning around this European retailer but faces a brutal environment. As our discipline dictates for a name whose value has declined significantly, we reassigned coverage to take a fresh look at our Carrefour case. Our original appraisal underestimated the complexity and time needed to turn around the French and Spanish hypermarkets. While then-CEO Lars Olofsson had excellent credentials from his time at Nestle, his lack of retail experience combined with the challenges of turning around the European business of Carrefour, proved that he was not the right person for the job. A large part of our margin of safety rested in the underevaluation of Carrefour’s French real estate and non-core geographies. While Plassat has indicated his willingness to shrink the company’s footprint and rationalize real estate in core markets, economic conditions are likely to prolong progress. The stock remains discounted from its long-term value, but the company’s outlook will likely get worse before improving. We determined that Carrefour no longer meets our criteria and completed the exit after quarter end.

We sold our Colgate-Palmolive option positions and added two new qualifiers, Vivendi and Anglo American, both which we have previously owned. Colgate, which we held via a five year “risk reversal” that gave us upside in the price over $80/share and an entry price of $65 if the stock traded down to that level, was around $77 when we took the position in early 2011. Because of low interest rates and the stability of this dominant oral and personal care products company, the net cost for our long exposure over $80 was only $3.50/share. We closed out the position for approximately $18.50/share because the stock approached full value based on our DCF model. Vivendi moved out of our buying range soon after we started the position when the company announced that its CEO, who was thought to be against monetizing the company’s undervalued assets, stepped down due to differences over strategy. We initiated a position in Anglo American, a global leader in iron ore, diamond, and precious metals mining. While Anglo American trades at a large discount to value, its public stake in iron ore miner Kumba sells at a premium. To increase our margin of safety, we bought a long position in Anglo American and shorted our exposure to Kumba. This trade was similar to our previous ownership of these assets in 2000 when we bought DeBeers (the diamond business) and shorted our exposure to the company’s overvalued public stake in Anglo American (the base metals business).
Several recent purchases and sales have involved swaps or options. While we have opportunistically owned positions other than long equity securities in the past, the combination of low financing costs and high premiums associated with volatility has increased the attractiveness of various investment structures. When interest rates rise and/or markets become less volatile, these derivative structures will likely become less attractive relative to owning the straight equity.

We own a collection of competitively entrenched businesses managed by shareholder-oriented, owner-operators. The price-to-value ratio of the portfolio is in the high-50%s, below the long-term average. Many of the European and more cyclical businesses that are among the most discounted names in the portfolio are best positioned to drive long-term outperformance. The portfolio management team invested a substantial amount into the Fund in the second quarter to take advantage of the compelling opportunity.
International Fund Management Discussion

Longleaf Partners International Fund had strong absolute and relative returns in the first quarter, gaining 11.51% versus EAFE Index’s 10.86%. Although 2011 results have weighed on performance for all periods through this quarter end, the Fund has almost tripled the benchmark since starting in 1998.

Cumulative Returns at March 31, 2012

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<th>Inception</th>
<th>One Year</th>
<th>1Q</th>
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<tbody>
<tr>
<td>International Fund</td>
<td>181.36%</td>
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<td>11.51%</td>
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<tr>
<td>MSCI EAFE Index</td>
<td>63.63</td>
<td>(5.77)</td>
<td>10.86</td>
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<tr>
<td>Inflation + 10%</td>
<td>392.90</td>
<td>12.63</td>
<td>na</td>
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See page 24 for additional performance information.

Most companies appreciated in the first quarter, and almost half of the portfolio holdings recorded double-digit gains. Many of the strongest performers were the companies that became most heavily discounted and hurt Fund performance in 2011.

The Fund’s materials holdings — Cemex and Lafarge — were the top contributors in the quarter, appreciating 50% and 36% respectively. Cemex had a fifth consecutive quarter of top line growth thanks in part to price increases in most markets, as well as demand growth from infrastructure and housing improvements. Improved margins reflected lower energy costs and overall expense reductions. For the first time in four years sales and EBITDA grew in 2011. The company expects no debt covenant issues in 2012 given successful asset sales, and in February Cemex made an exchange offer for approximately $2 billion of debt, which will lower absolute debt levels, push maturities further out while reducing dependence on bank financing, and provide more flexibility with banks. Lafarge reported volume growth in emerging markets and stabilization in the U.S. Aggregates results met expectations, and pricing was strong. Management remains focused on cost cutting and is aggressively reducing debt with plans for another €1 billion of divestitures this year. Cemex and Lafarge have different underlying geographic exposures and value drivers. Cemex has significant U.S. exposure in addition to its strength in Mexico and South America, while Lafarge operates largely in the Middle East and numerous emerging markets.

Recent asset sales by Holcim, the third major player in the global cement market, and Cimpor, a Portuguese cement company, were at prices in line with or higher than our per ton and discounted cash flow values for Lafarge and Cemex. Even after a six month stock rally, both companies trade at steep discounts to our appraisals.

Ingersoll-Rand’s price rose 36% after reporting strong performance and guidance, driven primarily by climate solutions and industrial technologies. Management is focused on paying down debt and returned capital to shareholders through share buybacks in 2011 and an increased dividend in 2012. C&C Group appreciated 38% after reporting stronger than expected growth in domestic and international markets, with international becoming a more significant part of its mix. Tennets beer strength offset cider pressure in Ireland and kept overall results for the country flat. MillerCoors’ acquisition of the number three U.S. cider brand increased attention on premium cider’s global potential. Accor’s price was severely punished in 2011 due to fears that this European hotel company would face pricing and occupancy challenges in a recession. However, half of Accor’s earnings come from Economy hotels, which benefit in a period when travelers switch to lower priced rooms. Additionally, Accor controls 80% of the economy hotel market share in France, giving it significant pricing power. Accor appreciated 41% in the first quarter after
Most companies appreciated in the first quarter, and almost half of the portfolio holdings recorded double-digit gains.

reporting increased revenue-per-available room (RevPar) in the second half of 2011. We trimmed the position as price appreciated.

ACS, Ferrovial, and Philips declined in the quarter primarily based on economic uncertainty in the Eurozone, which we believe faces near-term challenges. Each company, however, has limited exposure to the European consumer and has significant, growing value in non-European markets. ACS declined 11% primarily due to questions around its equity stake in Spanish utility Iberdrola. The Spanish utility industry fell on speculation that the government would levy a windfall tax on the industry. While this tax is essentially neutral from an appraisal standpoint, both ACS’s and Iberdrola’s prices were heavily impacted. In the weeks after quarter end, concern around Iberdrola peaked after ACS sold 3.7% of its holding at €3.60 and used proceeds to reduce debt against its remaining 14.8% stake. ACS maintains its strategy for Iberdrola to play a part in the coming consolidation of the European energy sector. ACS’ previously stated 2012 plan of selling non-core assets should add to ACS’ sizeable cash cushion, offset its capital loss on Iberdrola, and prevent any additional sales at discounted prices. The Iberdrola sale reduced our ACS appraisal by 5%, but our outlook for the company has not changed, and the stock sells for below 40% of value.

Ferrovial declined 5% in the quarter, not because the underlying business fundamentals have deteriorated, but because the company is located in Spain. Ferrovial had better-than-expected results in all divisions, including construction and services, as well as at BAA and Cintra, which owns the ETR-407 toll road in Toronto. BAA increased traffic and tariffs across its airports and agreed to pay out £240 million in dividends in 2012, of which 49.9% will flow through to Ferrovial. In April, BAA sold the Edinburgh airport for £807 million, or 17X trailing EBITDA, highlighting the discounted value of BAA. The ETR-407 toll road increased tariffs by 8.5% and paid out C$460 million of dividends in 2011 to its owners. The outlook for Spain does not need to improve for Ferrovial’s value to be recognized. Management will continue to create value through its asset rotation plan and is returning capital to shareholders through a dividend. Philips declined 3% in the quarter as the company reported EBITDA approximately 5% below consensus expectations, primarily due to one-time issues in the healthcare and lighting segments. Although management firmly expressed a commitment to 2013 targets based on reduced costs and global GDP growth of 3%, their cautious stance on first half 2012 results and the concurrent buyback plan extension compounded skepticism over what the company will deliver. Western Europe’s economic challenges are likely to last for some time, but this area generates less than 30% of revenues. Philips’ consumer brands as well as its medical and lighting businesses are dominant and growing in emerging markets, which account for over one-third of revenues and should dwarf Europe’s importance to the company’s results over time. Fairfax lost 4% as catastrophes in the fourth quarter hurt underwriting results. Book value also declined reflecting dual investment challenges of being 100% hedged in a rising stock market and having several weak underlying investments. The first quarter of 2012 will likely suffer from the same dynamic. In spite of these recent challenges, Prem Watsa remains one of the most skilled long-term investors we know, and we are partnering with him at an attractive P/V of less than 70%. Willis declined 9% after the company reported lower margins following a revenue decline in North America where some of the sales force departed as non-competes from previous acquisitions rolled off.

We sold NKSJ, a disappointment that we discussed in the Annual Report. We began selling Olympus and completed the sale in April. Subsequent to our Annual Report, in which we assessed this investment mistake as well as company developments, we worked to identify and propose independent board candidates who would protect the value of the medical business and instill western corporate governance standards. We decided to sell in March when the announcement of the new president and board nominees indicated that shareholder interests would not necessarily be the primary focus once new leadership was elected in April. The
“independent” directors were weighted toward creditors with the Chairman being affiliated with Olympus’ largest creditor. Holding onto Olympus to pursue our interests after the initial fraud revelations proved a good short-term decision, as our average sale price was over 300% higher than the ¥424 low in November 2011. Over our full holding period this investment made a small positive return for which we paid a large opportunity cost.

We sold some of our Cemex shares to purchase Cemex convertible bonds that offer an attractive yield and the longer-term upside of the stock whenever global recovery moves into higher gear. We trimmed six positions as prices appreciated in the quarter and added to Genting. We also initiated one new position.

The Fund’s P/V in the low-60%s remains compelling even after the strong performance in the first quarter. The volatility in the first few weeks of April indicates a high level of uncertainty in the market, but we remain confident in the long-term prospective returns from our current portfolio holdings because of the substantial discount in prices and the value growth outlook.
Longleaf Partners International Fund returned 0.6% in the fourth quarter and (20.3)% for the year, falling short of the EAFE Index, which delivered 3.3% and (12.1)% in the same periods.

The disappointing 2011 returns negatively impacted five and ten year results, but since inception, the Fund has substantially outperformed EAFE.

Cumulative Returns at December 31, 2011

<table>
<thead>
<tr>
<th></th>
<th>Inception</th>
<th>Ten Year</th>
<th>Five Year</th>
<th>Three Year</th>
<th>One Year</th>
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<tbody>
<tr>
<td>International Fund</td>
<td>152.31%</td>
<td>33.76%</td>
<td>(22.27)%</td>
<td>11.61%</td>
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<td>MSCI EAFE Index</td>
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<td>Inflation + 10%</td>
<td>373.27</td>
<td>224.06</td>
<td>78.30</td>
<td>41.97</td>
<td>12.96</td>
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</table>

See page 24 for additional performance information.

Market volatility dominated the second half of the year with exacerbated macro fears around European default, Middle East unrest, a Chinese real estate bubble, emerging market currencies, and U.S. political and economic uncertainty. The overwhelming fear in the market offers a significant advantage for our ability to look through to the underlying value of individual businesses. Many of our companies’ prices have correlated with their broader sectors (i.e., Cemex and Lafarge thrown out with construction materials) or with their home markets (i.e., European domiciled holdings disdained for broader Eurozone concerns, Cheung Kong declining with fears of a Chinese real estate bubble, and HRT discarded with the mass exodus from Brazil). Our company appraisals incorporate the uncertain economic outlook, but our investment decisions are bottom-up and based on company fundamentals rather than top-down based on macro views. Our long time horizon and disciplined company analysis uncover compelling opportunities in macro-driven environments.

Our research team recently spent a week meeting with European management teams. While all are bearish on the near-term prospects and expect a challenged consumer, none of our investments depend heavily on European consumers. Our appraisals assume negative top line growth over the next two years in European segments. These investments, however, while having limited exposure to consumers on the continent, feature significant value outside of European markets.

Ferrovial is listed in Spain, but 80% of its business is in the UK (through its investment in BAA) and Canada (through its investment in Cintra). Similarly, ACS is categorized as Spanish construction, but 50% of its business comes from outside of Spain. Less than 25% of Philips’ revenues are European. The bulk of the value is in the medical business where 50% of revenues are in the U.S. and 30% in emerging markets. Consumer health sales are primarily in emerging markets, and the global lighting business has over 70% of revenues outside of Europe. Even Carrefour, which has been primarily challenged by disappointing results in France, derives 50% of its value from Latin America and Asia. Accor has more direct European consumer exposure, but its leading share in economy hotels benefits in a downturn as travelers switch to lower priced rooms.

In the fourth quarter, many stocks rebounded from September lows, but not enough to offset earlier declines. Diminished fears of a U.S. recession helped Cemex add 71% in the quarter, although the stock was among the worst performers for the year with a decline of 48%. Philips recovered 17% in the quarter, but finished down 29% following our purchase in the second quarter. With indications of improved insurance pricing Willis and Fairfax rose 14% and 11% respectively over the last three months. Both stocks remain at discounts to intrinsic value, but we trimmed Fairfax, the Fund’s largest position, after recent gains. Willis was also among the top contributors to the Fund’s 2011 return. The other top
contributors for the year were Edenred and Yum! Brands, both of which we sold in the third quarter.

HRT was the largest detractor in 2011 as price declined 25% in the fourth quarter and 68% for the year. HRT has faced several headwinds, starting with the price tumbling early in the spring as the lock-up on 40% of its pre-IPO shareholders expired. Later in the year macro factors pressured the stock, and the market questioned HRT’s deal with TNK-BP for 45% of its Solimoes blocks. Most recently, initial drilling results were a disappointment. Although they supported the geological case for hydrocarbons in the Solimoes basin, the low permeability and porosity of the rock will mean higher cost and time to drill than originally anticipated. The stock currently trades near the value of net cash, ignoring the company’s assets in Brazil and Namibia. ACS, another detractor, declined 17% in the quarter and 32% in 2011. Fear over European sovereign debt and economic decline pressured the stock of this global infrastructure engineering firm. Although headquartered in Spain, most of ACS’ business is outside of Europe when looking through their 50% ownership of Hochtief. The company sells for half of our appraisal, and this value should grow over the next few years even without any Spanish or European economic recovery.

The biggest disappointment in the fourth quarter was Olympus which fell 58%. The revelation that the company had been hiding investment losses for over a decade indicated an initial mistake we made in assessing management. With the appointment of Michael Woodford as CEO, we believed we had upgraded to the right partner. We were stunned when he uncovered the massive fraud. Since the first report of wrongdoing in October, the three executives most involved have resigned, the independent committee’s audit report has provided transparency, the Tokyo Stock Exchange has determined not to delist the stock, and an extraordinary general meeting has been called for April to replace much of management and the board. Our intense due diligence since learning of the fraud indicates that the investment case and underlying value of the globally dominant medical business are intact. We are pursuing various avenues to ensure that the medical division value and our rights as owners are protected. We strive to learn from mistakes and improve our process. Assessing management is the most challenging part of our analysis. Humans are more difficult to predict than businesses or financials. Owning good companies at deep discounts helps dampen the impact when we make an error. In the case of Olympus, although our ultimate return will be lower than we hoped, the large margin of safety in our purchase price should help minimize a loss even after the unforgivable fraud. We have already recouped two-thirds of our original investment when considering previously booked gains and dividends, and the current price is approximately half of our reduced appraisal. The quality of the medical business is unchanged in spite of bad partners.

While Japan remains one of the statistically cheapest markets, “cheap” is never enough, nor is “good business” without the right partners. Going forward in Japan, we must have an owner operator at the helm given the low priority for shareholder rights and corporate governance in the country.

In extremely volatile markets such as 2011, we may sell positions below full value to fund opportunities that are more qualitatively or quantitatively attractive. We sold ten positions in the year, including Hirose, Julius Baer, and Seven Bank in the fourth quarter. We trimmed five holdings in the quarter and eight positions over the year. We added eleven new investments in 2011, including Melco in the fourth quarter, and increased five existing positions at opportunistic points. We positioned the portfolio in attractively discounted, high quality businesses with management teams who are taking key steps to grow values.

Southeastern employees added significantly to their investments in the Fund in 2011. Likewise, our management teams have been heavy insider buyers and share repurchasers. Their activity reflects the compelling math that the Fund’s P/V in the low-50% implies. We thank you for your patience, and we look forward to delivering strong future returns that reward your long-term partnership.

We positioned the portfolio in attractively discounted, high quality businesses with management teams who are taking key steps to grow values.
International Fund Management Discussion

Longleaf Partners International Fund declined 23.6% in the third quarter, bringing the year-to-date return to (20.7)%%. The EAFE Index also posted negative returns over both periods, declining 19.0% in the quarter and 15.0% for the year. Disappointing 2011 returns have negatively impacted performance numbers for most periods, although since the Fund’s inception, it has more than tripled the Index.

Cumulative Returns at September 30, 2011

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<th>Inception</th>
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<th>One Year</th>
<th>YTD</th>
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<tr>
<td>International Fund</td>
<td>150.9%</td>
<td>37.6%</td>
<td>(14.9)%</td>
<td>(20.7)%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>42.8</td>
<td>63.3</td>
<td>(9.4)</td>
<td>(15.0)</td>
</tr>
<tr>
<td>Inflation + 10%</td>
<td>365.1</td>
<td>223.1</td>
<td>13.9</td>
<td>na</td>
</tr>
</tbody>
</table>

See page 24 for additional performance information.

Most holdings fell in the quarter, as macro-driven negative sentiment led to rapid price declines across all industries without regard to underlying business strength or intrinsic value. Three holdings contributed positively, including two newly purchased in the period. Japanese discount furniture retailer Nitori appreciated 7% over the last three months and 18% since our purchase. Nitori announced strong results that beat guidance by a wide margin with sales up 11% and operating income up 20%. The company has recovered from the earthquake and tsunami in March and is on track to achieve double-digit top line growth and high teens operating margins. Even in a strained economic environment, Nitori stands to benefit as consumers trade down to lower priced furniture. In August, we purchased Hirose, a Japanese manufacturer of high end, custom electronic connectors. Hirose is among the top ten companies that control over 50% of the global connector industry. 80% of its connectors are custom designed into its customers’ products. The business increased market share and maintained strong margins through the recession in 2008-09. Hirose has net cash equal to 80% of its market cap, and management has consistently repurchased discounted shares, most recently in September 2011. In late September, we bought Malaysian-based casino operator Genting, which we last purchased in the 2008 downturn and sold at full value a year ago. Mr. Market has once again provided the opportunity to partner with owner-operator KT Lim, who took advantage of the recent price decline to buy in shares. Genting’s Singapore casino is growing, and the company will open its first U.S. casino in New York this year.

Brazilian exploration and production company HRT was the largest detractor for the quarter and second largest for the year after falling 55% and 58% respectively. Early in its exploratory drilling campaign, HRT has thus far announced positive results which confirm CEO Marcio Mello’s geological assumption that the Solimoes Basin contains crude oil deeper underground. Talks with potential strategic investors in the Solimoes Field have accelerated. At the end of October, HRT announced that TNK-BP will acquire 45% of the Solimoes for $1 billion with additional upside. Independent consulting firm DeGolyer & MacNaughton increased its estimate of HRT’s certified resource volume in Namibia where Petrobras and BP each purchased blocks adjacent to HRT’s in the Orange Basin.

After significant stock declines in the third quarter, global cement producers Cemex and Lafarge were among the largest detractors from performance for the year. Cemex fell 63% and Lafarge declined 44% over the last three months. Cemex faces three primary challenges — the inability of the U.S. government to pass a long-term transportation bill covering much-needed
infrastructure improvements, low housing starts in the U.S. and other developed markets, and debt-related covenants and maturities in the next three years. The first two challenges will delay cash flows but not impair either the long-term asset values of the U.S. cement facilities and aggregates that Cemex owns or the intrinsic worth of its non-U.S. markets which represent the majority of the company’s value. The company’s assets support its debt and remain desirable to others even in this industry depression.

Management faced much more severe challenges in 2008, yet the stock has fallen to lower levels. As owner-operators management did an excellent job in the recession reducing and restructuring debt while looking out for shareholders’ interests. Management is equally focused on protecting intrinsic value while managing the business and capital structure in this depressed environment. While Lafarge faces similar pressures of a slow global economic recovery, its business is less heavily weighted in the U.S., and the company has a much lower debt-to-equity ratio. Lafarge’s emerging markets business is growing, but concerns over unrest in the Middle East continue to weigh on the price.

ACS remains widely hated due to its exposure to Spanish construction and its seemingly high debt level. 55% of ACS’ civil works construction segment is in Spain where we expect declines of 20% in 2011 and 15% in 2012. The remaining 45% of the business, however, is in other geographies where revenues are growing in the mid-teens. The waste management and industrial services segments are growing at low single-digit rates despite the depressed market in Spain. ACS’s public stakes in Hochtfief (51%), Iberdrola (19%), and Abertis (10%) all trade at a significant discount to intrinsic value. Of ACS’ €9.5 billion of net debt at 6/30/11, over 80% was non-recourse to the company, and the portion held against its concession assets is long-dated, fixed rate debt. ACS has sold over €2.6 billion in assets since the beginning of the summer, including €1.78 billion of renewable wind assets and, most recently, two Chilean toll roads sold at a 30% premium to our carrying value. Management has used proceeds to buy in shares materially and pay down debt since the second quarter.

We wrote in last quarter’s letter about the positive outlook at Olympus with Michael Woodford as the new President and CEO. The stock rose upon his appointment, and we trimmed the position early in the third quarter. We were shocked by Woodford’s dismissal in October amid his allegations about corporate governance. We take seriously his accusations and are working diligently to get a comprehensive response from the board. While the stock price is down meaningfully, none of the allegations have yet changed the value of the underlying medical business at Olympus, but they obviously have destroyed the integrity of the entire board save Mr. Woodford. We are evaluating all options and will act accordingly depending upon the board’s response.

We took advantage of short-term price volatility in the quarter to purchase high quality businesses trading at a significant discount. We sold Edenred and Yum! Brands, among the strongest positive contributors this year, recognizing long-term gains of 37% and 637% respectively. We have great respect for the management teams at both companies, who have consistently built business value for shareholders. We also sold Shanda bonds and trimmed eight other holdings to fund four new positions and add to seven existing names. In addition to the new positions in Hirose and Genting discussed above, we bought Julius Baer, which declined alongside most European financials in the quarter. Julius Baer provides private banking in Switzerland with exposure to Asia through Singapore and Hong Kong. It is the most strongly capitalized bank in Europe with a 22% Tier 1 capital trust and has no direct treasury exposure to Greek, Italian, Spanish, Portuguese, or Irish sovereign credit. Chairman Raymond Baer is a significant owner, and management announced a large share buyback plan in 2011. We also purchased Ingersoll-Rand, the world’s leading climate control company, which we sold in late 2009. The company is generating large free cash flow per share even in a tough environment for its segments. It is currently among the largest share repurchasers across the Longleaf Funds.
Although prices have declined across the portfolio, appraisal values, which are based on conservative assumptions of low or negative near-term growth, have been generally unaffected. A number of our management partners have grown values by cutting costs, buying in discounted shares, selling off assets at attractive prices, and/or paying down debt. The portfolio trades near a 50% P/V and includes high quality businesses. The short-term negative returns are disappointing, but we are excited by the long-term opportunities provided by the price volatility and encourage our partners to join us in adding to the Fund.
Longleaf Partners International Fund returned 0.8% in the second quarter, bringing the year-to-date return to 3.7%. The EAFE Index returned 1.6% and 5.0% in the same periods. Over the last 12 months the Fund more than doubled our absolute annual return goal of inflation + 10%.

Cumulative Returns at June 30, 2011

<table>
<thead>
<tr>
<th>Fund</th>
<th>Inception</th>
<th>Ten Year</th>
<th>One Year</th>
<th>YTD</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>228.3%</td>
<td>66.2%</td>
<td>29.7%</td>
<td>3.7%</td>
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<tr>
<td>MSCI EAFE Index</td>
<td>76.4</td>
<td>73.4</td>
<td>30.4</td>
<td>5.0</td>
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<td>Inflation plus 10%</td>
<td>352.4</td>
<td>222.1</td>
<td>13.7</td>
<td>na</td>
</tr>
</tbody>
</table>

See page 20 for additional performance information.

As in the previous quarter, the largest positive contributors had strong operating results and fundamental business improvements. After declining in the first quarter alongside most Japanese stocks, Olympus rose 20% in the last three months as a result of several positive developments. Michael Woodford became the first non-Japanese president of Olympus, and he immediately highlighted the importance of the medical and life sciences businesses where we attribute all of the company’s value. He also sees substantial opportunity for reducing bureaucracy and costs — upside to our appraisal. The company’s repurchase of 1.5% of its discounted shares was welcome news.

Dell surpassed margin and earnings expectations for a third consecutive quarter, making it a top Fund contributor for both the quarter and the last six months. The company’s results reflect ongoing migration from end user computers to higher margin enterprise solutions. Additionally, supply chain improvements, product simplification, and better pricing have enabled the company to deliver profits in the consumer segment of the business. Dell also announced that it repurchased $1.1 billion of stock in the last two months — an especially high return choice for shareholders given that the stock trades for around half of appraised intrinsic value.

Edenred added the most to the Fund’s performance year-to-date (up 32% in the half and 4% for the quarter). The company grew voucher issue volume and revenues steadily in Europe and substantially in Latin America. Willis returned 20% in the first half, 3% in the second quarter. This insurance broker stands to benefit as insurance pricing hardens following this year’s multiple natural disaster losses. Willis expects further margin and earnings growth as revenues rise and management reduces operating costs.

The stocks that weighed most on performance in the quarter had mostly positive developments. HRT, the Brazilian exploration and production company, lost 14%. The stock’s weakness primarily reflected the end of the lock-up period following the company’s IPO last fall. Because of large gains, many initial funders had to sell shares to reduce position size. HRT should have its first well results from the Solimoes basin this summer. The company’s UNX acquisition in the quarter more than doubled Namibian acreage, giving HRT the second largest position in that country. Additionally, independent report findings increased the likelihood of reserves in this acreage.

As a reminder, while Dell is a U.S. company, a large portion of its business derives from international markets which is why it’s a holding in the International Fund. C&C Group returned 16% in the quarter, and its value grew despite our lower assumptions for the Irish business due to macro issues in that economy. The U.K. cider business increased steadily. The cider market has significant opportunity for international expansion. C&C reduced debt, creating net cash on its balance sheet.

The stocks that weighed most on performance in the quarter had mostly positive developments. HRT, the Brazilian exploration and production company, lost 14%. The stock’s weakness primarily reflected the end of the lock-up period following the company’s IPO last fall. Because of large gains, many initial funders had to sell shares to reduce position size. HRT should have its first well results from the Solimoes basin this summer. The company’s UNX acquisition in the quarter more than doubled Namibian acreage, giving HRT the second largest position in that country. Additionally, independent report findings increased the likelihood of reserves in this acreage. The construction company Hochtief declined after Australian construction firm Leighton, 55%-owned by Hochtief, announced a rare profit miss due in large part to impairments related to catastrophic weather and flooding in two projects. The market ignores the operating
assets of Hochtief, which trades for only slightly more than the market value of its Leighton stake. The company intends to IPO or sell concession assets in 2011 and plans to sell a portion of its real estate assets in 2012. These actions should highlight the underlying asset value. ACS now holds over 50% of Hochtief shares. ACS’s capital allocation discipline and operational capabilities will make Hochtief even stronger. Cheung Kong fell 8%. This Hong Kong conglomerate run by Li Ka Shing completed both the biggest IPO in Singapore by selling ports at 16.5x OCF and the first Chinese REIT in Hong Kong by selling Chinese investment property at a 4% yield. Its retail business via Hutchison Whampoa has grown top line and margins. The government crackdown on real estate has made construction financing difficult for developers, and Cheung Kong has used its size and financial strength to cheaply acquire good sites in the fallout. The company anticipates a more challenging real estate environment in Hong Kong as the government attempts to cool prices.

NKSJ, flat in the second quarter, was the largest performance detractor year-to-date following the Japanese earthquake and tsunami in March. The catastrophe minimally impacted the company’s long-term value and pushed management to commit to combining the non-life insurance operations of Sompo and NipponKoa. Cemex remained under pressure, and the stock’s 16% decline in 2011 hurt Fund results. Even though most of its international markets have improved, the slow U.S. construction recovery remains the major challenge for this cement and aggregates producer. U.S. volumes are a fraction of 2006 levels. A possible highway bill delay past the 2012 elections has caused some concern about near term demand. Whether volume growth returns in one year or three, we own irreplaceable aggregate assets as well as production facilities that will not see new capacity threats for many years to come. Cemex sells far below both replacement value and prices recently paid for similar assets.

We sold Diageo at a gain as it approached appraisal value. We trimmed NKSJ, Olympus, Seven Bank, Willis, and Yum! Brands to initiate three new positions and to fill out the first quarter’s additions, Ferrovial and Nitori. The significant price volatility late in the quarter provided an opportunity to invest in quality businesses trading at discounts. After selling Philips Electronics in April 2010, we added the company back to the portfolio this quarter. Short-term margin pressures created a deep discount to the collective value for one of the world’s leaders in both medical equipment and lighting plus numerous consumer electronics brands. Subsequent to quarter end, the company announced a 12 month €2 billion buyback plan that will retire 11% of the outstanding shares. We initiated a position in French cement and aggregates business Lafarge. Like Cemex, Lafarge is under pressure with a slow global economic recovery. Concerns over its Egyptian business following the spring uprisings in the Middle East pushed the stock below replacement cost. Bruno LaFont is a solid operator and the board includes large owners with strong capital allocation records. Recently, Lafarge divested U.S. cement capacity, some ready mix assets, and a grinding plant at a premium to our appraisal. We had a rare opportunity to invest in a private placement in IronCo., a Brazilian iron ore mining business whose name will become Manabi Holding. The founders came from MMX, the first private sector iron ore company in Brazil, and are owner-operators with a strong track record and extensive industry experience. They have secured a world class asset, which could prove to be among the lowest cost and highest quality iron ore on the market, and is located adjacent to the Anglo American Minas Rio project. A contractual clawback on the management equity stake minimizes our investment risk, and the IPO is scheduled for 2012.

The International Fund’s price-to-value ratio (P/V) is compelling in the low-60%s. The companies we own are competitively entrenched and most are run by management partners who have built significant value for shareholders. Our appraisals are growing, making the P/V even more attractive. Subsequent to quarter end our on-deck list has deepened with opportunities across various geographies and industries.
Management Discussion

Longleaf Partners International Fund returned 2.9% in the quarter, trailing the MSCI EAFE Index’s 3.4% return. The Fund has exceeded our annual absolute return goal of inflation plus 10% over the last year. Since inception, the Fund has tripled the returns of the Index.

Cumulative Returns through March 31, 2011

<table>
<thead>
<tr>
<th></th>
<th>Inception</th>
<th>Ten Year</th>
<th>One Year</th>
<th>YTD</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>225.6%</td>
<td>74.8%</td>
<td>14.6%</td>
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<tr>
<td>MSCI EAFE Index</td>
<td>73.7</td>
<td>69.0</td>
<td>10.4</td>
<td>3.4</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>337.6</td>
<td>222.2</td>
<td>12.8</td>
<td>na</td>
</tr>
</tbody>
</table>

See page 20 for additional performance information.

Most holdings appreciated in the quarter. The top five contributors spanned across five countries and four industries. Performance was driven primarily by better-than-expected results and smart management execution at the individual company level, rather than by broad macro themes. Edenred, which gained 28%, has been a consistent, strong performer since its spin from Accor last summer. Edenred grew issuer volume by 10% (over 20% in Latin America), increased face value of vouchers, and further penetrated existing markets. Paper printing costs represent 30% of total operating expenses, and Edenred accelerated its plan to migrate 50% of the business to higher margin digital vouchers (currently 34% of the business is paperless). The company increased its float assets by 10% in the year and set a dividend of €0.50 per share for 2011 — a payout ratio of 70% based on EPS. Free cash flow is double stated earnings due to the cash generated from negative working capital — one of the reasons the stock is overlooked.

Insurance broker Willis appreciated 17% in the quarter. Recent natural disasters including the New Zealand earthquake, Australian floods, and Japan’s massive earthquake and tsunami, will remove substantial capital from the insurance industry and enable higher pricing. As a broker, Willis has no underwriting risk, and revenues should rise with premium increases. CEO Joe Plumeri continues to cut out operating costs and expects significant margin growth and improved earnings, even without the benefit of higher pricing. Hochtief’s stock rose 28%. Management ended its attempts to prevent ACS from acquiring over 30% of Hochtief shares in a tender offer, and ACS took its stake to over 40% in the quarter, with a goal of reaching 50% in the coming months. The Qatar Holding group also increased its ownership stake to over 10% of the company. Hochtief announced improved results in its European construction business, initiated the sale of its concessions business, and moved the planned sale of its real estate from 2013 to 2012. HRT was another strong performer, up 9% in the quarter. Increased seismic processing further confirmed the quality and level of HRT’s reserves in the Amazon valley. Initial drilling results should come in the next few months, and the company expects 750 million barrels in reserves by the end of the year. In the quarter, HRT acquired UNX Energy to expand their lease acreage position in Namibia offshore.

While company fundamentals drove good performance, the few holdings that negatively impacted performance suffered from short-term macro challenges that did not impair values and/or will create longer-term benefits. The earthquake and tsunami impacted prices of our holdings in Japan, most notably non-life insurance company NKSJ, which declined 7%. We decreased our current appraisal by a similar amount due to the combination of a reduced equity portfolio value and lower loss reserves. The company has ample capital to cover anticipated claims, which will be capped by the government’s stop-loss program, policy coverage limits, and reinsurance. Longer term, pricing for insurance
Management Discussion

Our appraisal values are growing, and we are partnered with managements who are focused on building values per share.

cost way to remove the dilution pain from the converts while strengthening the company’s balance sheet. We applaud management for taking this unconventional and logical action. Although we are finding fewer businesses that meet our required discount given the overall rise in global stock prices, we initiated three new positions in the quarter. We bought Ferrovial, the Spanish company that owns toll roads in Europe and North America, airports in Europe including London Heathrow, and infrastructure construction and servicing businesses. Unfortunately, price ran away before we were able to buy a full position, but the company was among the Fund’s top performance contributors. Given Southeastern’s long history of investing successfully in Japan, many asked about opportunities following the tsunami. Although the disaster created a brief window to buy Japanese equities at huge discounts (the Topix Index traded back at pre-crisis levels within 2 weeks), the events did not alter the biggest obstacle to finding Japanese qualifiers — corporate governance and management culture. We did, however, have one on-deck name that met our qualitative criteria prior to mid-March. The short market decline provided the opportunity to buy Nitori, a low cost home furnishings retailer that benefits from significant economies of scale, scope, and supply chain efficiencies. Arguably, rebuilding in northern Japan will create additional demand beyond our initial growth assumptions.

We added Colgate-Palmolive, a consumer brand behemoth in oral care products around the world, via options. When the stock sold in the mid-$70s, we used put and call options to effectively give us a long position in five years if the stock sells below $65 or above $80. Colgate’s exceptional business and capable management team should cause the company’s value to increase appreciably, driven by the stability of its massive international market share as well as its emerging market dominance. In five years we would be happy to be “put” the stock (have to buy it) at $65 since that price meets our required discount today and should be absurdly cheap by 2016. Likewise, our expectations for value growth mean a “call” on shares (right to buy) at $80 will be compelling in five years. If our Colgate appraisal...
proves incorrect, we have downside protection from the current price that buying the stock would not have provided. If something dramatically changes prior to 2016, we can simply close out the options contracts. To illustrate the upside return potential, if Colgate’s current value were around $100 and compounded at 12% per year, in five years the value would be approximately $175. Assuming the stock’s price reflected value, the call option would allow us to buy shares at $80 and sell them at $175 for a gain of $95 versus our net cost of the options at $3.50.

We sold Japan Petroleum as discussed last quarter, and we scaled back Accor and Diageo as their prices appreciated closer to appraisals. We tendered half of our shares in Hochtief to ACS in response to ACS’s public tender offer. We also trimmed the overweight position in NKSJ early in the quarter when price had risen. We moved from our equity position in Shanda into convertible bonds, a higher part of the capital structure that will be worth at least par when due in September of this year. The opportunity came about because the borrowing costs for Shanda shares rose significantly, forcing owners of the converts who were short the stock to liquidate their bonds at a discount.

The Fund is well positioned for value compounding and trades at a P/V in the low-60%, near the long-term average. Our appraisal values are growing, and we are partnered with managements who are focused on building value per share.
Longleaf Partners International Fund returned 7.4% in the fourth quarter and 13.7% for the year. The Fund outperformed our absolute return goal of inflation plus 10% and significantly beat the MSCI EAFE Index’s 6.6% in the quarter and 7.8% for 2010. Long-term cumulative results shown below also have meaningfully outperformed the index.

<table>
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<tr>
<th>Cumulative Returns through December 31, 2010</th>
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</thead>
<tbody>
<tr>
<td>Inception</td>
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<td>International Fund</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
</tr>
</tbody>
</table>

See page 28 for additional performance information.

Substantial gains across most holdings in the fourth quarter generated over half of the Fund's return in 2010. Among the largest contributors to performance were Genting, Cheung Kong, HRT, and Yum! Brands — each of which benefitted significantly from exposure to emerging market growth. Emerging markets (EM) has become a hot buzz phrase, as investors have poured assets into the strategy. Morningstar reported in September that EM funds saw over $18 billion inflows in the first three quarters of 2010. Southeastern has been able to benefit from indirect exposure to these growing markets through investments in developed market companies that contain significant top line exposure to emerging markets without some of the associated price and governance risks. As we have spent more time investigating these underlying market exposures, we have found select direct investments that met our criteria in countries like Malaysia, Brazil, China, and Mexico. Southeastern’s two-sided approach to EM exposure yielded strong results while taking considerably less qualitative risk than a forced allocation exclusive to countries domiciled in these market.

Genting, the Malaysian-based casino operator, was the strongest performer in the portfolio and rose over 70% in the year. Throughout the year the company reported success at its Singapore casino that opened in February 2010. Our appraisal for Genting increased almost 30% in the year, but price appreciated even faster. We sold the position at appraisal in the fourth quarter. Cheung Kong gained 23%, driven primarily by strong performance in Hong Kong real estate and Hutchison Whampoa’s ports and retail businesses. The company took advantage of its strong balance sheet to purchase attractive land in prime locations in mainland China and Hong Kong. The retail and real estate business should benefit from a rise in tourists after the government relaxed visa restrictions for mainland visitors traveling to Hong Kong. Chairman Li Ka-Shing personally purchased over 24 million shares in the year. As
Cheung Kong rallied in October and November, we trimmed the holding but maintain a full position in the company. Yum! Brands gained over 40% in the year, and our appraisal rose at double-digit rates. Notably, Yum is among the few companies we own that have grown value in each of the last three years, including 2008. The largest increase in value has come from China where scale, widespread brand recognition of KFC, and a wealth of talented local managers give Yum significant advantages. Half of profits come from developing markets including China, India, and Africa, which are growing at a much faster pace than the U.S. and other developed international locations. Within the U.S., Taco Bell is Yum’s largest brand, comprising 60% of franchise fee income. Management has returned capital to shareholders via repurchases, but also has invested in high-returning new stores in China. Because the price moved closer to appraisal, we scaled this holding back to 5% of the portfolio.

Our newest position, HRT, a Brazilian oil and gas exploration and production company, was the strongest performer in the quarter and among the top three contributors for the year. As the first investment in Brazil and the first IPO in the Fund’s history, HRT had to meet a much higher bar to qualify. Our extensive network provided unique access to various industry contacts, pre-IPO seed investors, independent board members, and company management to vet our case. The exhaustive review process confirmed that HRT is a leading independent geophysical exploration and production company in Brazil with world class concessions in the Brazilian Solimoes Basin and in Namibia. CEO Marcio Mello, one of the leading geochemists in the world, came from Petrobras and has put together a team of smart owner-operators with proper incentives. The price has appreciated 40% since our initial purchase, as oil prices rose and as Petrobras’ oil find in the Solimoes basin further validated HRT’s assets. We believe there is significant potential for value growth as the company begins drilling in 2011.

NKSJ, the company formed from the NipponKoa and Sompo merger in April, rebounded in the fourth quarter and ended the year as a top contributor. NKSJ benefited from its high exposure to cheap Japanese equities and a more benign competitive situation created by industry consolidation and premium rate hikes. Accor and Edenred were also strong performers in the fourth quarter. In July Accor spun out its service voucher business creating Edenred. Since the split, Accor rallied 51% and Edenred 28%, as the market began to recognize the merits of each underlying business. Edenred increased market share and grew issuer volume organically in Europe and Latin America. Emerging markets now account for over 50% of total volume. Accor appointed a new CEO, Denis Hennequin, a director since 2009. Denis joins in January 2011 from McDonald’s Europe, where he was Chairman and CEO
since 2005. Denis plans to accelerate the “asset light” strategy by selling owned hotels and moving to a franchise model.

The largest detractor from performance in the quarter and for the year was Carrefour, which fell 23% in the quarter after announcing a one-time charge against its Brazil operations and lowering operating income guidance for 2010. The short term price drop gave us the opportunity to increase our position late in the quarter. We remain confident in the management team and the value of Carrefour, which was supported by the recent sale of its Thailand stores at 13 x EBITDA. As the price dropped, the company bought in discounted shares. Subsequent to year-end, the company announced that results were much better than expected with improvements across most of Europe and Asia. Japan Petroleum was flat in the fourth quarter but down 14% for the year. As discussed in last quarter’s letter, we have been disappointed with management’s entrenchment and inattention to value creation and recognition. Although the underlying assets remained cheap, we used the position as a source of cash to fund more attractive opportunities and have subsequently exited the full position in January.

ACS and Hochtief both declined in the quarter, as ACS’s public bid to acquire Hochtief figured prominently in headlines. ACS announced its original offer to exchange eight shares of ACS for every five shares of Hochtief in mid-September. In early December, Hochtief issued 6.99 million shares (9.1% of shares outstanding) to the Qatar Holding group at €57.114/share, a significant discount to intrinsic value and below the stock price at the time. This diluted ACS’ ownership to 27.3% and significantly diminished shareholder value, causing us to question the “good people” aspect of our investment case at Hochtief. ACS subsequently revised its offer to nine ACS shares in exchange for every five Hochtief shares. ACS’ revised offer represented an improved price more reflective of the intrinsic value of Hochtief. By our calculation, the revised exchange ratio of 1.8 meant that any Hochtief share tendered in exchange for a share in ACS was worth €91.80 (our appraisal of ACS’ intrinsic value is €51.00 * 1.8 = €91.80), a price that is very close to our €95.00 appraisal for Hochtief. The better offer combined with our disappointment in Hochtief’s management led us to tender half of our shares. Partial participation reduced our dependence on a management team in which we lost confidence, but allowed our clients to benefit if the dramatic undervaluation at Hochtief is realized.

Activity in the fund was higher than average for the year as we took advantage of extreme market volatility in both directions. We bought six new names (HRT, Carrefour, Shanda Game, Shanda Interactive, Vodafone and C&C Group) and added to five existing holdings (Cemex, Hochtief, Seven Bank, ACS, and Carrefour) when
prices declined in the late spring and through the early fall. We sold three holdings in the fourth quarter and six over the full year. We exited Benesse and Shanda Game as their prices rallied, and we sold Linde, Philips, and Genting at a substantial gain as each approached our appraisal. We sold Daiwa in the first quarter after management actions permanently impaired our value. Throughout the year, we trimmed nine holdings (Cemex, Dell, Diageo, Fairfax, NKSJ, Willis, Yum!, Accor, and Cheung Kong) as prices rallied and position sizes grew in the late summer and in the fourth quarter.

The portfolio today represents the most geographically diverse set of opportunities in the Fund’s history. Over the past five years, we have built out our investment team to enhance our global capabilities. Market volatility combined with having a deeper, experienced team on the ground in Asia and in Europe has greatly benefited productivity, which is visibly reflected in the portfolio. In 2005, over half of the International Fund was invested in Japan and North America, with a handful of holdings in select European developed markets. The “network” benefits of being on the ground and building out relationships with corporate managements, boards, and clients outside of the U.S. has greatly expanded our potential universe and improved our evaluation process. In 2010, the portfolio was invested in companies in 13 different countries, including Spain, Brazil, Ireland, Germany, Hong Kong, China, and Malaysia, which were added in the last five years. The Fund’s diverse portfolio of high quality businesses with capable management teams trades at a price-to-value ratio in the mid-60%. Our business values are growing, and our investment team continues to find qualifying opportunities around the globe to upgrade the portfolio. We have a strong foundation in place for successful compounding, and we thank you for your continued partnership.
Longleaf Partners International Fund returned 16.4% in the third quarter and 5.9% for the year-to-date. Performance for the quarter was roughly in line with the EAFE index’s return of 16.5% and well above our inflation plus 10% absolute annual return goal. The Fund’s year-to-date return exceeds the EAFE’s 1.1% by a wide margin, but trails our absolute return goal slightly. The cumulative results below highlight the significant relative outperformance over longer periods.

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<th>Cumulative Returns through September 30, 2010</th>
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<tr>
<td>--------------------</td>
</tr>
<tr>
<td>International Fund</td>
</tr>
<tr>
<td>EAFE Index</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
</tr>
</tbody>
</table>

See page 22 for additional performance information.

Most names in the portfolio were positive performers in the quarter, with Genting, ACS, Cheung Kong, Hochtief and Carrefour contributing the most substantial gains. Genting added the most for the quarter and year-to-date, returning 46% and 52% over the two periods respectively. The company’s Singapore casino that opened early this year already is generating revenue at an annual run rate of Singapore $3.5 billion. The casino has had 20,000-30,000 visitors daily, and management has increased its annual visitor estimate from 13 million to 15 million. Additionally, Genting recently won the rights to redevelop the Aqueduct Racetrack in Queens to operate New York City’s first slot machine casino, which represents the opportunity to expand in a new market.

Cheung Kong returned 31% in the quarter after reporting positive results across all its businesses. Ports rebounded nicely; Hong Kong property sales added to balance sheet cash levels; the retail business continued to grow revenues and operating income margins; and the previously loss-making 3G business grew subscribers and is expected to produce positive operating income this year. CEO Li Ka Shing has purchased over 15 million shares in Cheung Kong in 2010, an incredible amount of insider buying that takes his ownership of the company over 42%.

ACS and Hochtief each rose over 40% in the quarter, following ACS’s zero premium, all-share bid to acquire the remaining 70% of Hochtief that it does not already own. The management team at ACS, under the leadership of owner-operator Florentino Perez, consistently has created value for shareholders through disciplined operations and smart capital allocation. Both companies trade at a significant discount to our appraisal values.

The second quarter purchase of Carrefour has already shown results, returning 34% over the last three months. Lars Olofsson’s transformation plan is on track to cut
€500 million of costs this year. The company successfully launched its reinvented hypermarket model in Europe in the quarter. The core French business reported positive organic revenue growth and increased its market share. Additionally, Carrefour put its Thailand, Malaysia, and Singapore operations up for sale as part of Olofsson’s plan to exit non-core markets where the company is not the number one or two player. Carrefour bought in shares at a discount, with plans to retire 6% of total outstanding shares by next spring.

Yum!Brands (YUM), which rose 19% in the quarter, has been one of the top contributors in 2010 after gaining 34%. The U.S. Taco Bell and Pizza Hut franchises have increased revenues, but the company’s China business remains the highest return and fastest growing part of the company. YUM’s advantages in China include strong Chinese management, broad brand recognition, scale that far exceeds any competitor, and a comprehensive supply chain that the company controls. Because the value growth has been so strong, the stock still sells at a discount. The international value of YUM is far higher than the U.S. value, which is the basis for owning this stock in Longleaf Partners International Fund.

Cemex was the largest detractor from performance for the quarter and the year, declining 12% and 25% respectively. All construction remained weak in the U.S. with little residential and commercial construction coupled with slow stimulus spending and a delay in a transportation bill from Congress. Mexican volumes were somewhat light, but Latin America, the Middle East, and Asia grew. The company remains competitively entrenched in an oligopoly that has pricing power even amidst large unit declines. Cemex’s U.S. operations made $2.4 billion of EBITDA at the peak; today the U.S. breaks even. Without any help from one of its largest markets, the company is currently producing around $0.80 per share of free cash flow, and the stock is $8.50. Japan Petroleum declined 8% in the quarter and is down 14% this year. The company trades at a significant discount to its book value, but we have been disappointed that management has not taken steps to create shareholder value. Although Olympus posted a 10% gain over the last three months, the stock’s 18% decline in 2010 places it among the primary detractors from Fund performance.

Market volatility continued in the third quarter giving us the opportunity to add to several positions including the relatively new stake in Vodafone. We also initiated a new position in C&C Group, which produces the dominant Irish and UK premium alcoholic cider brand. At the outset of the quarter Accor successfully spun out its service voucher business into a new company trading under the name Edenred. Both Edenred and Accor meet our criteria of good businesses, managed by shareholder-oriented, capable operators, and both trade at a discount to intrinsic value. As prices
rallied later in the quarter we trimmed positions in Genting and Accor. We also trimmed Benesse, NKSJ Holdings, and Japan Petroleum to fund more compelling ideas including C&C and a new name added in October.

Because of the Fund’s tax loss carry forwards, sales in 2010 will not trigger a capital gain distribution. The Fund’s remaining loss carry forwards equate to 9% of NAV. As global macro concerns – rather than an analysis of individual business values – continue to drive stock prices, we are finding many compelling investment opportunities. The portfolio today holds less than one position worth of cash, and our on-deck list of prospective investments is diversified across geographies and industries. Even after a rally in prices in the past two months, the portfolio trades at a P/V in the low-60%s, equivalent to the Fund’s long-term average. Your partners at Southeastern are adding to our investments in the International portfolio, and we encourage others to do the same.

Note: All stock return numbers are stated in US dollars rather than local currencies since the Fund is reported in USD.
Longleaf Partners International Fund declined 10.9% in the second quarter, outperforming the EAFE Index's return of (14.0)%. The Fund's year-to-date return of (9.1)% also beat the EAFE's (13.2)% but trails our absolute annual goal of inflation plus 10%. Over the long-term the Fund has delivered superior relative results.

<table>
<thead>
<tr>
<th>Inception</th>
<th>10 Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>153.2% 66.1%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>35.3 1.6</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>298.1 220.9</td>
</tr>
</tbody>
</table>

See page 22 for additional performance information.

While most portfolio holdings declined in the last three months, Genting, Yum! Brands, and Benesse were positive contributors for the quarter and the year. Genting rose 10% in the second quarter after losing ground earlier in the year over concerns that duopoly competitor Las Vegas Sands’ (LVS) opening would draw from Genting's Singapore casino. Genting has not lost business, but has benefitted as the LVS casino has expanded the Singapore market. Tourist arrivals were up an unprecedented 30% year-over-year in May following record highs in the previous five months. Additionally, Singapore Universal Studios reached a positive EBITDA level and should double its current 8,000 visitors per day as new rides open this year. Yum! Brands grew its China operations at double digit rates, continued to expand its international franchise business, and improved domestic margins. Even though YUM is headquartered in the U.S., well over two thirds of our appraisal of intrinsic value is from non-U.S. operations. Management increased value by repurchasing undervalued shares. The stock rose 2% in the quarter and 13% in 2010. Benesse was up 5% over the last three months and 9% for the year. Its education business performed well with increased enrollment and record operating margins that continued to grow. Although down slightly in the last three months, Willis, which has gained 16% this year, has been the largest contributor to YTD performance. The company has succeeded in increasing new business wins, revenues, and margins.

NKSJ was the largest detractor in the quarter, down 20%, after strong performance in the first quarter. The company announced an overseas acquisition. We continue to encourage management to reduce costs by quickly combining the operating businesses of NipponKoa and Sompo, improve investing, and to assess all decisions based on creating value per share.

The 20% decline in the euro against the U.S. dollar over the past 6 months has been a large driver of poor performance among our European stocks. Short-term currency
fluctuations have not impacted the long-term competitive positions or cash flow production of the underlying businesses. After a positive first quarter, Hochtief lost 27% over the last three months. The stock’s YTD return is (19)% in dollars but (6)% in euros. The company reported no surprises and confirmed guidance for this year. Hochtief’s 55% ownership of Leighton, however, hurt performance when Leighton lowered guidance 3% based on changes in currency rates. ACS’s 20% decline in the quarter made it the largest detractor to YTD performance. The stock has declined this year 11% in euros but 24% in dollars. We wrote last quarter that the market has discarded ACS wrongly as a Spanish construction company that would be punished as infrastructure spending contracted and residential construction collapsed. Although ACS’s total construction revenue is expected to decline slightly in 2010 and 2011, construction represents only 15% of our intrinsic value for the company. 85% is civil works. Over half of that business is outside Spain and growing at double digits with higher margins. ACS trades at a significant discount and remains an attractive opportunity in the hands of outstanding owner-operators. Accor fell 15% in the quarter. For the year the stock is down 14%, but is flat in euros. On July 1, the company successfully split the service voucher business (trading under the name Edenred) from the hotel business. We continue to hold both stocks as each trades at a material discount to its intrinsic value.

The negative performance in the quarter reflects the extreme price volatility which has yielded significant opportunity to enhance the portfolio. In the quarter, we sold Philips as its price rallied through late April and approached our appraisal. We also scaled back Genting, Yum! Brands, NKSJ, and Fairfax, which were all overweight. We used the proceeds to initiate four new positions — Carrefour, Vodafone, Shanda Games, and Shanda Interactive. Carrefour and Vodafone represent competitively entrenched market leaders with huge scale and room to grow in developed as well as emerging markets. Both companies had been mismanaged in the past, but new management teams have focused on improving the core businesses and creating shareholder value. The combined position in Shanda Games and Shanda Interactive is our first direct investment in mainland China. Shanda Interactive is a leading online entertainment media company and majority owner of Shanda Games, a developer and operator of over 33 online games. This rapidly growing business has an attractive network effect, a sticky revenue model, low threat of substitutes, and high barriers to entry.

Throughout the year, we have further improved the qualitative position of the portfolio through new purchases that meet our criteria — “business, people, and price.” We continue to unearth compelling new investment opportunities around the world, and our on-deck list has increased significantly. The quantitative positioning of
the portfolio is equally attractive. The Fund’s P/V ratio in the mid-50%\textedsignifies both a large margin of safety and the potential for above average future returns. At these levels we encourage our partners to add to their stakes, particularly taxable investors who receive the added benefit of a tax loss carry forward of approximately 12% imbedded in the NAV. Thank you for your continued partnership.
Longleaf Partners International Fund gained 2.1% in the first quarter, beating the EAFE Index’s return of 0.9% and continuing the Fund’s long-term outperformance as shown below. Over the last year the International Fund significantly outperformed our absolute annual return goal of inflation plus 10%, gaining 48.3%.

<table>
<thead>
<tr>
<th>Cumulative Returns through March 31, 2010</th>
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</thead>
<tbody>
<tr>
<td>Inception</td>
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<tr>
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<tr>
<td><strong>International Fund</strong></td>
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<tr>
<td><strong>EAFE Index</strong></td>
</tr>
<tr>
<td><strong>Inflation plus 10%</strong></td>
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</tbody>
</table>

Please see page 20 for additional performance information.

We took advantage of market volatility in the quarter to further improve the qualitative positioning of the portfolio. As prices came down in January and February, we added to the heavily discounted holding in Cemex and filled out positions in Hochtief and Seven Bank. We trimmed positions in Fairfax, Philips, Willis, and Yum! Brands as prices appreciated in early January and again in late March. We also sold Daiwa and Linde in the quarter. Although Daiwa remained cheap, our value became permanently impaired as management raised a significant amount of capital last year and made plans to invest $1 billion into its inferior investment banking business. Linde remains a great business and was a solid value compounding, but after gaining 40% since our purchase in early 2009, our discipline dictated that we sell the position as it reached our appraisal.

Our investments in NipponKoa and Sompo merged April 1st to become NKSJ Holdings Inc. Combined, the two companies were the largest contributor to performance in the quarter. We remain in discussions with management to ensure they will take the right steps to reduce costs and improve profitability of the new company. Willis rose 20%, reporting a great quarter with improved margins, organic top line growth, and impressive net new business. With the integration of Hilb Rogal now complete, the North American business realized significant synergies and cost savings. Japan Petroleum, up 15% in the quarter, introduced a new pricing formula that incorporates fluctuating natural gas prices and should help improve domestic gas margins. Interestingly, the primary drivers of relative underperformance in 2009, our Japanese holdings and insurance-related stocks, have proven to be among the biggest contributors to first quarter performance in 2010. NKSJ, Willis, and Japex each still trades at or below 61% of our conservative appraisals, signifying a considerable margin of safety and potential for material upside from here.

Although most positions contributed positively in the quarter, Cemex, Genting, and ACS detracted from performance. Cemex fell 14%. The company reported
disappointing earnings, and stimulus funding may not impact the industry’s revenues this year as had been anticipated. Non-residential construction in the U.S., one of Cemex’s primary markets, continues to decline. These short-term challenges are reflected in both our appraisal and the stock price. Meanwhile, the company remains a dominant provider in the global cement business and has incredible assets in its aggregates division. Debt obligations are manageable, and our management partners are proven owner-operators. When infrastructure spending and real estate development pick up, Cemex’s value should rise at a fast pace given the operating and financial leverage in the business. The share price for Genting Singapore declined 10% in the quarter, as its duopoly competitor, Las Vegas Sands, approached a late April opening. Genting’s newly opened Singapore casinos were crowded in the first few months of operations, as visitor arrivals to Singapore were up nearly 20% year over year in January, and the Universal Studios theme park opened in late March. The Malaysian casinos continued to do well, increasing revenues and EBITDA margins in the quarter. Genting’s value rose in the quarter. ACS is discarded by the market as a Spanish construction company, yet construction represents only 15% of its business, with the majority in higher margin civil infrastructure projects. Although there has been short-term noise over delayed Spanish infrastructure spending, it is a matter of when — not if — the government will go forward with these necessary projects. In the meantime, ACS has increasingly expanded its infrastructure projects overseas, giving the business a good outlook for 2010. Management has taken advantage of the price decline to increase value by buying in cheap shares.

We continue to find new opportunities in Europe and Asia to partner with great management teams at competitively entrenched, top class businesses that we believe are temporarily trading at a discount. Subsequent to quarter end, we have initiated two new positions. The portfolio is fully invested and trades at a P/V ratio in the low-60%, with only one name selling above 82% of appraisal. Our ability to benefit from the growth in emerging markets remains part of the appeal in the Fund’s portfolio. Many investors do not realize that a number of our well-run, dominant, competitively entrenched businesses contain significant top line exposure to emerging markets. We like having our capital in companies that can participate in economic growth but that also meet our qualitative and quantitative criteria without some of the associated price and governance risks that exist in those geographies. As discussed in the shareholder letter at the beginning of this report, we think the quality of the holdings in our portfolio is the highest in the Fund’s history. Our appraisals use current results, which are still depressed relative to historic levels, as a baseline, thus making valuations conservative. We expect significant value growth from here, improving the quantitative positioning of the portfolio even further.
The Longleaf Partners International Fund returned 1.5% in the fourth quarter and finished 2009 with a strong absolute return of 23.2%, beating our goal of inflation plus 10%. While the Fund underperformed the EAFE Index’s 31.8% return in 2009, Longleaf International’s long-term results have far surpassed EAFE.

Inception 10 Year
Cumulative Returns through December 31, 2009

<table>
<thead>
<tr>
<th>Fund</th>
<th>Inception</th>
<th>10 Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>178.4%</td>
<td>105.4%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>55.9</td>
<td>12.4</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>275.8</td>
<td>225.5</td>
</tr>
</tbody>
</table>

Please see page 26 for additional performance information.

Olympus was the largest contributor in the quarter, rising 25%, and among the top performers for the year, up 70%. Management significantly cut costs and saw a recovery in the medical business, which comprises the large majority of our appraisal. The camera business also regained profitability. Genting and Philips added to the Fund’s results both in the fourth quarter and for the year. Genting’s price almost doubled in 2009 as its Malaysian casinos generated strong results, and its Singapore casino will open in February 2010. Philips gained over 20% in the fourth quarter and nearly 50% for the year, as the company beat expectations in the second half in all divisions. The healthcare business grew nicely in emerging markets, and top line declines slowed in developed markets within the lighting and healthcare divisions. Fairfax Financial was one of the largest contributors to returns in the fourth quarter in spite of weak pricing for insurance coverage. Fairfax dramatically grew book value, maintained underwriting discipline, and enhanced future available cash flow through recent privatizations of Odyssey Re and Northbridge. Our value grew over the quarter, and Fairfax remains attractively discounted. After scaling back all four names in the recent quarter, the Fund still holds a full position in Philips and Olympus and overweight positions in Genting and Fairfax.

Ingersoll-Rand and Cheung Kong also contributed to performance for the year. We sold Ingersoll-Rand in the third quarter when it approached our appraisal after almost tripling from its 2008 lows as the company proved concerns over its balance sheet were severely overblown. Cheung Kong rose over 40% in the year as demand for real estate in Hong Kong and China remained strong, and property transaction prices in the market far exceeded those we use in our appraisals of the company’s assets. Li Ka Shing bought more shares, taking his personal ownership to over 40%.

While the Fund exceeded our absolute return goal in 2009, the relative performance to EAFE lagged for three primary reasons. First, approximately 6% of EAFE’s return
came from the dollar’s weakening against other currencies in countries where the International Fund had little or no exposure. Second, the financial sector dominated EAFE’s return. Not surprisingly we do not own any big banks that have heavily levered balance sheets, questionable reserves, and significant government regulatory uncertainty. Many of these banks drove EAFE’s rebound. Conversely, the Fund’s financial exposure consists primarily of property/casualty insurers and an insurance broker. Insurance related stocks were among the weaker industries in 2009. Third, the Fund’s 30% weight in Japanese companies contributed to the relative underperformance. Japan was one of only five major world markets that did not compound at greater than 20% in 2009, rising only 6.8% for the year.

The primary negative impact on the Fund’s return both in 2009 and the fourth quarter was our combined position in Japanese non-life insurers NipponKoa and Sompo which both maintained their strong balance sheets. Under the recently approved merger, the new governance structure should hold management accountable for both underwriting and investing. We are confident that management is committed to the combined company being a best-in-class global non-life insurance business. Two other stocks, Japan Petroleum and Cemex, also hurt Fund returns over the last three months, though both were positive contributors for the year. In the fourth quarter our appraisal of JAPEX grew slightly, and the company sells at a discount to the value of its net cash and public stake in INPEX. We believe a merger of the two companies would benefit all stakeholders. Our appraisal of Cemex held steady in the second half of the year. The company maintained pricing in many markets even as units fell dramatically over the past few years. Cemex could more than triple its free cash flow coupon over the next five years. Its U.S. operations have gone from generating over $2 billion of pro forma EBITDA at the peak to less than $150 million now.

In the fourth quarter, we sold EnCana and trimmed several names that appreciated to fund new purchases in Benesse, Seven Bank, and Hochtief. EnCana rose to our value in the quarter as management followed through with its announcement to split the business into an integrated oil company and a pure-play natural gas producer. Benesse is the dominant Japanese supplementary education company. Seven Bank manages a network of 14,000 ATMs in Japan. Both companies are examples of overcapitalized, growing businesses that are being overlooked in Japan. German-based infrastructure construction company Hochtief has dominant market share in Australia through its 55% ownership of Leighton and competes in the U.S. through Turner and Flatiron. Earlier in the year we bought Linde and Diageo, and both added to performance.

Many investors ask about Longleaf International’s approach to emerging markets. When appraising international companies, our discount rates take into account interest rate differentials so that our comparisons of investment opportunities are
on an “apples to apples” basis across different countries. This adjustment helps insure that we do not give too much credit for higher growth rates in emerging countries without penalizing companies for their higher cost of capital in those areas. Many seemingly attractively priced equities in emerging markets do not qualify on a risk adjusted basis. If a company such as Genting does qualify both quantitatively and qualitatively, we are indifferent to its locale assuming we do not see risk of nationalization or other governmental value impairment. We primarily have emerging market exposure through dominant, competitively entrenched international companies with growing pieces of their business in developing economies. Whether through Yum! Brands’ pipeline of thousands of KFC China stores, Philips’ entrenched emerging markets position in consumer products, medical, and lighting, Diageo’s dominant market share in Africa, or Accor’s leading service voucher business in Brazil, we are able to participate in these markets while protecting capital and partnering with shareholder oriented managements.

Even after a year of strong absolute performance, the International Fund portfolio remains attractively discounted in the low-60%. We have significant opportunity for outperformance, but also a built-in margin of safety both in the price of the portfolio and the qualitative strength of the underlying businesses. Management teams across our holdings have taken advantage of the market environment to strengthen their companies through cost cutting, smart M&A activity, and/or buying in discounted shares. Companies have emerged stronger from the recession, maintaining their competitive positioning and pricing power, which will help protect from the potential threat of inflation. Our appraisals based on depressed 2009 operating results are conservative, and we believe our companies are well positioned for significant value growth over the next several years.
Longleaf Partners International Fund returned 15.4% in the third quarter and 21.4% for the year-to-date, beating our absolute return goal of inflation plus 10% for both periods. Although the Fund has not matched the MSCI EAFE’s returns in 2009, the longer term results shown below have far exceeded the benchmark.

<table>
<thead>
<tr>
<th>Cumulative Returns through September 30, 2009</th>
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</thead>
<tbody>
<tr>
<td>Inception</td>
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<tr>
<td>----------</td>
</tr>
<tr>
<td>International Fund</td>
</tr>
<tr>
<td>EAFE Index</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
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</tbody>
</table>

Please see page 22 for additional performance information.

During the quarter we made several enhancements to the structure of the International Fund to benefit our investment partners. First, we cut the Fund’s management fee 20% reflecting the changes to Southeastern’s cost structure over the last decade due to growth in accounts investing in international securities. Second, we ended our practice of hedging the Fund’s economic exposure to non-US currencies given that shareholders wanted more flexibility to manage their currency exposure, and various methods for individuals and institutions to hedge easily have developed. Historically, the portfolio has been between 30-40% hedged, reflecting the weightings of country-specific holdings as opposed to more global businesses. Third, we restructured Southeastern’s international research team, elevating Scott Cobb to head of European research and Ken Siazon to head of Asian research. As members of the investment team Scott and Ken have generated most of the Fund’s new ideas over the last several years, proven their ability to originate successful investments, and been positive team participants. Andrew McDermott, one of the Fund’s three co-managers, accelerated his Southeastern departure, an event that we began planning for over two years ago. We believe these changes to the Fund will improve the long-term opportunity for current shareholders.

Also, during the third quarter we sold Benesse and Ingersoll-Rand and trimmed five overweight positions after prices appreciated, including Accor, Dell, Fairfax, Olympus, and Philips. Ingersoll-Rand gained 47% in the quarter and over 80% year-to-date. The company further assimilated its Trane acquisition and strengthened its balance sheet. As the stock approached our appraisal, we sold most of our position in the quarter and have subsequently completed the liquidation. We bought a minimal stake in Benesse before its price rallied over 20%, and we sold the small holding at a gain. We bought a new position in German company Linde, the second largest distributor of
industrial gas in the world. Linde has already been a significant positive contributor to performance with its price up 30% since our initial purchase.

The biggest contributors to performance in the quarter were Fairfax, Ingersoll-Rand, and Accor. Fairfax rose 49% as it benefited from strong equity and tax-free bond returns. The company also announced the acquisition of the publicly traded minority interest of Odyssey Re at an attractive price, financed by new FFH shares. This value-neutral transaction will enhance Fairfax’s financial flexibility by allowing management to upstream excess cash from this key subsidiary to the holding company, thereby giving Prem Watsa and his capable team more investment discretion. Accor’s price rose 35% in the quarter after management announced its intention to split the company into two segments: hotels and prepaid services. The service voucher business has been the “hidden gem” at Accor, and the planned split should help the market properly weigh both parts of Accor. Management also built intrinsic worth through a sale-leaseback of a portion of its economy hotel business at above replacement value in a depressed market.

Other notable contributors in the quarter and for the year were Genting, Cheung Kong, and Cemex. In each of these companies, we have management teams in place who are taking the right steps to create value for shareholders. Genting has risen 86% this year. Its Singapore casino project is on track to open by February 2010 amid rumors that its sole competitor, Las Vegas Sands, will see further delays. Cheung Kong has appreciated almost 40% this year as property sales and rentals accelerated, particularly in China, which accounts for approximately 25% of property sales. The company’s chairman, Li Ka Shing, personally purchased a significant number of shares in the quarter. Cemex gained almost 40% in the quarter and is ahead about 50% for the year. Management sold assets and successfully refinanced the business by issuing $1.8 billion in equity. In turn, maturities were extended at favorable interest rates. While cement unit demand has dropped precipitously with the global recession, local pricing is up in almost every market aside from the U.S. and Spain. Sales in developing markets are beginning to recover, and infrastructure stimulus spending is being released in more developed areas. In each of these companies, we have management teams in place who are taking the right steps to create value for shareholders. We saw another example of great management at EnCana, which rallied 16% in the quarter after announcing a definitive date (November 30, 2009) for its intended split into two distinct energy companies, an integrated oil company with significant oil sands assets and a pure-play natural gas producer. The split of the company will allow the market to better value these world-class operations as stand-alone entities. We continue to applaud management’s efforts in creating long-term value for shareholders.
Only two names contributed negatively for the quarter — Daiwa and Japan Petroleum. Daiwa was heavily punished after management raised 200 billion yen through public offerings in July. This diluted our value, but the company is now extremely well capitalized. The stock remains attractive at this depressed price. Japex also declined and sells at a discount to the value of its public stake in INPEX with no credit given for the company's oil and gas assets. NipponKoa appreciated in the third quarter, but has been the largest detractor from 2009 performance. The proposed merger with Sompo will be voted on in December, and Southeastern has been explicit with management regarding the terms we must see in order to support the marriage. We believe the company needs our votes for the merger to occur. If the joint company is structured as we advocate, a unique company will be created, and we should reap handsome returns. If the merger fails, shareholders have alternative options for closing the large gap between NipponKoa's price and its intrinsic value.

While we were pleased to see most stock prices continue their upward march in the quarter, we are far more excited for the potential for value growth from this point at each of the companies in the portfolio. The geographical diversity of the portfolio highlights the increased breadth of our international research, as we continue to unearth attractive investments around the globe. Importantly, we have followed our discipline of selling names that reach full value and trimming overweight names that appreciate to fund more heavily discounted, competitively entrenched businesses. Despite the market rally, we continue to see opportunities both in our existing holdings and in a few new companies that are “on-deck.” With a compelling P/V in the low-60%s and the qualitative strength of our businesses and management teams, the International Fund is positioned to deliver significant excess returns over the next several years. Thank you for your continued support and partnership.
International Fund
MANAGEMENT DISCUSSION

Longleaf Partners International Fund produced its second highest quarterly return since inception, adding 24.0% compared to the MSCI EAFE Index’s 25.4% return. The Fund exceeded our absolute return goal of inflation + 10% over the last three months. For the year-to-date the International Fund is up 5.1% while EAFE has risen 8.0%. The Fund’s long-term results have significantly outpaced the benchmark.

<table>
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<th>Cumulative Returns through June 30, 2009</th>
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<td>EAFE Index</td>
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<tr>
<td>Inflation plus 10%</td>
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<td>10 Year</td>
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<tr>
<td>EAFE Index</td>
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<tr>
<td>Inflation plus 10%</td>
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</tbody>
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Please see page 18 for additional performance information.

All portfolio holdings appreciated in the quarter with the exception of Fairfax Financial. Companies that were punished most heavily in late 2008 contributed meaningfully to second quarter and 2009 YTD returns. Over the last three months Genting Berhad, Cheung Kong, and Ingersoll-Rand added the most to performance with prices up 54%, 33%, and 51%, respectively. Genting and Cheung Kong were also the largest contributors to YTD performance. Genting’s monopoly Malaysian casino business saw continued strength, while its Singapore project appears on track to open early next year ahead of its only competitor, financially troubled Las Vegas Sands. Cheung Kong benefitted from China’s strong economic growth and a property demand rebound. Recent transaction prices for both raw land and completed residential units validated our Hong Kong real estate appraisals. Cheung Kong’s port assets have outperformed competitors in a difficult market. Ingersoll-Rand rallied after successfully refinancing the short-term debt accumulated to acquire Trane. Enhanced financial stability more than compensated for the small value dilution caused by the financing.

Businesses that exhibited stability in 2008 have underperformed the market in the past six months. Fairfax, one of the Fund’s best performing names last year, declined in the second quarter and has fallen 20% over the first half of the year. Our appraisal has grown, and we are as optimistic as we described three months ago about the company’s prospects given its investment and underwriting opportunities in conjunction with its capital strength. Furthermore, Fairfax announced that the SEC completed its investigation of the company without recommending any enforcement action, removing a cloud of investor concern. NipponKoa stabilized in the second quarter but remains the Fund’s largest detractor from YTD results. The stock’s performance must be set against
that of proposed merger partner Sompo Japan, which increased 70% from its March lows and contributed strongly to second quarter performance.

We have taken advantage of the relative underperformance of more stable businesses in the first half of the year by trimming some of our more cyclical holdings to initiate two new positions. We completed the sale of NH Hoteles and trimmed ACS, Cheung Kong, Daiwa, Dell, Ingersoll-Rand, and Japan Petroleum in the quarter. We used the proceeds to purchase Diageo and Benesse and to add to Accor and EnCana. Diageo and Benesse each exemplify the well-capitalized, stable, competitively-entrenched opportunities that our research process continues to unearth across the globe.

As cyclical and leveraged companies have rallied, our on-deck list today looks very different from the on-deck list at the end of March. We have fewer 45-cent dollars to choose from, but we are watching closely a number of high quality 65-cent dollars that we hope will drift lower. As always, we will remain patient and disciplined on price.

Despite the recent rally, Longleaf Partners International Fund remains attractive in both relative and absolute terms. The P/V is in the mid-50%s, below the long-term average. While the short-term outlook remains questionable for many of our businesses and, indeed, for the global economy, the absolute levels of earnings that we capitalize today are far below peak levels of eighteen months ago. In fact, recent results from some investees such as Olympus have begun to exceed our reduced expectations. If the macro headwinds buffeting all our companies simply abate, current values will explode. If not, a substantial margin of safety remains between price and value.

We remain grateful for your support and partnership.
Longleaf Partners International Fund fell 15.2% during the first quarter compared to a 13.9% decline in the MSCI EAFE Index. We are disappointed in these short term results, but believe they are ephemeral. In spite of the last three months, the Fund’s long-term relative numbers remain impressive.

<table>
<thead>
<tr>
<th></th>
<th>Cumulative Returns through March 31, 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Inception</td>
</tr>
<tr>
<td><strong>International Fund</strong></td>
<td>91.6%</td>
</tr>
<tr>
<td><strong>MSCI EAFE Index</strong></td>
<td>1.8</td>
</tr>
<tr>
<td><strong>Inflation plus 10%</strong></td>
<td>245.6</td>
</tr>
</tbody>
</table>

Please see page 24 for additional performance information.

An unremitting stream of bad macro and micro economic news continues to outvote significant corporate values confirmed by conservative individual security analysis. Current events support the pessimists: aggregate corporate earnings have collapsed and show no clear signs of improving in the short term. Credit remains expensive, consumer demand weak, and employment uncertain. A few numbers highlight the depth and severity of the continuing downturn. In February, German exports declined over 20%, Japanese exports declined 50%, and Port of Los Angeles container volumes declined 32% from 2008 levels. Despite these horrific statistics, stocks began recovering in March and contributed to the Fund’s 13% gain in the quarter’s last three weeks. Much of the bad news that has surrounded us has been discounted. Macro conditions, however, have improved: debt markets have reopened to high quality issuers, commodity prices have rebounded and, most important, the mergers and acquisition market has reawakened. The collapsing of time horizons within the public equity markets in recent months has created the largest ever disconnect between the values that real business people place on entire companies and the prices that stock market participants pay for portions of businesses. Both sets of individuals face the same uncertainties, but one group sees opportunity in low stock prices while the other sees reinforcement for reasons to flee to the so-called safety of cash.

Four of the Fund’s five Japanese investees announced substantial M&A transactions during the quarter. Long-time Japan watchers would find such a high incidence of corporate transactions surprising at any time. Their occurrence in the first quarter of 2009 indicates both the degree of positive change within the Japanese market and the fact that global business leaders are moving away from the paralysis that characterized last year’s fourth quarter, even as operating results remain weak. The announced merger between Sompo Japan and NipponKoa could create tremendous value if managements act in shareholders’ interests as they develop integration plans. Without question, in the deals Daiwa and Olympus negotiated, each management created
substantial value for shareholders by monetizing assets that had minimal earnings power. Both Daiwa’s sale of Sanyo and Olympus’s sale of its life science unit to Beckman Coulter represented over 20% of the seller's market capitalization at the time of sale and achieved substantial premiums to Wall Street's estimates of business values. Many of our other companies also hold assets that currently generate little or no earnings but remain valuable to other owners. Today’s market ignores these assets, whether they are rock pits at Cemex, casinos under construction at Genting, or equity stakes at ACS. This ignorance will not last forever: either the market will recognize this hidden value, or management will act to crystallize value via asset sales.

Despite the deals and global equity rally discussed above, all positions declined during the quarter. NipponKoa, Accor, Fairfax, and Cemex hurt performance most. NipponKoa’s decline occurred in tandem with a substantial rise in Sompo’s price as arbitrageurs bet that a merger ratio would favor Sompo at the expense of NipponKoa. We consider this reaction premature because the merger ratio will not be set until July, and the merger will require approval by two-thirds of each company’s shareholders. In any event, NAVs at both firms have increased substantially since the merger was announced as their Japanese equity portfolios have rallied. In contrast, Cemex and Accor continue to suffer from weak end markets in construction and hotels, respectively. The peso’s decline against the dollar aggravated worries over Cemex’s ability to pay its dollar-denominated maturities in late 2009. The company has an asset sale awaiting regulatory approval, and in an environment with demand for hard assets, Cemex could sell additional assets if needed. The company is working with its primary banks on financing alternatives and in the meantime, the peso’s recent strength and early signs of easing credit markets helped the stock rebound 55% from its first quarter low. At Accor, recent changes in the board reflected management’s commitment to creating value while reducing cyclicity. The market is focused on short-term hotel REVPAR trends while ignoring Accor’s shift away from hotel ownership towards a less volatile, fee-driven operating model. Accor’s voucher business benefits from the current environment as governments utilize vouchers to extend stimulus spending to consumers. We are reasonably confident that the new board will act to highlight the value inherent in Accor. Fairfax declined after reporting somewhat weaker than expected fourth quarter insurance and investment results. The company has never been as strongly capitalized and is well-positioned to benefit from current investment and underwriting opportunities. Volatility in quarterly results is a price worth paying for the superior long-term investment returns that Prem Watsa and his team have delivered to Fairfax shareholders.

There were no additions to the portfolio during the quarter. We sold most of our NH Hoteles position and have completed the sale as of this writing. Unlike Accor, NH
owned most of its underlying hotel assets and carried substantial off-balance sheet leverage in the form of operating leases. We misjudged the company’s ability to withstand a severe recession. NH may survive, but the chance that it will fail is too great to take at this point in the cycle when better risk-adjusted returns are available around the world. We trimmed several other names, and used some of the proceeds to add to our position in Genting Berhad.

Several stocks have made substantial moves from their February lows: Cemex ended the quarter up 55%, Olympus up 28% and Cheung Kong up 19%. All three stocks operate in businesses exposed to the current cyclical downturns. They reached their recent bottoms at precisely the point of maximum pessimism, whether gauged by analyst sentiment, media coverage, or short-term backwards-looking trade statistics involving their industries. The current rally may prove short-lived, but these moves illustrate how dramatically stocks can rebound when bad news is slightly less bad than feared.

Destocking has been a substantial driver of recent earnings downgrades and value declines as intermediaries have reduced inventory at much higher rates than required by end demand. At some point, inventories will rebuild, orders will resume, and customers will spend. The companies that survive this downturn will emerge stronger than before. Even a very small increase in revenues will drive substantial earnings increases that will highlight the underlying values of the businesses we own. In the meantime, we have aligned ourselves with excellent partners who can capitalize on today’s uncertainty. Owner-operators KS Li, Florentino Perez, Prem Watsa, Lorenzo Zambrano, and KT Lim have spent their lifetimes creating value by acting intelligently for the long-term while many around them fret over current events. We do not know when the market will turn, but we do know that most of the gains will accrue to those investors with the courage to invest when all others are fleeing.

We appreciate your confidence and partnership.
Longleaf Partners International Fund fell 18.3% during the fourth quarter to end the year down 39.6%. The MSCI EAFE Index declined 20.0% and 43.4% during the quarter and year, respectively. Emerging markets fell even more than the EAFE Index in 2008. The MSCI Emerging Markets Index fell 54%. Individual markets suffered dramatic declines: China’s Shanghai Composite fell 65%, India’s Sensex fell 53%, and the Russia RTS$ Index declined 74%. The January 2008 consensus forecasts missed the mark on almost every count: the U.S. dollar strengthened, U.S. markets outperformed, and “decoupling” proved a myth.

Longleaf International marked its tenth anniversary in the fourth quarter. The long-term relative results have been rewarding, and prior to 2008’s downturn, the absolute results were well above our absolute goal of inflation plus 10%. The Fund opened amidst a global economic meltdown. A decade later we are facing a worldwide recession that has given us the opportunity to own higher quality businesses at deeper discounts than when we began.

<table>
<thead>
<tr>
<th>Cumulative Returns</th>
<th>Since Inception</th>
<th>10 years</th>
<th>5 years</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>126.1%</td>
<td>107.4%</td>
<td>1.4%</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>18.3</td>
<td>8.3</td>
<td>8.6</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>233.4</td>
<td>225.3</td>
<td>81.6</td>
</tr>
</tbody>
</table>

Please see page 36 for additional performance information.

The Fund’s 2008 returns were terrible. We apologize for these returns and wish that we could have acted as better stewards of your money and our own. The market has humbled and frightened many investors this year. While we can benefit from humility and hope to learn from our mistakes, we submit that the fear that grips markets demands that we stick to our discipline. For us stocks reflect the ownership of real businesses and should be treated as such, not as indicators of macro events or reflections of mass psychology. We submit that the best time to purchase individual businesses is precisely when all businesses are treated with equal disdain. Our portfolio has never been as deeply discounted, even if we assume no recovery from estimated 2009 earnings.

Most stocks behaved equally poorly in 2008. Only four stocks positively contributed to performance: Fairfax, Tokio Marine, Nestle, and Encana. Of these, Nestle, Encana and Tokio were sold at or near appraisal early in the year. Fairfax’s extraordinary contribution should be compared to the negative impact of UBS and Allied Irish. We thought the non-bank assets at both UBS and Allied Irish differentiated them from the many seemingly cheap lenders we avoided. We were wrong on these stocks. Fortunately, we sold both well above their recent lows after recognizing our mistakes.
On the other hand, Prem Watsa’s prudent positioning of Fairfax’s balance sheet paid much greater dividends than we ever imagined for the same reasons that nearly destroyed UBS and Allied Irish.

Our fourth quarter performance reflected the spread of the financial sector’s woes into the real economy. The global economy ground to a halt in November. In the space of three weeks, the tone and content in our management meetings around the world changed from cautious optimism to near despair. Several companies that we either own or were researching reported orders down between 20% and 40% with “zero visibility” into 2009.

Our companies have suffered from the sharp downturn, some greatly, but none irreparably. The four biggest decliners for the year and the quarter were Dell, Ingersoll-Rand, Cemex, and Olympus. Ingersoll-Rand and Cemex suffered most because they face short-term refinancing needs that seemed modest when incurred, but currently overshadow all rational discussion of their long-term prospects. After spending a great deal of analytical time on these, we believe that both companies will emerge from 2009 with adequate liquidity. Unlike financial or commodity “plays” that have fallen as much as these stocks, both Cemex and Ingersoll-Rand have valuable, enduring franchises in the global cement and climate management industries. While earnings have declined more than we expected, both companies will benefit from infrastructure and energy efficiency spending in both developed and developing markets.

Dell and Olympus suffered with electronics companies as the extent of order declines became clear. Going into this recession, all manufacturers of electronic goods have been treated equally. Important characteristics distinguish Dell and Olympus from these competitors. Both Olympus and Dell differ from the crowd by delivering cash earnings consistently higher than reported EPS. Both suffer from short-term FX volatility that complicates earnings comparisons. When they are analyzed at all, both companies receive inordinate scrutiny of non-core operations such as the U.S. consumer business at Dell and the digital camera business at Olympus. Both companies trade near all-time low multiples of FCF: Dell at less than 5X, Olympus at approximately 12X. In Dell, we have an excellent CEO with his name on the door, an enormous personal stake in the company, and a clear path towards improved margins, even in a downturn. In fact, margins were up in the last reported quarter even on down revenues. Olympus’ gastrointestinal endoscopy business could be one of the best businesses we have ever owned. These scopes allow early prevention and detection of colorectal cancer, the second biggest killer in the United States and a growing threat around the world. Olympus maintains 70% market share, generates substantial recurring revenues, and has opportunities for product extensions into surgical
procedures that will save patients and hospitals time and money. Favorable demographics and a solid patent portfolio ensure long-term value creation even if hospitals curtail short-term spending. Management has responded to our request for a share buyback and has experience in emerging stronger from severe downturns. Both Olympus and Dell compete with weaker competitors who may not survive this crisis.

Our confidence in the biggest decliners does not reflect blind optimism. Although Kyocera’s management did improve capital allocation, we sold the position during the quarter. Like our earlier sales of KDDI and SK Telecom, this sale below appraisal was painful, but provided liquidity and allowed us to concentrate in our best ideas. More interesting were sales earlier in the year of Cheung Kong and Encana. Both names have reappeared in our portfolio at half the prices at which we sold less than twelve months ago. While we have marked our appraisals down for the current environment, we are ecstatic that we are once more able to partner with K.S. Li and Randy Eresman, two of the best CEOs we have ever encountered.

We do not know when this market will turn. We do know that, throughout history, buying good businesses run by good managers at low prices has led to good results over the long term. Today’s market allows us to take our pick of investments and managements. We have said “no” to more statistically cheap qualifiers in the past six months than we have analyzed in the past ten years. Two of our largest positions, ACS and Fairfax, are managed by owner-operators who have created tremendous value in troubled times. Most portfolio companies hold excess capital, many have incredibly valuable businesses that other owners want, and all trade at historic discounts to value. Our free cash yield based on looking through to the “economic earnings,” or coupon, that we would clip if we were private owners of our companies approaches 20%. When we compare this return to what James Grant calls the “return free risk” available on supposedly “safe” cash and treasuries, we sleep well at night even though we do not pretend to know how bad things will get in the short term.

Thank you for your support in these very difficult times.
Longleaf Partners International Fund fell 26.1% in the year to date compared to a 29.3% drop for the MSCI EAFE Index. The Fund fell 15.2% compared to a 20.6% drop in the index during the second quarter. Longer term returns are shown below.

<table>
<thead>
<tr>
<th>Cumulative Returns at September 30, 2008</th>
<th>Since Inception</th>
<th>5 Year</th>
<th>1 Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>176.6%</td>
<td>37.4%</td>
<td>(26.5)%</td>
</tr>
<tr>
<td>MSCI EAFE Index</td>
<td>47.8</td>
<td>58.8</td>
<td>(30.5)</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>238.1</td>
<td>87.5</td>
<td>15.0</td>
</tr>
</tbody>
</table>

Please see postscript on page 6 regarding recent volatility and page 24 for additional performance information.

The falling market continues to create opportunities for long-term buyers while exposing mistakes. Unfortunately, mistakes and opportunities look alike in a bear market and will continue to do so until the deleveraging and fear that grip markets today pass. The speculative bubble in real estate, commodities, emerging markets, and credit reached what we considered extreme levels as early as 2003, but prices kept climbing into 2007-2008. Given that prices exceeded fair value by many multiples on the way up, it is entirely possible that prices will drop far below fair value and remain there for an extended period of time. We wish that we could call the bottom or predict the turn.

We focus on intrinsic business value and its per share growth. We are certain that a concentrated portfolio of well-capitalized businesses purchased at a discount to conservatively appraised intrinsic values provides investors with the best possible outcome over long periods of time. We say this in full knowledge that a short-term drop of nearly 30% has inflicted great damage to your personal portfolios and, possibly, to your peace of mind. We submit that purchasing 60-cent or less dollars remains the best course of action for long-term investors, even if, in the short term, those 60-cent dollars become 30-cent dollars due to forced selling by leveraged or frightened shareholders.

This drop from 60% of value to 30% best characterizes the price action in the Fund's securities in the third quarter, the year-to-date, and through October. With the exception of Fairfax, every stock declined in the third quarter. For the year-to-date, excluding Fairfax, all stocks that we held as of September 30th had declined. The Fund’s 26% year-to-date decline primarily reflects declining prices and only limited reductions in our appraisals. As a result of a series of difficult decisions, we have acted aggressively to improve the Fund's aggregate P/V from the high-60%s on January 1 to the high-40%s at the end of September.
This P/V improvement does not imply flawless execution. We have made appraisal errors: Allied Irish Bank did not have the capital strength that we believed when we made our initial investment. When the stock rallied in the middle of the quarter, we sold this position at a loss. Both SK Telecom and KDDI reported lower margins than we had hoped while flunking their capital allocation tests. We sold KDDI at a much smaller profit than we would have realized had we acted last summer, and completed selling SK Telecom at a loss subsequent to quarter-end. The prices of many other holdings suffered either directly or indirectly from slowing economies (Dell), financial turmoil (NipponKoa, UBS), or both (Cemex). UBS, which we sold in October, NipponKoa, Dell, and Allied Irish Bank hurt performance most in the year-to-date, while NipponKoa and Dell declined most in the third quarter.

Despite these price disappointments, the vast majority of the portfolio has weathered the first part of the storm well. As important, we have used sales proceeds, including those from Tokio Marine and British Sky Broadcasting during the quarter, to improve the Fund’s ability to ride out, and perhaps benefit from, continued market problems. All three of our newest investees, Genting, Cheung Kong, and Sompo, combine extreme discounts to appraisal with exceptionally strong balance sheets. All three companies are led by managers who have demonstrated their abilities to create value during downturns at the expense of less ably led competitors.

Our sale of Allied Irish Bank and our Cheung Kong experience deserve particular mention because they illustrate the integrity of our process. Appraisals are our anchor to windward. Our comfort in their validity allows us to sleep at night even when our net worths have been temporarily marked down, together with yours, by 30% in less than twelve months. For these appraisals to have any meaning, we must demonstrate two attributes: intellectual honesty and real-world relevance. Our willingness to admit a mistake at Allied Irish Bank created the position of cash needed to purchase Cheung Kong later in the quarter. Our sales earlier this year of Nestle, Encana, and Cheung Kong (yes, the same) as they approached full value verified that our appraisals have been approximately right.

Approximately correct appraisals are no match for a full-blown financial panic in the short term. Our stocks will fall as long as forced sellers rule the day. We know this because we started Longleaf International almost exactly ten years ago when we thought international stocks could get no cheaper. No sooner had we identified twenty of the cheapest stocks on the planet than we saw their prices drop another twenty percent. We had no idea then when the market would turn, but we were richly rewarded by holding to our positions when most people were leaving the game. Today, we own much better businesses than we owned then. We have a much stronger analytical team and much deeper relationships with managements than we did then. Many of our smartest competitors have left the field. We are glad you remain with us.
Longleaf Partners International Fund fell 12.9% in the year-to-date compared to an 11.0% drop for the MSCI EAFE Index. The Fund fell 1.6% compared to a 2.3% drop in the Index during the second quarter. Fear, apathy, and panic dominate markets. We see more opportunities today, both in the Fund and in our extensive on-deck list, than we have seen since 1998 when similar passions ruled the day.

Most stocks in the portfolio declined both in the quarter and the year-to-date, largely because of macro-economic concerns as opposed to company-specific problems. UBS, Allied Irish Bank, and SK Telecom hurt performance most in the first half. Fairfax, Ingersoll-Rand, UBS, and Allied Irish hurt most in the quarter. Despite a continuing drip of negative headlines concerning many of these companies and/or the markets in which they participate, we learned nothing during the quarter that fundamentally changed our appraisals. What has changed is investor sentiment. After a wild spring rally collapsed, pessimism gripped investors in everything but commodities.

Amidst the gloom that has settled over global stock markets, why have we added to the Fund’s holdings at a record pace and approached work with a renewed sense of energy and purpose? Two words: price matters. The Japanese and Chinese markets provide the most recent and relevant illustration of this fundamental premise. Both Japan and China suffer when the global economy slows. However, the Chinese index, which everyone “had to own” last year, declined over 45% in dollars during the first half compared to Japan’s 5% decline. In fact, the Topix actually rose in the second quarter as the Shanghai index’s decline accelerated. Why? We think the simplest explanation is best, not only because it fits, but because it provides food for thought as we look at today’s opportunity set. At the beginning of the year, Japan traded near record lows on every valuation measure despite solid progress in both corporate governance and increasing returns on equity - progress overlooked or misreported by the media. Shanghai, on the other hand, sold at peak valuations despite unproven governance and rapidly deteriorating terms of trade. Chinese corporates had recently issued new equity at record levels while Japanese corporates did the reverse. Sometime early this year, the markets reached levels where sellers vastly outnumbered buyers in China while the opposite occurred in Japan. This macro trend played itself out, as all macro trends must, in individual stocks. Our biggest contributors for the half were all Japanese: Millea, Daiwa, and Kyocera, despite the fact that business conditions arguably worsened for all three.

We submit that something resembling the Japanese “buyer’s strike” grips today’s global equity markets. Everyone knows that the economy has slowed and that the next few years will be tougher than the recent past. The relevant question for investors (rather than speculators) is: “what’s in the price?” One year ago, we reported an extraordinary first half. We expressed delight at the Fund’s reported performance of nearly 15%, but cautioned that both international markets and the Fund’s price-to-value ratio were
“elevated” at the beginning of 2007 and remained so in June of 2007. Today, “depressed” best describes both the state of the market and the Fund’s mid-50% P/V. Investors once comfortable using extreme leverage to pay extreme multiples across asset classes now worry about the contents of their money market funds and cower in the face of modest leverage applied to mid-cycle earnings. Accor, the Fund’s newest holding, perfectly illustrates this trend.

As managers and fellow investors in the Fund, we are neither depressed nor afraid. We know that investment risk more often accompanies complacency than fear. We also know that stocks represent ownership in a business, not merely blips on a screen. Any sensible appraisal must take into account both good times and bad. When we compare prices to values and reflect that our investment horizon, thanks to your support, is measured in years rather than months, we take comfort in our margin of safety. As mentioned last quarter, our comfort and yours depend on the accuracy of our appraisals. We remain confident that our appraisals are approximately correct. For confirmation, we note that our first half sales of Nestle, EnCana and Cheung Kong occurred near appraisal.

Perhaps more important, our management partners share our view that the market has over-discounted bad news. We have rarely witnessed such a broad-based surge of corporate share buybacks and personal investments by executives in companies in which we have invested. This surge means more to us now than in the past because it comes in the face of deteriorating fundamentals and tightening credit. Florentino Perez at ACS, Michael Dell at Dell, Gerard Kleisterlee at Philips, and Shigeharu Suzuki at Daiwa Securities all continued share buybacks during the first half. Marcel Rohner and the entire board of UBS committed substantial incremental personal capital to UBS during the quarter. Tsuyoshi Kikukawa announced Olympus’ first buyback after fruitful discussions between Southeastern and the Olympus Board.

Olympus and Daiwa’s CEOs joined a host of Japanese executives in executing record buybacks at a time when foreign disillusion with the Japanese market reached its peak. They did this in spite of temporarily weakened balance sheets because they, like the other management partners mentioned above, believed their shares were extraordinarily cheap. They understand their sustainable earnings power better than the growing crowd of speculators who will not or cannot look beyond the next quarter.

We do not know when we will reach the magic point where willing buyers suddenly outnumber sellers again for the market as a whole or for the Fund’s particular portfolio companies. Nothing is certain other than the fact that, by definition, the highest-return, lowest-risk equity investments occur precisely when most people have given up hope. Superior long-term returns result from holding steady or indeed adding to quality businesses at these times of market panic, or, even better, apathy. We have continued to add to our stakes in the Fund. We hope you join us.
Longleaf Partners International Fund fell 11.5% in the first quarter compared to an 8.9% decline for the EAFE index. Long-term performance appears in the chart below.

<table>
<thead>
<tr>
<th>Cumulative Returns</th>
<th>Inception</th>
<th>5 years</th>
<th>1 year</th>
<th>1st Quarter</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Fund</td>
<td>231.3%</td>
<td>138.6%</td>
<td>(3.4)%</td>
<td>(11.5)%</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
<td>215.4</td>
<td>84.2</td>
<td>14.0</td>
<td>3.3</td>
</tr>
<tr>
<td>EAFE Index</td>
<td>90.4</td>
<td>163.7</td>
<td>(2.7)</td>
<td>(8.9)</td>
</tr>
</tbody>
</table>

Please see page 24 for additional performance information.

Performance approached the Fund’s worst ever quarter: March 2003. Then, as now, panic selling drove prices in selected markets far below intrinsic value. Then, as now, the portfolio included mistakes both acknowledged and unanticipated. Then, as now, the overall quality of the portfolio combined with bargain prices to move the composite P/V below 60%. Longleaf International’s long-term track record of superior compounding results primarily from periods when the entire portfolio sold below 60% of value. This quarter marked the first drop below 60% since early 2003.

The most important question for shareholders today, and that includes your management team, is: “Should we have confidence in the analytical ability reflected in the all-important “V” of the P/V ratio?”

The best answer to this question begins with a frank admission of our mistakes. UBS, the biggest detractor from performance in the quarter, was a mistake. Our case assumed that new management led by Marcel Rohner would return the firm to its roots as the world’s best private bank at minimal cost. We were half right: Rohner has taken the steps required to focus UBS exclusively on its high-return, low risk wealth management and asset management businesses. The cost, however, has far exceeded our worst-case estimates of how much the historically prudent and conservative Swiss bank’s board permitted the investment bank to over-leverage its balance sheet with questionable assets. Write offs of nearly $40 billion plus dilution associated with two rights issues have destroyed $100 billion of value, several times the capital committed to the investment bank in our initial appraisal. As you would expect of owner-operators, we have taken a fresh look at the Fund’s existing investment. The company has installed a new chairman and completely replaced the management who put its balance sheet at risk. We believe that current leadership is committed to protecting and building the valuable wealth management business, which has proven resilient. The role of
International Fund - MANAGEMENT DISCUSSION

investment banking has been reined in to serve solely as a support function to wealth management clients. If management acts as promised, UBS should be a tremendous investment from this point.

The real story of the past twelve months is not our mistake at UBS, but the string of appraisal successes that have resulted in multiple sales at or near intrinsic value. This quarter’s sales of Cheong Kong, EnCana, and Nestle joined last year’s exits from Renault, Nikko Cordial, and Vivendi. We also reduced overweighted positions in Fairfax and Olympus. EnCana and Nikko Cordial reached value in less than a year. Renault and Vivendi reached value after five years, but paid us to wait by building value in the interim.

Although we have adjusted corporate appraisals as earnings growth has slowed and asset markets have deflated, our appraisals have fared significantly better than stock prices. We care about intrinsic values, not the market. New investments can perform poorly initially as they are often in the midst of the troubles that made them cheap enough to buy, and we do not attempt to time purchases. The Fund’s two newest additions, Daiwa Securities and NH Hoteles, declined steadily after we began buying, only to reverse sharply at the end of the quarter and join Nestle and Millea as the quarter’s largest contributors.

Fairfax, another major contributor, deserves special mention because it benefited from the widening credit spreads that hurt short-term performance at many companies. Prem Watsa’s correct bets against credit markets have worked out spectacularly well, driving performance and value growth at the company. Only two years ago Fairfax reached the point of maximum pessimism, and from that level has more than quadrupled.

Dell and Olympus hurt performance most after UBS. Their declines illustrate the opportunity provided by today’s portfolio. At Dell, which was down 19%, revenues are growing, margins are improving, the business produces an annual cash coupon of over $2 per share, and the company bought in 8% of its stock in the past quarter at less than half of our appraisal of intrinsic value. In addition, the company announced intentions to reduce annual costs by $3 billion — more than $1.00 per share after tax — over three years, which extends beyond the horizon of most Wall Street analysts. We do not fully incorporate these savings into our cash projections. We expect significant further repurchases given Michael Dell’s previous actions and his confidence in the company’s future. After netting out the $5 per share of net cash on the 2/1/08 balance sheet, Dell sells for less than 7x its cash net earnings.
At Olympus, nothing significant has changed since the stock traded near appraisal last summer. The stronger yen will impact reported yen profits, but the short-term impact on dollar profits will be less severe. The long-term pricing power of a market-leader with 70% market share in medical endoscopes will allow Olympus to maintain long-term margins. Olympus declined primarily because of its Japanese listing, a market that investors have abandoned for the third time in the Fund's history. In the first quarter, foreign investors were net sellers of Japanese stocks by the largest margin since 1987. A stronger yen softened the performance impact in U.S. dollars (an impact partly offset in the Fund by our hedges of some Japanese holdings). Nevertheless, the frustration amongst investors with Japanese equities leaps from every headline.

We view this disdain with enthusiasm. While we have had our share of frustrations with Japanese management partners, we have observed slow but steady progress both in general and within the Fund's holdings over the past decade. We prefer today's Japanese opportunity set to those offered the last two times Japan dropped off investors' maps in 1998 and 2003. Today's valuations are similar, but returns on capital are higher, attitudes towards M&A have improved, dividend payouts are increasing, and share repurchases are accelerating. This activity extends to the portfolio, where Millea, Daiwa, and NipponKoa have all been significant repurchasers. Opportunities exist for improvement, but the Fund's Japanese companies enter this downturn with stable businesses and strong balance sheets in a capital-starved world. Most important, valuations discount Armageddon. For confirmation that valuations matter, we need only look across the Sea of Japan to China, last year's sure-fire winner. Amidst all the doom and gloom about Japan, the Shanghai composite dropped an eye-popping 33% in the quarter compared to the 6.4% decline for the TOPIX. At last summer's peak, the Shanghai Index traded at over 50x earnings. Today, the Nikkei trades at about 13x earnings.

We end the quarter much as we have ended other difficult periods: determined to improve, but confident in our process, people, and partners. Longleaf Partners International Fund started as a vehicle to allow us to invest our own money alongside yours in compelling overseas opportunities. In the past three months, your managers have added significantly to the Fund. We hope that you will join us.
Longleaf Partners International Fund gained 15.3% in 2007 compared to an 11.2% gain for the MSCI EAFE Index. The Fund fell 0.6% compared to a 1.8% decline for the Index during the fourth quarter. We are pleased that the International Fund delivered another year that outstripped our absolute goal of inflation plus 10%. The Fund’s cumulative returns are shown below:

<table>
<thead>
<tr>
<th>Cumulative Returns</th>
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<tbody>
<tr>
<td>ticker</td>
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<tr>
<td>International Fund</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
</tr>
<tr>
<td>EAFE Index</td>
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Please see page 24 for additional performance information.

The Fund’s performance has remained flat since June, but the portfolio has been transformed. We invest with a long-term perspective that results in an average holding period of approximately five years. This year’s volatility created an abnormal level of activity. This activity does not imply a change in focus or approach. On the contrary, our willingness to sell dear and buy cheap explains the Fund’s strong performance in 2007.

We began the year with twenty positions, 7.6% cash, and a P/V ratio in the mid-70%. We ended the year fully invested with a P/V ratio in the low-70%. Along the way, we sold or trimmed twelve positions and initiated seven new positions.

As discussed in earlier reports, we sold Vivendi, Renault, DoCoMo, News Corp. and Sankyo earlier in the year and purchased SK Telecom, Japex, UBS and EnCan. In the fourth quarter, we added Allied Irish Bank, Kyocera, and ACS to the portfolio. Over the last three months we sold Nikko Cordial and trimmed several more fully valued positions, including Olympus, EnCan, Fairfax, and Cheung Kong.

Unsurprisingly, the Fund’s five biggest contributors for the year were Cheung Kong, Fairfax, EnCan, Olympus, and Nikko Cordial. The two worst performers were UBS and Cemex. In the fourth quarter, Fairfax, Nikko Cordial, and Cheung Kong contributed most while Dell and Ingersoll-Rand hurt performance.

The stories behind a few of these names illustrate how volatility plays into the hands of concentrated and disciplined long-term investors. In a year in which Japan suffered its second consecutive annual decline, two of the Fund’s top contributors were Japanese companies, and overall Japanese exposure delivered strongly positive returns. In a dreadful year for financial stocks, Fairfax and
Nikko Cordial provided excellent returns. Fairfax shorted the overvalued credit market while improving its own underwriting. Nikko Cordial’s undervaluation attracted a bid from Citigroup that we ultimately accepted after minority shareholders twice forced Citigroup to improve its offer.

More broadly, Cheung Kong, YUM! Brands, and Nestle benefited from the beginning of a flight towards quality, well-capitalized large-cap companies that have been ignored for the past few years in favor of financials, natural resources, and emerging markets. This flight may have only begun. The vast majority of emerging market stocks appear even more overvalued than last year, particularly when adjusted for opaque corporate governance and untested and/or commodity-driven business models. In contrast, Cheung Kong, Yum!, and Nestle remain undervalued, largely because of their “developed markets” exposure.

Cemex’s poor performance might appear to contradict our comments regarding emerging market and commodity-driven companies: the Mexico headquartered company seemingly operates a commodity business, yet it has dropped more than 40% from its highs. Cemex likewise reflected the market’s disillusion with developed markets, as the price declined after Cemex’s acquisition of Rinker increased its exposure to the U.S. housing market. We have lowered our value of Cemex but believe the market has underestimated the positive changes brought to the cement market by consolidation and has overestimated the impact of U.S. housing declines on Cemex’s business.

UBS declined after announcing much larger credit losses than expected. The market price remains far below our reduced appraisal. New management has exited the proprietary trading operations responsible for the losses. We cannot predict the next few quarters, but we feel confident that CEO Marcel Rohner will take the steps needed to reduce risk while maximizing the value of the world’s premier private banking franchise.

At Dell, a price decline of 11% masked positive news in the fourth quarter. The company filed its restated financials, improved margins, and announced a buyback equating to $4.50 per share by using some of the cash on its balance sheet. The ability to buy these shares almost $10 per share cheaper than in early November hurt the Fund’s short-term performance but is a big win for value growth and future long-term performance.

Ingersoll-Rand also fell in the fourth quarter after announcing the acquisition of Trane and in spite of selling its more cyclical Bobcat and road-paving businesses at very favorable prices. The stock’s price does not reflect the transformation of the
company led by Herb Henkel from a diversified heavy industry cyclical to a tightly focused provider of high-value cooling services.

The year ended with signs everywhere of a deteriorating earnings environment. We detect a whiff of fear in international markets that have been characterized by unbridled enthusiasm since 2003. Japanese stocks and financials everywhere have entered a bear market, most equities appear fairly valued, and many are cheap. We have more qualifying investments than at any time since early 2003. Maximizing opportunities for future returns will require painful decisions as we sell undervalued businesses that we like to buy even more undervalued businesses that we love. We will continue to make these decisions as your partners.

Our greatest asset is our ability to take a long-term view that does not depend on the next quarter’s earnings. We thank you for your commitment and invite you to join us in adding to our investment in the Fund.
Longleaf Partners International Fund gained 16.0% in the year to date compared to a 13.2% gain for the MSCI EAFE Index. The Fund gained 0.9% compared to 2.2% for the Index during the third quarter. As the cumulative returns below show, the Fund has significantly outpaced our absolute annual goal of inflation plus 10% since opening almost nine years ago.

<table>
<thead>
<tr>
<th>Cumulative Returns at September 30, 2007</th>
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<tbody>
<tr>
<td>Since Inception 10/26/98</td>
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<tr>
<td>-------------------------</td>
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<tr>
<td>International Fund</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
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<tr>
<td>EAFE Index</td>
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Please see page 20 for additional performance information.

Minor performance gains masked substantial activity in both the Fund and the market, during the third quarter. The Fund’s strong year-to-date performance resulted partly from the volatility that has returned to international markets in 2007. The EAFE Index dropped over 12% in the middle of the third quarter before roaring back to all time highs after the U.S. Fed cut interest rates. A similar cycle in the first quarter featured a 6% decline before the market recovered. Moves in the Morgan Stanley Emerging Markets Index were even more dramatic: drops of 10% and 20% in the first and third quarters preceded snap-back rallies. Individual stocks moved much more in each direction.

We have sold into strength and bought on weakness throughout the year. During the third quarter, we completed selling Vivendi, trimmed Nestle, and exited a small Sankyo position. We added new positions in UBS and SK Telecom. As discussed in previous letters, we sold Renault, News Corp. and DoCoMo while purchasing Japanese Petroleum Exploration earlier in the year. We will continue to take advantage of volatile markets to exit fully priced positions while adding to cheaper names. This reinvestment process has kept the Fund’s price-to-value ratio in the low-70%s even as performance has exceeded our inflation plus 10% objective.

The International Fund’s biggest contributors year-to-date were Olympus, Ingersoll-Rand, and Cheung Kong. For the quarter, Fairfax, Cheung Kong and Nestle helped most. Olympus continued to report strong results in its core medical business while exceeding management’s own expectations in the turn-around of its camera operations. Cheung Kong’s diversified ports, real estate, energy, and retail businesses have finally begun to overshadow its European 3G challenges.
Ingersoll-Rand and Nestle have improved their business mixes through a series of M&A transactions that moved both companies up the value chain. Management at each company announced significant share buybacks during the year to capitalize on strong balance sheets and continued undervaluation. Fairfax benefited from a favorable hurricane season and a well-positioned investment portfolio that anticipated many of this summer’s negative credit events.

Only UBS and Cemex detracted meaningfully from 2007 performance after declines in the third quarter, driven by weak credit and housing markets. We believe that the stock market has overlooked less cyclical franchises outside of fixed income at UBS and residential housing at Cemex that account for the majority of our appraisals.

For the past nine months, the activity around the edges of the portfolio has been perhaps as significant as what has happened within the portfolio itself. After several years of slim pickings, we are beginning to see a wide range of opportunities. We have passed on a number of fifty-cent dollars that failed our “people” test, and we have been within a few points of adding several exceptional businesses that were overpriced a year ago.

The market’s rally shortened our “on-deck” list. We do not have a crystal ball, but we doubt that the volatility the market has exhibited so far this year has ended simply because the Fed cut rates 50 basis points. When prices move as dramatically as they have in the recent past, we find opportunities to buy and sell to the advantage of long-term shareholders. Disciplined buying and selling, realistic appraisals, and a long-term time horizon have been the keys to profiting from volatility in the past. We suspect they will remain so in the future.
Longleaf Partners International Fund gained 15.0% year-to-date compared to a 10.7% gain for the MSCI EAFE index. The Fund gained 8.8% compared to 6.4% for the Index during the second quarter. For both periods and over the long term, the International Fund has far exceeded our absolute annual goal of inflation plus 10%.

<table>
<thead>
<tr>
<th>Cumulative Total Returns at June 30, 2007</th>
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<tbody>
<tr>
<td>Since Inception 10/26/98</td>
</tr>
<tr>
<td>International Fund</td>
</tr>
<tr>
<td>Inflation plus 10%</td>
</tr>
<tr>
<td>EAFE Index</td>
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Please see page 22 for additional performance information.

With the exception of slight pullbacks at Fairfax and Sankyo and a minor decline in News Corp, all names advanced in the first half. The largest contributor was Ingersoll-Rand, followed by EnCana, Olympus, and Dell. Ingersoll’s CEO Herbert Henkel has already proven himself one of our most capable partners, despite the Fund’s holding period of less than one year. He has improved margins at core businesses while selling non-core businesses at prices above our appraisal. With these proceeds he has aggressively repurchased shares. We have seen no better example by management of pulling all available levers to enhance shareholder value per share. EnCana’s price has risen with oil prices, but the strategic value of its unconventional, long-term oil and gas reserves remains unappreciated by the market. Olympus has successfully turned around its camera business while reporting better than expected growth in its core medical equipment business.

The top performers in the half also led performance in the quarter, though in a different order. Dell contributed most gaining 23%. Michael Dell returned to the CEO role early in the year and has added several strong members to the executive team. Results announced at the end of May were significantly better than Wall Street expected, due in part to stronger pricing and double-digit growth in Europe and storage products. In addition the company announced that headcount would be reduced by 10%. Dell began addressing concerns about the consumer market, which represents only 15% of revenues, by exploring alternative distribution channels and introducing new designs. While our appraisal has remained stable, sentiment has begun to improve, thus driving the stock’s appreciation.

Over the last three months, most names advanced. Of those that declined, Fairfax fell most, probably as a result of general industry concerns over the performance...
of bond portfolios as interest rates rose. Our appraisal of Fairfax was not affected. Nikko Cordial also declined after the Citigroup tender offer expired. KDDI dropped as a result of a short-term loss of share in net cellular subscriber adds, a number that does not directly impact our appraisal, but frequently influences market sentiment.

As mentioned in the first quarter letter, we sold News Corp early in the year. In the second quarter, we sold Renault as it approached our appraisal after almost tripling our investment over seven years. Renault illustrates Ben Graham’s teaching that, at the right price, any stock can be a good investment, while also highlighting the importance of good partners. We have no affinity for the automotive business, but our entry price allowed us to buy an admittedly average auto business for a stunning price of less than zero. As part of the bargain, we received the now widely recognized operational genius of Carlos Ghosn, who turned Renault’s investment in Nissan into a home run, and the still unrecognized capital allocation skills of Louis Schweitzer, who made the original Nissan investment while swapping Renault’s sub-scale Mack truck business for a valuable piece of Volvo. Today, the same analysts who argued that Renault should always trade at a conglomerate discount trumpet the value of the holding company structure and give full credit for a complicated Renault turnaround in the face of a deteriorating macro environment. We fervently hope that we can again partner with Carlos Ghosn, but are happy to part with Renault at our exit price, particularly when we can reinvest the proceeds at a more attractive price-to-value ratio. For the same reason, we also sold NTT DoCoMo. Finally, we bought Japan Petroleum Exploration in the second quarter.

Considering the elevated level of both international markets and the Fund’s price-to-value ratio at the beginning of the year, we are delighted by the first half’s performance which has already exceeded our annual target of inflation plus 10%. We will be surprised if we are able to sustain such a pace over the short term, but, over the long term, we feel very good about the Fund’s position. Our research productivity has continued to increase thanks to the efforts of the analysts introduced at our annual meeting; the P/V is currently in the mid-70%s; we are replacing fully valued equities with cheaper qualifiers; and we have a list of on-deck candidates that will become buys if and when their prices weaken. Finally, and perhaps most important, we believe that the financial and business strengths of our existing holdings will become more apparent as the credit-fueled tide that has driven most global markets to new highs begins to recede.

Please see postscript on page 5 regrading recent volatility.
Longleaf Partners International Fund gained 5.7% in the first quarter outperforming both the 4.1% gain for the MSCI EAFE Index and 3.7% for annualized inflation plus 10%. Since the Fund’s inception almost nine years ago, returns have bested both the absolute and relative benchmarks.

<table>
<thead>
<tr>
<th>International Fund</th>
<th>Inflation Plus 10%</th>
<th>EAFE Index</th>
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</thead>
<tbody>
<tr>
<td>Value of $100,000 invested at inception</td>
<td>$342,956</td>
<td>$277,327</td>
</tr>
<tr>
<td>Cumulative return since inception</td>
<td>243.0%</td>
<td>177.3%</td>
</tr>
<tr>
<td>Average annual return since inception</td>
<td>15.7%</td>
<td>12.7%</td>
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Please see page 20 for additional performance information.

Nikko Cordial, Japan’s third largest brokerage firm, contributed most to the quarter’s performance. The market’s overreaction to penalties imposed by the Japanese regulator, the FSA, upon Nikko Cordial in the fourth quarter of last year allowed us to rapidly accumulate a sizeable position in a company with a tarnished reputation, but with a pristine balance sheet and a valuable franchise. In March Citigroup made a bid for all of Nikko Cordial’s outstanding shares, and raised the bid after the announcement that the company’s shares would not be delisted. The revised offer of 1,700 yen per share remains below our appraisal, but represents a substantial premium to the Fund’s cost. Citigroup’s bid was outstanding at the end of the quarter.

The Nikko Cordial experience validates components that underpin all of our Japanese investments. First, the tide of large-scale, cross-border mergers and acquisitions that has swept most of the developed world has touched Japan’s shores. The tide may not move as fast as we would like, but we believe it is irreversible. Second, courts and regulators increasingly uphold and protect shareholder rights. Third, despite a multi-year malaise, the Japanese financial markets provide substantial opportunities to managements who provide innovative solutions to Japan’s savers, as Nikko Asset Management’s success has proven. Fourth, despite recent increased attention from investors, the Japanese market remains surprisingly inefficient given its size and maturity. Finally, executives of undervalued companies increasingly are being held accountable, and in some cases, are being replaced by managers, whether inside or outside of Japan, who think they can do a better job.

In addition to Nikko Cordial, Fairfax and KDDI were significant contributors to performance, and most other positions advanced. Fairfax continued to benefit from the market’s increased confidence in both its balance sheet and its operating
performance. KDDI has emerged as the clear winner in Japan’s introduction of mobile number portability, but, perhaps as important, has done so in a way that did not destroy the industry’s profitability.

Dell, the Fund’s largest holding, was the only name that meaningfully detracted from the Fund’s results. Kevin Rollins resigned and Michael Dell has taken the reins as CEO. Dell has brought in several new senior managers, is improving customer support, and is focused on restoring margins and sales growth to previous levels. While the outcome of the SEC’s investigation of Dell’s accounting is uncertain, we believe that the company’s competitive advantages remain in place, i.e. being the low cost provider via the direct sale model and having an entrenched distribution network with unique access to small and mid-sized customers. Even in what was arguably a bleak year, the company earned $3.7 billion in free cash flow and had margins, albeit depressed, that were higher than its competitors (in the case of HP, this excludes the printer cartridge business.) Our appraisal is significantly higher than the current price, and as the business improves, overseas sales continue to grow, and the company repurchases shares, Dell’s intrinsic value should grow meaningfully.

During the quarter dramatic short-term moves in natural gas prices provided an opportunity to purchase the Fund’s newest position, EnCana. We have known EnCana’s predecessor companies and management for nearly a decade. It owns substantial natural gas reserves as well as Canada’s most competitive oil sands project. A warm December and a weak natural gas spot price contributed to a dramatic decline in EnCana’s price despite limited impact on our appraisal. We are delighted to own this high-quality collection of long-lived assets at such an attractive price.

We completed the sale of News Corp and trimmed Renault, NTT DoCoMo, Vivendi, and Nestle as they became more fully valued. The International Fund’s price-to-value ratio (P/V) remains in the mid-70%.
Longleaf Partners International Fund exceeded our absolute goal of inflation plus 10% by over 450 basis points, returning 17.1% in 2006. This performance lagged the 26.3% result posted by the EAFE Index. In the fourth quarter, the Fund gained 7.8% compared to 10.4% for EAFE.

Renault, Shaw, and Fairfax contributed the most to returns during the year. Renault’s price increasingly reflected the value of its disparate parts, thanks largely to CEO Carlos Ghosn’s stewardship. Shaw Communications rose 36% and reached our appraisal. We mentioned in the Third Quarter Report our immense gratitude to Jim Shaw for his management acumen. Fairfax improved its capital position by selling a portion of its Odyssey Re subsidiary. This sale along with good 2006 underwriting and terrific long-term investing reversed Fairfax’s slide. The stock was the Fund’s largest fourth quarter contributor, and rose 39% during the year.

Only two stocks declined last year: Dell and SkyPerfect. In the second quarter we sold the Fund’s remaining SkyPerfect position. Dell rose 10% in the fourth quarter, but declined 16% for the full year. Earnings over the last twelve months were disappointing and there is a question of whether some numbers will be restated. However, we believe Dell’s direct sale model is the most competitive over the long run, and that the operating problems related to consumer support and gross margins are less relevant than their strength in the corporate world and their rapid growth in foreign operations. Our corporate partners are both significant owners and smart capital allocators. Although we lowered our appraisal to reflect the last year’s troubles, we think the company’s normal earnings power is much higher than recent numbers, and the true value could be well above the appraisal we use.

Overall, Longleaf Partners International Fund had a successful 2006:

- The 17.1% return handily exceeded our absolute return objective.
- Appraisals of most holdings grew.
- Research productivity accelerated: we added five positions this year and have added seven since the third quarter of 2005.
- We upgraded the portfolio’s quality: never before have we partnered with a better combination of managements and franchises in the International Fund.
- Many of the Fund’s holdings repurchased shares at significant rates.
- Ken Siazon and Scott Cobb joined the research team in our overseas offices and made contributions to new name generation.
- The Fund’s price-to-value ratio (P/V) remains in the low-70%s where it started the year, high by historical standards, but still attractive.
2006 was particularly active. We sold Molson Coors, Shaw, a large piece of News Corp as well as smaller pieces of other appreciated holdings. We used existing cash and the proceeds of these sales to buy Cheung Kong, more Dell, Ingersoll-Rand, Sankyo, and Nikko Cordial. Making swaps like these and holding cash when nothing qualifies are critical to long-term success and to preservation of capital. Sometimes these disciplines can cause underperformance in a rising market, particularly when the market’s return is driven by speculation and a declining dollar.

We emphasize risk to capital as much as potential returns on capital. As a result, we will generally lag markets that reward the riskiest companies. A comparison between Millea, the only Fund holding that declined during the fourth quarter, and China Life illustrates this disparity. Millea has a AA rated balance sheet, consistently underwrites profitably, holds an attractive portfolio of Japanese equities, and leads the Japanese property and casualty market with over 20% market share. Millea trades at less than 1x book value, about 10x economic earnings, and is steadily repurchasing shares. Government controlled China Life has been one of the hottest stocks of the last few years. Just after the year ended, China Life sold additional shares on the Shanghai exchange. The shares doubled on the day of issue and traded at over 7x book value and approximately 70x earnings, making China Life briefly the third most valuable insurance company in the world.

The preference for risk illustrated in the China Life/Millea comparison repeated itself around the world in 2006. The best performing stock markets were in China, Venezuela, and Indonesia. The three largest IPOs were two Chinese government controlled banks and a state controlled Russian energy company. We have nothing against either Russia or China and believe that their increasing integration with the West provides an important counterweight to the more publicized risks emanating from the Middle East. However, we have not analyzed a single Chinese or Russian company in which we would feel comfortable investing our net worth even if the markets were to shut down (a theoretical test that has recently become a reality for investors in Thailand.) On the other hand, we have found superb partners with excellent businesses in China, Russia and other emerging markets at Philips, Cheung Kong, Nestle, and Yum!. Each of these companies has exceptional management with large stakes in the same shares we own. Each has a pristine balance sheet. Each has lagged the most exciting markets.

We started the International Fund in 1998 to invest in compelling, mispriced overseas businesses that were limited to 30% of Longleaf’s domestic funds. Since
International Fund - MANAGEMENT DISCUSSION

inception the Fund has compounded at 15.5%, while minimizing political, financial, and business risk, and nearly doubled EAFE’s return. We evaluate investments based on business, people, and price. Compared to prior years, the Fund’s P/V is higher than average, but its businesses and people are the best we have ever had.
Longleaf Partners International Fund gained 4.7% in the third quarter compared to a 3.9% gain for the EAFE Index. For the year-to-date, the Fund has advanced 8.6% versus the Index’s 14.5% rise but is approaching our absolute goal of inflation plus 10%.

Much of the year’s good performance has been attributable to the media related holdings in the portfolio including Shaw Communications, News Corp, and BSkyB. Although market sentiment has dramatically changed from disdain in 2005 to enthusiasm in 2006, these businesses have performed as we expected. Renault also has been among the Fund’s largest contributors this year, despite operating headwinds in both Europe and the U.S.

Dell has detracted meaningfully from year-to-date performance, and was down 7% in the third quarter. The company’s miscues have been well-documented, but its fundamentals as described in the Longleaf Semi-Annual Report remain intact. In addition, Dell’s customer service efforts have begun to show results. We believe that the overweight position will be extremely rewarding over the long run. The short-term negative sentiment on Dell, which worsened dramatically over the summer, is typical for a new Longleaf holding. If anything, this sentiment helps explain why “Mr. Market” has thrown Dell into the bargain bin.

In the third quarter Fairfax reversed some of its earlier decline and was the largest contributor to performance. The company has delivered steadily improving operating performance on both the investing and underwriting fronts. Insurance broker Willis, and Philips Electronics, which advanced after the sale of its semiconductor operations highlighted the undervaluation of its remaining businesses, also aided recent returns for Longleaf International.

Over the last three months we trimmed several positions as their prices grew closer to appraisal including Shaw Communications. Subsequent to quarter-end, we completed the sale of Shaw. Jim Shaw has been a wonderful partner to Southeastern and Longleaf twice in the firm’s history. We expect that he will continue to build value. Our investment discipline, however, dictates that we exit a position when no margin of safety remains between price and value. We hope to have the opportunity to partner with Jim Shaw again someday, and we are grateful to him. We began the purchase of one new position in the quarter, Ingersoll-Rand, a global manufacturer incorporated in Bermuda.

Given the extended bull market in international equities over the past few years, it appears incongruous that the Fund has reopened and is almost fully invested so near all-time market highs. We decided to reopen the International Fund in June when global markets were retreating and the list of qualifying opportunities was
expanding. Fortunately we were able to make some investments before the markets rallied. We do not pretend that the portfolio’s cheapness compares with that of 1998 or 2003. On an objective level, the price-to-value ratio (P/V) has returned to the low-70%s and most existing holdings have moved out of reach to buy. At a subjective level, the fear that created opportunities in Asia in 1998 and worldwide in 2003 has been replaced by a risk appetite that seems to increase in the face of the wars and hedge fund blow-ups that historically coincided with market collapses.

Despite these factors, we are more excited about the quality of the portfolio than ever before. One reason relates to a review of the Fund’s country weightings, something we rarely perform because we buy each name on its own merits, not its locale. After Japan, the U.S.A. is the largest weighting. We did not intentionally initiate this shift. Many of the cheapest international businesses are based in the U.S. today. This starkly contrasts with 1998, when we started the Fund because domestic portfolios were nearly 1/3rd foreign and we had no place to hold the many non-U.S. based qualifiers that our research process uncovered. All other things being equal, we prefer to own international businesses that are subject to U.S. securities laws. We find it surprising, but perhaps reflective of the current market environment, that highly levered commodity producers based in countries with a demonstrated record of shareholder unfriendliness seem most in demand while U.S. companies with a strong overseas franchise are frequently ignored. We suspect that the tyranny of the indices is at play — many “have” to own the emerging markets players, while the U.S. company that does not fit neatly into a popular style, geography or industry quadrant frequently finds itself the only purchaser of its shares.

Our ability to seek out the best risk-adjusted opportunities, even when they do not fit into a “style box” depends on your support and long-term perspective. We appreciate both.
Longleaf Partners International Fund lost 1.7% in the second quarter compared to a 0.7% gain for the EAFE Index. For the year-to-date, the Fund advanced 3.7% versus the Index’s 10.2% rise. The Index’s small absolute gain in the quarter masked a return of volatility to markets that have levitated since early 2003. Drops of over 20% from peak to trough characterized many emerging markets: Turkey declined 30%, Mexico and Brazil both dropped by nearly a quarter, Russia dropped 32%, and the Morgan Stanley Emerging Markets Index dropped 25%. Developed markets were somewhat less volatile: the EAFE Index dropped 15%. The Fund itself declined nearly 10% from its absolute peak in May to its June trough. Markets rallied strongly at the end of the quarter, but the declines marked the first significant setbacks for international equities in four years. When we started the Fund in 1998, international equities as measured by the EAFE Index had returned less than 4% a year for the prior decade, and those who had piled into emerging markets had lost most of their money after Thailand and Russia collapsed. Much has changed in the past decade, but not the alternating cycles of fear and greed that have always characterized markets. In the second quarter, fear came back to a table previously ruled by greed. This type of environment usually creates opportunities for long-term investors, and the second quarter was no exception.

The Fund has paid a performance price for standing aside during the multi-year rally in the world’s riskiest assets. Absolute performance since inception remains above our long-term objective of inflation plus 10%, but the Fund’s more recent returns have somewhat lagged this objective and have trailed most international indices. We have made a few analytical mistakes, but the biggest performance drag has been the high cash balances carried over the past three years as we waited for ideas that qualified both qualitatively and quantitatively. This patience has finally paid off. At precisely the time that the bloom has begun to fade from riskier equities, we have completed the assembly of the highest quality portfolio of international businesses that the Fund has ever owned. At one point during the quarter, Longleaf International was fully invested with several qualifying names on deck. While some of these names moved away with the recent rally, we are finally in a position to put significant new capital to work, and improve the P/V of the Fund for existing investors from its current high-60s%. For this reason, as of July 10th, Longleaf Partners International Fund is open to new shareholders.

We spent the Fund’s last full position of cash to buy Cheung Kong, Hong Kong’s leading residential property developer and, via Hutchison Whampoa, the world’s largest owner of container ports. No investment better illustrates our current opportunity set: the cheapest stocks happen to be franchises that we as analysts, and more importantly, as consumers, stare in the face every day. Cheung Kong’s
ticker, “1 HK,” symbolizes this phenomenon. No stock could be more obvious, yet few are as ignored. We have wanted to own Cheung Kong since we started the Fund to take advantage of the Asian crises in 1998, but even then, it was too expensive.

We have amassed positions in companies we never thought we could own. Over half of the portfolio consists of “perma-holdings” — companies with superior economics that dominate their industries and delight their customers. Nestle, Dell, YUM, News Corp, Olympus’ and Philips’ medical businesses, Shaw, BSkyB, Cheung Kong, Cemex, Millea, and even the much maligned Japanese cellular carriers DoCoMo and KDDI all fall into this category. Their names resonate with the consumer within us. None could be easily dislodged by even the best-capitalized new competitor. Some face temporary problems, but we are reasonably certain that all these franchises will become more valuable over time. Not only does the Fund own great businesses, but we have extraordinary partners with enormous personal capital tied up in these companies. Lorenzo Zambrano, Li Ka-shing, Michael Dell, Jim Shaw and Rupert Murdoch could form a global management all-star team. They not only manage over a third of the Fund’s holdings, but these five managers together have personal investments of nearly $30 billion in portfolio companies.

Ironically, three of the Fund’s best businesses, Dell, Cemex and Olympus, hurt performance over the last three months. Dell’s weak quarterly results disappointed Wall Street again. The company’s long-term prospects, particularly outside the U.S., remain solid, and Dell’s valuation has become extraordinarily compelling. Cemex and Olympus operations continued to excel. Their prices seem to have fallen in sympathy with emerging market and tech stocks, even though Cemex generates most of its earnings in developed markets and Olympus’ medical profits overshadow its technology exposure.

Shaw, News Corp and BSkyB contributed the most to performance in the quarter. Nothing material changed at any of the companies, though all seemed to benefit from a flow of capital back towards media companies. We completed the sale of SkyPerfect during the quarter.

The same three companies, together with Renault, contributed the most to performance for the year-to-date. Renault’s strong performance, as discussed in the first quarter letter, partly reflected recognition of Renault’s exceptional asset base and partly reflected CEO Carlos Ghosn’s announcement of a concrete plan to improve margins across all of Renault’s markets. Although Fairfax’s stock price recovered from the lows reached during the first quarter, it joined Dell and
Willis on the list of major detractors from the half’s performance. Our appraisals at both Fairfax and Willis remained stable, but both stock prices reacted to the insurance sector’s recently increased volatility.

We want to introduce the newest member of our research team: Ken Siazon. We have known Ken for fifteen years. He brings a keen sense of value and many years of experience in Asian markets to the Fund. He will be based in Asia and has already had an impact on idea generation.
Longleaf Partners International Fund gained 5.5% in the first quarter compared to a 9.4% gain for the EAFE index. We are well on our way towards achieving our annual absolute return objective of inflation plus 10%.

Renault contributed most to the quarter’s performance, despite reporting disappointing operating results. New CEO Carlos Ghosn has committed to aggressive operating targets at Renault. We hope that he succeeds, but take comfort even if he fails in the fact that Renault remains cheap because its investments in Nissan and Volvo account for most of Renault’s current market capitalization. NipponKoa and Millea were the next largest contributors, even though the Japanese market, which conventional wisdom insists drives the performance of Japanese non-life stocks, barely moved. Cemex’s strong operating performance continued during the quarter, as did the strength of its stock price. Olympus rounded out the list of major contributors after reporting stronger than expected camera earnings. The market continues to focus on the fortunes of cameras, even though Olympus’ medical equipment business generates over 90% of earnings.

Of the portfolio’s other fourteen equity positions, half advanced, and six declined marginally. Only Fairfax Financial Holdings detracted meaningfully from the quarter’s performance after delaying the release of its annual report because of a restatement that auditors required at Odyssey Re, the reinsurance company that is 80% owned by Fairfax. The restatement related to the timing of when profits on a certain finite reinsurance contracts from as long as ten years ago would be recognized. Odyssey filed its 10-K, and Fairfax released its annual report, after trading hours on March 31. Ratings agencies have affirmed Fairfax’s ratings. None of this impacted our appraisal, which is substantially higher than the price.

We added one new position during the quarter: Dell Inc. The Partners Fund established a position in Dell in 2005. We bought Dell for the International Fund after its most recent quarterly results brought our appraisal of Dell’s rapidly growing international business in line with its U.S. business value. A combination of double-digit international growth, increasing margins, and low tax rates makes Dell’s international business one of the fastest growing business segments anywhere. We are delighted that an intense focus on Dell’s U.S. slowdown has given us a chance to buy the international business for free.

While one stock does not make or break a trend, it is perhaps symbolic that the Fund’s purchase of Dell marks the first time in recent years that the research flow amongst the Longleaf Funds has reversed. For most of the last eight years, the Partners and Small-Cap Funds have benefited from non-U.S. names generated by our international research. In fact, the primary reason that we started the Longleaf Partners International Fund in 1998 was that we were consistently
finding more international names than the Partners and Small-Cap Funds could accommodate.

This flow’s reversal is not surprising. International markets continue to outperform the U.S. market, both in local and U.S. dollar terms. In the past five years, the EAFE index has handily outperformed the S&P 500 index: 9.6% to 4.0%. Enthusiasm for international funds, both traditional and “hedge,” has sustained or even gathered momentum into 2006. Some of the riskiest international markets and stocks have turned in the strongest performances: the Russian RTS index gained over 27% during the quarter, the Pakistani KSE100 gained 21% and the Brazilian Bovespa gained 13%.

Turning to our own internal metrics, international and domestic price-to-value ratios are broadly in line, and our U.S. on-deck and buy lists are larger than international. The Fund’s price-to-value ratio remains in the low-70%s.

The international market is so broad and diverse that it is impossible to have an intelligent “market view” and unclear how a “view” would help an investor tasked with selecting specific stocks. What is clear is that sentiment towards international investing is extraordinarily positive. This optimism is perhaps warranted by the facts, but not conducive to finding bargains. Ironically, the companies that appeal to us most are those that are attractively priced in this environment: franchises such as Nestle and BSkyB, companies with rock-solid balance sheets such as NipponKoa and Millea, and companies with hidden jewels masked by holding company discounts such as Renault, Philips and Olympus. These companies tend to prosper when the tide recedes, even if they sometimes miss the big performance waves when the tide is high. We will continue to search for new qualifiers without sacrificing our principles. We hope that you share our enthusiasm about the Fund’s current holdings and long-term prospects.
Longleaf Partners International Fund gained 12.9% in 2005 after rising 3.0% in the fourth quarter. The EAFE Index was up 4.1% during the quarter, and increased 13.5% for the year. Since inception in October of 1998, the Fund has returned 15.3% per year against 5.7% for EAFE.

Cemex, NipponKoa, Olympus and Philips contributed the most to the year’s results. Cemex’s stock price began to reflect its outstanding operational performance combined with increased global demand for cement. NipponKoa’s value exploded as underwriting operations remained profitable while its investment portfolio grew with the Japanese stock market. Olympus’ high-growth medical business began to overshadow its unprofitable camera business. Philips continued to improve its capital management policies even in the face of difficult markets, most recently by announcing the possible separation of the semiconductor business.

All seven of the Fund’s biggest decliners belonged to two broad industry groups: insurance (Willis, Fairfax) and the rapidly converging media/telecom sector (SKY Perfect, NTT DoCoMo, News Corp, British Sky Broadcasting (BSkyB), and Nippon Telegraph and Telephone). With the exception of Fairfax, appraisals at each of these companies grew. Fairfax’s price decline, which occurred mostly in the fourth quarter, accompanied an industry-wide inquiry related to finite reinsurance, which Fairfax states it has accounted for appropriately. The insurance brokerage industry suffered early in the year from competitive pricing and the loss of contingent commissions. In addition, Willis’ opportunistic hiring in the face of industry turmoil increased the company’s expenses. By the end of the year, the stock began to recover as Willis reported improved organic growth and substantial share repurchases. The media companies seemed to decline for a single reason: uncertainty about the future economics of a converged digital information market. We have not buried our heads in the sand about the risk the future holds for traditional media. In some cases, such as music and newspapers, we have lowered our appraisals. Nevertheless, we continue to find value in our media/telecom holdings. We believe that most of these risks have existed for years, but were simply ignored. Today, they are more than reflected in the prices of the Fund’s holdings, all of which generate solid free cash flow and hold valuable customer and technical franchises that may prove far more durable than the market currently expects.

Once again, foreign exchange hedges heavily influenced the Fund’s accounting results, this time for the better. As we noted last year, the performance of these hedges was approximately offset by the foreign currency related performance of the corresponding equity positions.
Performance approached our absolute return target of inflation plus 10%. The price-to-value ratio (P/V) ended the year approximately where it began, in the low-70%. While this level remains elevated compared to the long-term average, the combination of value growth and new discounted holdings enabled the P/V to remain stable over the last year even with the Fund’s low double-digit return. Delivering solid results while upgrading the portfolio made 2005 an excellent year.

It was also a transitional year. The sales of Gendis, Nippon Broadcasting, Ezaki Glico, and BIL International and the purchases of Nestle and BSkyB concluded a multi-year trend. In broad terms, the single-market, smaller-cap names that formed the core of the portfolio for many years have been replaced by large or even mega-cap names with global franchises. At the same time, and for related reasons, the Fund for the first time in its history holds more European names than Asian names. Japan in particular has shifted from a land of limitless opportunity for value investors into a more normal market, with both positive (active M&A, better management) and negative (higher prices, increased competition) consequences.

What has driven this transition? Certainly not a change of research focus or a particular preference for larger cap stocks. We remain opportunists unwed to any particular geography or industry. The popularity of international stocks described in last year’s Annual Report has intensified. Despite the dollar’s strength in the face of universal consensus that it would decline, 2005 inflows into international mutual funds exceeded 2004’s record-setting pace by over 60%. In addition, hedge funds and private equity funds, aided by low interest rates, aggressively pursued increasingly large buyouts. As a result, companies deemed potential buyout targets traded at prices implying an imminent takeout while companies deemed “too big to take” were ignored because they lacked an immediate catalyst. Frequently, deteriorating fundamentals served to increase enthusiasm for smaller companies that suddenly appeared vulnerable even as larger companies reported excellent results and improved capital allocation to yawning markets. This was the exact opposite of the trend that prevailed just five years ago when large-cap momentum investors pursued only the largest cap companies in their quest to mimic the major indices.

This market shift explains our ability to sell a single product Japanese confectionary company such as Ezaki Glico at a far higher multiple of earnings than we were able to buy Nestle, perhaps the world’s most valuable global food franchise. By the same token, we sold a Byzantine, poorly managed Japanese media conglomerate such as Nippon Broadcasting (NBS) and bought an incredibly focused and
shareholder oriented BSkyB. Both NBS and Ezaki Glico were excellent investments, but we enter 2006 with a much improved hand vis-à-vis 2005 even though the P/V is similar.

Portfolio sales highlighted one other critical point that we often discuss with shareholders: the primacy of margin of safety over daily liquidity. In one of his first letters to investors in his original partnership, Warren Buffett described a situation in which “our block of stock increased in value as its size grew, particularly after we became the second largest stockholder with sufficient voting power to warrant consultation on any merger proposal.” At BIL, Ezaki Glico, NBS and Gendis, our position resembled Buffett’s in that we held over 10% of each company’s outstanding shares, accumulated patiently over many years at bargain prices. Some observers questioned the wisdom of holding such large stakes because they thought we could never exit without hurting the stock price. In fact, in each case, our large stake allowed us to exit in one or two trades at a large premium to what we would have received had we sold a much smaller stake in the stock market and, with the exception of Gendis, at a substantial profit. We do not intentionally seek large stakes or influence over management when we initiate positions. However, we do not shrink from these situations because they provide double-barreled protection. Our large blocks frequently attract a premium in the frenzied atmosphere that characterizes the final stage of a successful investment. On the downside, they provide us with an important measure of influence if management misbehaves.

Like so many other parts of our investment operation, our ability to extract maximum value from larger stakes relies on your partnership and shared focus on long-term results. We could not execute this strategy if our shareholder partners rushed in and out of the Fund with the tides of sentiment. The Fund remains closed until we find enough opportunities to benefit existing shareholders by putting new money to work. Thank you for your support.

Longleaf Partners International Fund advanced 8.1% in the third quarter compared to a 10.4% advance for the EAFE Index. For the year-to-date, the Fund has gained 9.7% compared to 9.1% for EAFE and is approaching our inflation +10% annual goal. Only four holdings declined in the quarter, and their negative impact on performance was minimal. Cemex again led all contributors as the value of its RMC acquisition became more apparent while hurricane rebuilding plans highlighted the value of its global cement franchise.

Strong international markets were led by Japan, where the Fund has its largest concentration of investments. Every one of its eight Japanese investments advanced during the quarter, and Millea and NipponKoa provided two of the Fund’s top three performances. Japan’s rise reflected the market’s partial recognition of many of the trends described in Longleaf’s Semi-Annual Report. Most notable has been the change in attitudes towards the Japanese non-life stocks that make up the largest portion of our portfolio. After nearly a decade of neglect, NipponKoa and Millea have become investment darlings because of their exposure to the Japanese stock market via their large portfolios of domestic equities. To the extent that Wall Street paid any attention to these stocks over the past decade, they cited this same exposure and the related “overcapitalization” of non-life balance sheets as reasons to avoid the non-life sector. A similar story has unfolded in the Fund’s mobile telecommunications holdings where the market’s shift from focusing on the possibility of new entrants to the reality of strong and growing cash flow generation by both companies has propelled KDDI and DoCoMo upwards. Olympus advanced partly because of a slight improvement in digital camera sales, but primarily because of the sudden enthusiasm for all things Japanese.

This affinity for Japanese stocks has been positive for performance, but negative for idea generation. Our “buy list” in Japan dried up during the quarter. Fortunately, we found one new European idea, Nestle, which we believe fits the “perma-holding” description discussed in the Shareholder Letter at the outset of this report.

We sold BIL International for $1.20 SGD/share during the quarter after its price approached our appraisal. This stock is one of two that we have held since the Fund’s inception in 1998. We roughly doubled our money during this time period, thereby generating a relatively pedestrian return of about 10% per year. However, the stock provided a number of lessons on the importance of good partners even, or perhaps especially, in mediocre businesses. BIL was a holding company with nearly forty different assets when we initiated the position. Its exposure to the airline and hotel sector combined with its financial leverage
caused meaningful value deterioration after September 11th. The stock traded as low as $0.17 SGD and dropped off the radar screen of most analysts. Chairman and major shareholder Kwek Leng Chan patiently rebuilt the company around its best three assets while trading away the other pieces for good values under extraordinary pressure. We are grateful for his hard work and hope to partner with him again.

Performance for the year-to-date closely follows that of the most recent quarter: most names have advanced, led by Cemex and NipponKoa but also joined by Shaw Communications and Renault when the full nine months is taken into account. Only a handful of holdings have detracted from performance in 2005, but none meaningfully.

We end the quarter with less than 10% cash and with the prospect of becoming fully invested in the near future if one or two names move in our direction. The Fund’s price-to-value ratio is in the low-70%$s. We appreciate your support.
Longleaf Partners International Fund declined 0.8% in the second quarter compared to a 1.0% decline for the EAFE Index. For the year-to-date, the Fund has gained 1.5% compared to a 1.2% decline in the EAFE. The broad trends described in the First Quarter Report accelerated in the second. Many major international markets, including the CAC 40 and the FTSE, rose 5 to 10% in local currency, but declined in dollars. The Nikkei reversed its first quarter decline and was up marginally for the year, but down over 6% in dollars.

What does this mean to the Fund? Unfortunately, it means that many of the opportunities that were within reach at the end of the first quarter have moved above our buy limits despite what appears to be a bear market in international stocks if viewed with U.S. dollar goggles. With the exception of large multinationals such as Philips and Olympus, most international stocks we follow generate the majority of their earnings in local currencies. Their values do not fluctuate much or at all when the U.S. dollar moves against their local currency. In fact, this is one reason we hedge the foreign exchange component of many positions.

At the end of March, orders were on the trading desk for excellent companies that would have utilized most of the Fund’s cash. Those stocks are now too expensive to purchase. The international “on deck” list remains longer than its domestic counterpart, but most equities are as overpriced as we have seen them, with the continued exception of Japan. We note that we are “outperforming” our benchmark only to stress once again that our goals are absolute. We share your dissatisfaction with the essentially money market returns generated over the past year.

Despite the appearance that nothing has happened to the portfolio this year, tremendous activity took place on two fronts. First, and more important, values at most investees grew. At Cemex, the Fund’s best performer for the quarter and the year-to-date, a strong cement pricing environment together with higher than expected synergies from its acquisition of RMC drove both price and value higher. At Millea and DoCoMo, large share buybacks accelerated growth delivered by improving operating performance. At Fairfax, continued operating improvement and the recapitalization in which the Fund participated led to a critical ratings decision that will strengthen the competitiveness of Fairfax’s core insurance business. Most other appraisals grew simply because the underlying companies are well managed, good businesses. The partial recognition of such progress explains the appreciation at our other top contributors for the year-to-date: Shaw, YUM Brands, and Renault. Even some of the companies that have hurt performance most in the quarter and year-to-date, such as Olympus,
DoCoMo, Philips, and KDDI, grew their overall corporate values despite highly visible problems in parts of their operations.

We had a few setbacks. Willis, the Fund’s worst performer in 2005 and second worst in the quarter, and Molson Coors each reported deterioration in their UK businesses that lowered our appraisals. SkyPerfect, the Fund’s second worst performer year-to-date, faces stiffening competition in Japan’s multi-channel marketplace and may need to spend more capital than expected to maintain its leadership position.

Continuation of the mostly positive second quarter trends will lead to an improved price-to-value ratio from the current high 60% as we update appraisals through the summer and fall. We believe that sooner or later, performance will reflect this value growth. Considering the high cash flow generation and the increasing number of buybacks under way across the portfolio, we actually prefer that the prices at companies such as Millea and DoCoMo remain low. The lower the share price when a company executes a buyback, the greater the impact on value growth. We would much prefer Millea to repurchase shares at 75% of U.S. GAAP book than to buy in shares at fair value.

In addition to value growth, the other big change involved Japan. Investors frequently ask us macro questions about Japan because they misconstrue the Fund’s high Japanese weighting as either an indication of an affinity for the Japanese market or a reflection of expertise about Japanese trends. In fact, we have invested large sums in Japan over the past several years in spite of negative views of most macro factors. We agreed that the government was too intrusive, that managements generally did not care about shareholders, that “catalysts” and “exit strategies” were few and far between, and that returns on equity were too low. However, the prices for a select group of decent businesses were so low, frequently below net cash on the balance sheet, that they more than reflected these risks. Recent Longleaf reports have described structural changes in Japan’s financial markets: the decline in cross-shareholdings, the increase in mergers and acquisitions, and the appearance of activist local investors. These trends contributed to the takeover of Nippon Broadcasting, which was the third largest contributor to performance in the first half of 2005.

Changes in the recent quarter were more prosaic, but potentially more important. When we first visited Japan, managements rarely met with us or any shareholders. If they did, they spoke primarily about market share. Most companies consistently lowered prices to protect share while paying automatic salary increases to employees as they aged. Predictably, returns on equity spiraled towards low single digits across Japan. In the second quarter, which marked the beginning of the
fiscal year for most Japanese companies, widespread pricing improvements surfaced for the first time in nearly a decade. In many cases, these price hikes simply reflected rising input costs as commodity prices soared, though in the past managements intent on protecting share would have absorbed these costs. More interesting were the attempts by industry leaders to remove structural barriers to intelligent pricing. Viewed broadly, these moves were a long-overdue effort by producers to regain control of product pricing from inefficient distributors. For example, Ezaki Glico led a move to stabilize pricing in the candy sector after Japan’s major brewers initiated a similar process in January. Property and casualty premiums rose based on improved pricing and increased customer spending on plant and equipment. Even the cut-throat pricing trends that have pressured cellular margins at DoCoMo and KDDI showed signs of improving. At the same time that they are raising prices, most of our Japanese management partners are replacing seniority driven pay scales with merit based incentives that frequently include an equity component and generally result in lower overall personnel costs. For example, both Millea and NipponKoa recently replaced cash bonuses paid to retiring directors with options, and aggressively encouraged all employees to participate directly in employee stock ownership programs.

There will be bumps in the road, but the shift in Japan towards working for shareholders has begun to occur and appears irreversible. Considering the low bar set for most Japanese managements by prevailing local interest rates and historically low margins and returns, a small improvement could have tremendous value implications for Japan in general and for the Fund’s Japanese holdings in particular.

The portfolio had a few minor changes during the first half. We sold Nippon Broadcasting and NTT for the reasons described in the First Quarter Report. We also liquidated Gendis, a small position that had distributed its most valuable assets to shareholders over the Fund’s holding period. We thank Albert Cohen for his work in this effort during a difficult period.

We end the quarter as we began the year: focused on the Fund’s holdings, searching for opportunities that make sense, and unwilling to invest our and your capital on unattractive terms.
Longleaf Partners International Fund returned 2.3% in the first quarter compared to a 0.2% decline for the EAFE index. The Fund’s return in the quarter was lower than our goal of inflation plus 10%. International markets outperformed U.S. markets in local currency terms. However, the consensus bet that the U.S. dollar would continue to weaken has proven incorrect so far this year. The U.S. Dollar Index strengthened 4% in the first quarter at the same time that short-term interest rates rose in the U.S. While we do not generally dwell on macro issues such as currency and interest rates, it is clear in our analysis of individual companies that the “carry trade” based on borrowing U.S. dollars and investing the proceeds in foreign equities has influenced valuations in many markets we follow. This trade has been reinforced by the uncharacteristically large inflows into international mutual funds discussed in our 2004 Annual Report. It is too early to tell whether these trends have reversed or simply paused, but we are beginning to find opportunities in areas that just six months ago were absurdly expensive. If the money that poured into overseas markets over the past two years reverses course, we suspect that we will quickly find qualifying investments for the Fund’s cash holdings. Until the market moves our way, we will continue to search for one-off opportunities.

Several stocks made substantial moves during the quarter. The largest contributors were Nippon Broadcasting, Shaw Communications and Olympus, while the largest detractors were Fairfax, Willis and SkyPerfect. Neither Shaw nor Olympus announced significant developments during the quarter. Fairfax and Willis declined at least partly because of the fallout from ongoing regulatory scrutiny of the insurance and insurance brokerage industries. Both Prem Watsa at Fairfax and Joe Plumeri at Willis remain highly regarded by regulators and industry participants. In fact, shortly after the quarter ended, Willis announced settlements with the attorneys general of both New York and Minnesota. These settlements were far smaller than those reached by competitors and included praise from Eliot Spitzer for Willis’ handling of the investigation. At Fairfax, management pre-empted the current industry-wide investigation into finite reinsurance by voluntarily canceling a number of such contracts in the latter half of 2004. SkyPerfect fell after announcing continued weak subscriber trends and a dramatic increase in capital spending that led to a decline in our appraisal. However, subscribers continue to grow in low single digits, contribution margins remain high and management reacted to the decline in its stock price by repurchasing nearly 5% of shares outstanding during the quarter.

Nippon Broadcasting (NBS) appreciated approximately 20% during the quarter after it became the target of a rare, contested takeover bid in Japan. The Fund’s experience with NBS highlights the importance of price and business quality.
NBS has generated substantial returns twice for the Fund. The stock nearly tripled during our first holding period from 1998-2000. We initiated our second position in early 2001 after the stock declined over 70% from its tech bubble highs. We sold the entire position over the last several months for a gain of over 50%. The investment case was simple: NBS traded at a discount to the liquidation value of its holdings in Fuji TV, which was fairly valued or undervalued each time we purchased NBS. Both companies had net cash on their balance sheets and operated businesses that were difficult to replicate. Most important, we paid an implied multiple of between one and three times depressed EBITDA for Japan’s top rated TV broadcaster, a substantial discount to fair value on any measure, especially since broadcasters frequently change hands at over ten times EBITDA elsewhere in the developed world. The price we paid for this margin of safety was uncertainty as to when NBS shares would reach fair value. In Wall Street parlance, we bought without a “catalyst.” The few Wall Street analysts who followed NBS acknowledged that it was cheap, but maintained that it would always remain cheap simply because it had in the past. Our advantage, supplied by Longleaf shareholders, was that we could wait until something good happened provided that the business value grew at a rate at least equal to our discount rate. In spite of bad capital allocation decisions by NBS management, the underlying TV franchise performed well enough to ensure a fantastic return the first time and a decent return the second time we invested.

The NBS takeover battle has ignited a firestorm in the Japanese media and financial markets and will potentially mark the beginning of a new era in Japanese capitalism. The political response has been swift and generally not favorable for shareholders: Japan’s Diet is now considering laws to further restrict foreign ownership in the Japanese media industry. Laws designed to liberalize mergers and acquisitions have been postponed, and Japanese managements have begun to study poison pills with the expressed intent of protecting themselves rather than ensuring that shareholders receive fair value. Nevertheless, the more important trends favor shareholders. First, Japanese courts have begun to protect shareholders from management efforts to entrench themselves at the expense of owners, most recently by blocking NBS management’s attempt to protect itself via a below-market issuance of share subscription options to Fuji TV. Second, crossholdings have unwound to the point that management can rarely expect protection if it fails to perform. Third, the investors pressuring management are increasingly Japanese. Finally, many Japanese managers now understand that improving returns to shareholders helps the company and employees. This perspective characterizes almost all of our Japanese managements. NBS’ managers
International Fund - MANAGEMENT DISCUSSION
by Mason Hawkins, Staley Cates, and Andrew McDermott

turned out to be an exception. This meaningful turn of events has already improved our dialogue with other Japanese managements.

In addition to selling NBS, the Fund sold the remainder of its NTT position and added to its KDDI position. This completed the trade described in the 2004 Annual Report.

Qualifying opportunities remain difficult to find. However, for the first time since early 2003, we have orders on the trading desk that will utilize most of our remaining cash if prices cooperate. We appreciate your continued support.
Longleaf Partners International Fund gained 10.2% in 2004 after rising 8.7% in the fourth quarter. The EAFE Index posted 15.3% during the quarter, and increased 20.3% for the year. Since inception in October of 1998, the Fund has returned 15.6% per year against 4.5% for the EAFE.

With four exceptions, all holdings advanced in 2004. The largest contributors were Vivendi, NipponKoa, YUM! Brands, Willis and Renault. A favorable tax ruling and the sale of its stake in Veolia strengthened Vivendi’s balance sheet. Subsidiaries Canal Plus and Universal Music improved margins, and the SFR telecom business continued its strong performance. Vivendi trades at a “conglomerate discount,” meaning Wall Street acknowledges the company’s undervaluation, but does not see a near-term catalyst that will close the gap between price and value. We have no particular insight into how Vivendi’s management will play its remaining cards, but we have confidence in our appraisal and in their commitment to act in our interest.

NipponKoa’s strong performance both in the fourth quarter and for the year reflected the market’s partial recognition of the financial strength of Japanese non-life insurers in general and the shareholder orientation of NipponKoa in particular. Despite suffering the worst typhoon season in decades, Japanese non-life balance sheets remained overcapitalized. At both NipponKoa and Millea Holdings management used proceeds from asset sales to repurchase shares even while paying significant typhoon related claims.

Although YUM! Brands’ domestic results were steady, the stock’s strength in 2004 primarily reflected the market’s recognition of YUM’s overseas operations. YUM’s quick service brands frequently boast higher market shares in fast growing overseas markets such as China than in the more mature U.S. market. The international business accounts for over half of our YUM appraisal, but was generally ignored by other firms prior to this year.

We purchased Willis in the third quarter during the fallout from Eliot Spitzer’s investigation of the insurance brokerage industry. Willis’ price fell far below our appraisal, which excluded any potential market share gains due to charges against its largest competitor.

Renault’s appreciation reflected the continuing recovery of the company’s core automotive operations, which outperformed most European peers in a difficult market. Renault trades at a significant discount to any appraisal that includes conservative values for Renault’s stakes in Nissan Motor and Volvo.

Our financial statements require us to report foreign currency hedges separately from the equity investments that offset these hedges. These foreign currency
positions, taken in aggregate, hurt performance more than any other position during 2004. However, losses on foreign currency hedges were approximately offset by the foreign currency appreciation related to our equity positions.

Two stocks that declined during the year were NTT and NTT DoCoMo. Because NTT owns 62% of DoCoMo and derives most of its consolidated earnings from DoCoMo’s wireless business, the decline in DoCoMo earnings discussed in the Fund’s first quarter report affected both stocks. We reduced our appraisals of DoCoMo and NTT to reflect both lower earnings and increased competition in the Japanese wireless sector. However, we believe that the market overreacted by lowering Japanese telecom valuations below both our more conservative appraisals and the recent prices paid for weaker franchises in other markets. Earnings momentum has undoubtedly slowed in the Japanese wireless sector, but values are growing, free cash flow remains strong, and 3G services have the potential both to increase revenues and lower costs. We now find DoCoMo and KDDI, which owns Japan’s second largest cellular company, more attractive than NTT and adjusted our holdings accordingly in the fourth quarter. All three companies recently executed share repurchases.

Other recent changes to the portfolio included the sale of Trizec Properties at our appraisal, and the addition of Cemex, Mexico’s largest cement producer which became cheap after announcing the acquisition of U.K. competitor RMC. Earlier in the year, we described the purchases of Coors and Olympus and the sales of Brascan and Hollinger.

Where do we stand today? International stocks have suddenly become fashionable. According to the Wall Street Journal, international mutual funds attracted over $61 billion through November, compared to a previous record of $49.8 billion in 2000. International companies are meeting this demand by selling record volumes of stock. The top equity deal in 2004 was a $9.5 billion offering by Enel, an Italian utility, followed by France Telecom. Several other international companies that could not raise a dime three years ago sold billions of dollars worth of equity, even as last year’s hot Russian market cratered. Our most important metric, the Fund’s price-to-value ratio, remains in the high-60%s, near its all-time high, and the Fund has nearly 15% in cash despite research productivity that yielded six new names during the year. Considering that we started from a similar position in January 2004, a 10.2% return pleased us even though it fell below our long-term objective of inflation plus 10%. Taken together, all these numbers imply that our companies performed about as we anticipated. If P/Vs and cash remain stable, performance equates to value growth, implying that our companies grew at the low double-digit rate that we expect.
Our biggest surprise in 2004 was that we found so many new ideas, despite the relatively high levels of global equity markets throughout the year and the absence of market volatility that frequently provides us with opportunities to build new positions. We find ideas in four ways: individual companies disappoint the market (Cemex), industries fall out of favor (insurance brokers, digital camera producers, Japanese telecoms), volatility creates price instability (late 2002/early 2003), or the market crashes, making many stocks cheap (Fall of 1998). We have no idea when or if a broad market decline will expand our selection of companies. Until it does, we will continue to take advantage of the one-off opportunities we find.

In closing, we will repeat last year’s paragraph detailing our thoughts on foreign currencies and our hedging policy. Although the dollar actually moved less in 2004 than in 2003, the topic of “the dollar” gained air time in the last year. When combined with massive inflows into foreign mutual funds, this media attention reminds us of the internet bubble. There are strong arguments on both sides of the currency issue, but picking individual stocks based on anything other than the merits of that particular investment strikes us as a recipe for disaster.

The dollar’s weakness dominated headlines this year much as the dollar’s strength was news only two years ago. In both cases, the Fund’s returns were somewhat insulated from currency moves by our hedging policies. Our hedges offset the currency-related appreciation or depreciation in foreign stocks. As a result, the return from a hedged position approximately reflects the actual performance of the company’s stock price. We believe that our expertise rests in arbitraging price and value in specific equities, not in predicting currency swings. That said, it is impossible to totally isolate any equity portfolio from currency moves. We generally hedge stocks that have earnings almost wholly in foreign currencies.
Longleaf Partners International Fund lost 4.7% in the third quarter compared to a 0.3% loss in the EAFE Index. The Fund’s return for the year-to-date was 1.4% versus 4.3% for EAFE.

We bought two new names this quarter – Willis Holdings, an insurance broker in the U.K., and Olympus Corporation, the Japanese maker of medical endoscope devices and cameras. We added to several existing positions as they fell below our required discount to appraisal. Both the Fund’s price-to-value ratio, which is in the mid 60’s, and its cash balance, now at 25%, declined during the quarter. As is often the case for long-term investors, we paid a short-term performance penalty to position ourselves for what we expect will be superior long-term returns.

Our work load increases substantially when markets fall, and the third quarter is a good illustration, though the indices’ performance perhaps masked the extent of the declines in areas important to the Fund. For example, the EAFE’s flat return during the quarter obscured the decline in Japanese markets that began at the end of June. At the industry level, takeovers in the financial services and natural resources areas led to price rises that partially offset large declines in insurance, telecommunications, semiconductor and media stocks. Concerns about everything from severe weather to high oil prices to new entrants in the telecom industry reemerged after an eighteen month period during which the markets ignored almost all negatives. As always, these concerns have some validity. However, we think they have been overdone at the critical point where macro concerns intersect with the prices of a handful of individual securities.

In addition to researching Willis and Olympus, we revisited the cases that support the companies that declined the most during the quarter: Fairfax, NTT, NTT DoCoMo, Philips, NipponKoa, Vivendi and Millea. At each company we updated our appraisals and spent time with management assessing the factors that contributed to this quarter’s decline. In every case we came away convinced that our appraisals remain conservative, our partners trustworthy, and our case valid. For example, the recent spate of typhoons that struck Japan will almost certainly lead to the highest catastrophe losses in years. Our Japanese insurers will report lower earnings than expected as they absorb these losses. However, these insurers are so well-capitalized that even a multiple of these losses would have only a fractional impact on our appraisals.

Several companies in the portfolio performed well, in spite of the Fund’s overall decline. The leader was BIL Holdings, which continues to execute its plan of realizing the underlying real estate value of its U.K. hotel portfolio. Renault again contributed by demonstrating improved profitability in Europe, while YUM!
Brands rose on the back of strong earnings and continued progress in overseas markets, especially Asia.

We do not enjoy posting negative performance numbers, but we do welcome the increased potential investments that often coincide with disappointing short term results. Adding two new names in a quarter reflects high research productivity. As we enter the fourth quarter, our “on deck” circle contains more names than at any time in recent memory. Although reduced slightly from last quarter, our cash position remains substantial enough to allow us to quickly accumulate positions that fall into range.
Longleaf Partners International Fund lost 0.2% in the second quarter compared to a 0.2% return from the EAFE Index. The Fund’s return for the first half was 6.3% versus 4.6% for the EAFE Index.

The second quarter was among the most inactive in our history: we neither bought nor sold meaningful amounts of securities anywhere in the world. This inactivity masked two positive trends for long-term investors. First, corporate values at companies we own and those in our “on deck” circle grew. Second, many markets declined, significantly in some cases. These events held the price-to-value ratio in the Fund under 70% and brought many attractive names within reach. We do not know when we will put our large cash position to work, but we are much closer to doing so now than we were six months ago.

Most stocks in the portfolio were flat in the second quarter. No company accounted for more than a 1% change in the Fund’s portfolio. SkyPerfect, DoCoMo, and NipponKoa were the largest decliners, primarily because the Japanese market pulled back somewhat during the quarter. Renault, Fairfax and Vivendi were the largest contributors as each company continued to deliver on management’s restructuring objectives.

For the entire first half, the biggest contributor to the International Fund’s performance was NipponKoa, while NTT DoCoMo was the largest decliner. Both companies reported strong earnings for the twelve months ended March 31, but DoCoMo indicated that it would sacrifice margins for market share in the upcoming year. While we lowered our appraisal to reflect this margin decline, DoCoMo remained one of our most undervalued holdings. NipponKoa’s appreciation reflected continued strength in both its underwriting and investment operations, which benefited from the rise of Japan’s equity market. Other meaningful contributors to first half performance included most of our Japanese holdings, particularly Millea and NTT, together with Renault and Coors, a new holding discussed in our last report. Few other stocks fell during the half, though Philips and BIL posted modest declines.

China and Japan remain the media darlings in the world of international investing. Countries that were written off eighteen months ago because of SARS and “terminal economic decline” have become must-own markets for global investors. This enthusiasm makes us cautious. There is a kernel of truth in the stories propelling each market: China’s economy is growing rapidly and Japan’s economy seems to have turned a corner. These stories have very different implications for our individual stock selections, which will matter far more than whether we are right or wrong about macro trends. In Japan, the cost cutting and improved governance that we have described for the past five years have finally
been joined by some top line growth, or at least a slower rate of revenue decline than we expected. This growth has translated into meaningful profit and value growth at most of our companies. As a result, valuations remain compelling in spite of the dramatic price rises.

China, on the other hand, appears expensive and risky at the company level. Recent IPOs resemble the tech craze in the late 1990s when valuation momentarily became irrelevant. To cite just one example, Ping An, China’s second largest insurance company, recently went public at 4.2X book value. China’s insurance market will certainly grow faster than Japan’s, but we are far more comfortable paying less than book value for well governed, over-capitalized, equity-weighted and profitable Japanese insurers such as Millea and NipponKoa than rolling the dice at 4X book in China. That said, we do participate in China’s growth through our investments in companies such as YUM Brands, Renault, and Philips, all of which have large and expanding Chinese businesses. These companies provide a doubly attractive way to invest in China: we get great managements with a track record we respect together with an exposure to China that is typically ignored by investors who follow index-driven mandates that require investing in China directly.

It is frustrating to sit on large amounts of cash, but we are optimistic that our patience will be rewarded in the long term. Despite the drumbeat of negative news from the Middle East, the future has rarely looked brighter for global investors. Though Chinese businesses are overvalued and under-governed at the moment, the fact that they are available at all to U.S. investors is extraordinary. Even more extraordinary is that India and Eastern Europe are simultaneously racing China towards true market capitalism. This year’s integration of Poland and other Eastern European countries into the European Union has already had practical, positive effects on the moribund labor markets of Germany. More people than ever before are free to work where they want, travel where they wish, and keep what they own. Sooner or later, these countries will produce businesses that we can own at attractive prices.
Longleaf Partners International Fund returned 6.5% in the first quarter compared to a 4.3% return for the EAFE index. At this time last year, most international markets were hitting fresh lows as concerns about the war in Iraq and the Japanese economy drove money out of equities. The change in both sentiment and performance over just twelve months has been breathtaking. To take a few examples, the Japanese equity market reported a 47% gain in the fiscal year ended March 30, its best one year performance in thirty years. The EAFE Index soared 58% and Longleaf International returned 71% over the twelve months. Unfortunately, today’s renewed enthusiasm for equities implies far lower future returns.

Last year at this time, we wrote that we shared your disappointment with recent returns, but that we were convinced that shareholders would be rewarded for their patience. We based this conviction on the abundance of high quality companies available at once-in-a-lifetime prices. The Fund was fully invested, and the price-to-value ratio approached all time lows. Today, cash is nearly 30% of assets, the price-to-value ratio is at an all-time high at 74%, new ideas are scarce, and we have closed the Fund to new investors.

We sold positions that reached our appraisals and trimmed those that approached fair value. These sales were often painful, as in the case of Brascan, where the market finally appreciated the extraordinary leadership and value creation provided by Bruce Flatt. Few companies in the portfolio were as affected by September 11th as Brascan, which through its 50% stake in Brookfield Properties, owned several buildings damaged during the attacks. Bruce and his team redoubled their commitment to downtown New York at a time when many were writing off the area. He opportunistically repurchased shares and created value across Brascan’s portfolio. Other sales, such as Hollinger International, were a relief. Despite unresolved corporate governance issues, the premium value of Hollinger’s assets, in our opinion, was fully reflected in the price of Hollinger’s stock and in the ongoing private auction for these assets. Both Hollinger and Brascan served as reminders of the importance of insisting on a margin of safety between value and price. No one could have anticipated September 11th or the degree of controversy that enveloped Hollinger’s management. We made excellent returns on both investments despite these surprises — 36% in Hollinger and 166% in Brascan — because we bought the businesses at substantial discounts to appraisals that were approximately right. We exited as the market started to agree with us.

This same logic explains our sales of a portion of both Vivendi and SkyPerfect. The SkyPerfect case is particularly interesting because we sold a large block of shares to forced buyers of SkyPerfect when the stock was added to Japan’s TOPIX index in March. This is the inverse of the way we have acquired many of
our Japanese shares over the past five years — via purchases from forced sellers reducing their exposure to the Japanese markets because of either financial pressures or Japan’s declining weight in global indices.

Seeking the lowest-risk, highest-return investments almost always requires us to look dumb when we buy and when we sell. This is another reason that today’s nearly universal enthusiasm for equities makes us nervous. The same forces that gave us SkyPerfect at close to its net cash per share last March are taking it away at more than double the price only twelve months later despite no real change in the underlying business. This trend also explains the contribution of the other three top performers: NipponKoa, Millea, and NTT. All three are Japanese, and all are operating their businesses close to the way we and the market expected. Millea and NipponKoa have seen their book values grow as the Japanese market’s advance lifted their own equity portfolios, and NTT has seen slower declines in its fixed line business than expected, but nothing dramatic has changed in any of our Japanese investments other than their prices. We remain enthusiastic holders of all of our investees, but prices have clearly increased much faster than values have grown.

Fairfax contributed the only meaningful decline in the portfolio after reporting mixed operating results. Current underwriting operations are profitable, the investment portfolio is well-managed, the corporation’s capital position has improved, and problems with discontinued operations appear to be winding down.

Despite the market’s liftoff, we found two new investments in the first quarter: Coors and NTT DoCoMo. Coors was cheap for a number of reasons, but the most relevant for the International Fund was that few understood or appreciated the value of Coors’ substantial U.K. and Canadian businesses. NTT DoCoMo has lost market share in Japan’s advanced mobile telephone market. While the company faces near-term challenges, it also generates over $10 billion of pre-tax free cash flow that has been increasingly used to enhance value via share repurchases.

In normal times, adding two names in a quarter would represent exceptional research productivity. Our expected holding period is five years and we try to concentrate in our best twenty ideas. By this math, we need four new ideas a year to remain fully invested. We are confident that we will continue to find attractive opportunities, even though we will remain patient and committed to the idea that we must protect capital first and earn an adequate return second. We hope that you will share our patience as we wait for the next unique opportunity.
Longleaf Partners International Fund gained 41.5% in 2003 after rising 10.7% in the fourth quarter. The EAFE Index increased 38.6% for the year, and gained 17.1% during the quarter. Since inception in October of 1998, the Fund has returned 16.7% per year against 1.7% for the EAFE. More importantly, we have comfortably exceeded our absolute return goal of 10% plus inflation despite challenging market conditions.

All but three stocks advanced during the year, and only Sompo detracted meaningfully from our performance. The sale of Sompo funded our investment in Millea Holdings. In addition to Millea, the Fund’s largest contributors were Fairfax, Vivendi, NipponKoa and Shaw Communications. Fairfax's operational and investment performance exceeded the market’s expectations while the company strengthened its balance sheet by placing two attractive bond issues and successfully renegotiating its bank lines. Vivendi negotiated the transfer of its entertainment assets to a joint venture with General Electric’s NBC while continuing to streamline its asset portfolio. Shaw’s operating cash flow improved significantly under the capable leadership of the Shaw family, one of our most vested management teams. NipponKoa and Millea both benefited from a combination of improved underwriting performance and investment gains driven by Japan’s stock market recovery.

We sold six positions during the year: Sompo, Amdocs, Tokyo Style, Fiat, Fuji Fire and Marine, and Cable & Wireless. The first five sales were discussed in detail in earlier reports. We sold Cable & Wireless after it reached our revised appraisal. While the sale generated a loss over the time we held the stock, Cable & Wireless contributed greatly to the Fund’s 2003 return. The stock nearly quadrupled from its low after new management resolved several short-term problems. The stock was the worst performer in the FTSE 100 in 2002 and the best performer in 2003.

We purchased two new positions during the year: Millea Holdings and Diageo. In both cases, we had evaluated the businesses and managements for several years, and we have owned Diageo once before. We took advantage of temporary sell-offs in each name to build new positions that have already appreciated.

We received questions about two general topics during the year: our exposure to Japan and our currency policy. After reaching multi-decade lows in the first quarter, the Japanese market delivered exceptionally strong returns over the remainder of the year. The nearly universal pessimism regarding Japan that prevailed only nine months ago helped create a number of qualifying investments. Our bottoms up identification of these opportunities, not our macro view towards Japan, determined our stock selections. We are heavily weighted in Japan.
because these individual qualifiers remain cheap, not because we have any particular insight into the direction of Japan’s market.

The dollar’s weakness dominated headlines this year much as the dollar’s strength was news two years ago. In both cases, the Fund’s returns were somewhat insulated from currency moves by our hedging policies. Our hedges seek to offset the currency-related appreciation or depreciation in foreign stocks. As a result, the return from a hedged position approximately reflects the actual performance of the company’s stock price. We believe that our expertise rests in arbitraging price and value in specific equities, not in predicting currency swings. That said, it is impossible to totally isolate any equity portfolio from currency moves. We generally hedge stocks that have earnings almost wholly in specific foreign currencies.

We enter 2004 pleased with the progress that most of our management partners have made in building value over a difficult period. However, in the short term we face great difficulty in finding new underpriced equities, particularly outside of Japan. At year-end our cash level was approaching 20% and the price-to-value ratio of the Fund’s stocks had moved from near record lows in the first quarter to above 70% in December. By the end of January 2004 when this report was being finalized, cash had risen to over 25% of assets due to over $100 million in net inflows combined with several portfolio sales. Given that new investment opportunities remain elusive and several holdings are approaching our appraisal, your management and the Trustees of Longleaf International have decided to close the Fund to new investors to prevent dilution of our existing shareholders. Current owners can continue to add to their accounts. Other exceptions are identical to those of the Small-Cap Fund, listed in the Prospectus. We will reopen the Fund only when the Trustees and your management partners at Southeastern believe that new, qualifying investments are available and cash inflows would again benefit shareholders.

Despite current investing challenges, we are confident that opportunities will surface somewhere in the world if we remain patient and disciplined. Thank you very much for your support, which was essential in allowing us to make 2003 such a rewarding year.
Longleaf Partners International Fund gained 11.0% in the third quarter compared to an 8.1% return from the EAFE Index. The Fund’s return for the year-to-date was 27.9% versus 18.4% for EAFE.

Several Japanese investments accounted for the bulk of this quarter’s performance. Two of the strongest contributors were property & casualty insurers Millea Holdings and NipponKoa. Each holds large portfolios of Japanese equities that resemble Japan’s broad market indices. These portfolios have increased in value along with the Nikkei, which closed on September 30th up 12% for the quarter and up 35% from its multi-decade low reached on April 28th. In addition, each company is led by a progressive CEO committed to improving shareholder returns via share repurchases and improved investment performance.

Media holdings SkyPerfect and Nippon Broadcasting advanced 64% and 49%, respectively, during the quarter as Japan’s advertising market began to recover and as news reports highlighted the possibility of structural reform at Fuji Television. Fuji Television is both Nippon Broadcasting’s most valuable asset and one of SkyPerfect’s largest shareholders. Despite the strong Japanese rally this year, we continue to find our most promising new ideas in the Japanese market. This reflects both the market’s absurd cheapness earlier this year and the fact that many Japanese companies are increasing shareholder value, despite facing substantial macro-economic challenges.

Outside of Japan, Philips Electronics contributed the most to performance. Philips’ medical equipment business continues to progress while increased capacity utilization across the semiconductor sector has improved the outlook for Philips’ internal semiconductor business as well as for the company’s investee, Taiwan Semiconductor Manufacturing.

With the exception of Shaw Communications, most other positions advanced or posted slight declines. We do not know why Shaw has remained weak despite a global media rally, but we do know that our value is building and that our management partners, the Shaw family, continue to buy shares personally.

We added Diageo to the portfolio early in the quarter when it briefly traded at enough of a discount, and we eliminated our 0.1% position in Tokyo Style. We continue to struggle in our search for new ideas outside of Japan. Markets are generally rich and the most speculative names seem the most overvalued. We doubt that these market conditions are sustainable and suspect that we will be given opportunities to invest our cash. We are content to wait for the fat pitches that we are certain will come our way.
Longleaf Partners International Fund gained 30.7% in the second quarter compared to a 19.3% return from the EAFE Index. The Fund’s return for the first half of 2003 was 15.3% versus 9.5% for the EAFE Index. Almost every stock in the portfolio advanced during the best quarter in the Fund’s history. This performance partly reflected the worldwide post-war equity recovery, but primarily resulted from an extraordinary number of good things at specific holdings.

Fairfax Financial contributed the most to performance. The stock nearly tripled after demonstrating improved operating performance and exceptional investment returns during the first quarter. These results allowed CEO Prem Watsa to strengthen his balance sheet while continuing to take advantage of a hard insurance market. BIL International almost doubled after it successfully acquired London’s Thistle Hotels at an attractive price. Strong operating results at telecom subsidiary Cegetel and high interest in its US entertainment auction drove Vivendi’s performance. Shaw Communications’ performance reflected continued double-digit profit growth combined with strong free cash flow generation. Renault and Fiat benefited from a global recovery in auto stocks that followed the end of formal hostilities in Iraq.

We sold three holdings during the quarter: Amdocs, Sompo and Fiat. Each sale illustrated one of the three components of our sell discipline. We sell when a security reaches fair value (Amdocs), when we can meaningfully upgrade the portfolio’s quality (Sompo), and when we have changed our qualitative assessment of the business (Fiat).

Amdocs, a dominant telecom billing software provider, was the second largest contributor to the Fund’s quarterly results. We added to our Amdocs position as the common stock declined to its lows in the third quarter of 2002, when we, the company and insiders were the major buyers. After Amdocs won a number of competitive contracts, Wall Street’s view changed, and the common stock more than tripled. We sold our position when the shares approached and traded through our appraisal.

The sale of Sompo funded our purchase of Millea, Japan’s largest and strongly-capitalized non-life insurer. A number of technical issues, including forced selling by pension funds and extraordinary pessimism towards Japanese equities, created what may prove to be a one-time chance to buy one of Japan’s bluest chips at a knockdown price. We like Sompo, but we like Millea more at the right price.

We sold Fiat because the business changed and our value declined. We thought that Fiat’s CEO, Paolo Fresco, would exit the automotive business and concentrate on Fiat’s higher quality insurance and manufacturing businesses. Instead,
Fiat fired Fresco, sold its non-auto assets, and recapitalized its car company. Along the way, Fiat lost several billion euros and issued equity twice. Our appraisal declined, but, more importantly, Fiat’s risk profile changed. The stock may work well from this level, but only as a high-risk automotive turnaround.

The only bad news about the quarter is that much of our good news is reflected in current prices. At 61%, our price-to-value ratio remains attractive, and we own a number of undervalued businesses. It has become far harder, however, to find new qualifying investments. We do not consciously try to build up cash balances, but we will not force money into marginal names.

In closing, we reiterate our thanks for your patience during the last year. Despite disappointing performance, the Fund experienced net inflows over the past several quarters. These inflows allowed us to buy more good companies at lower prices and directly contributed to this quarter’s returns.
Longleaf Partners International Fund declined 11.8% during the first quarter compared to an 8.2% loss for the EAFE Index. Most of the Fund’s holdings fell during a quarter of international institutional selling. The war in Iraq and continued forced liquidations by mutual funds, European insurers, and Japanese financial institutions often overshadowed positive company developments.

The Fund’s price declines were proportionally spread across our holdings in Europe, Japan, and Canada. Various combinations of the macro factors mentioned above, rather than company specifics, drove most of these declines. In fact, each of the following companies is making fundamental progress although their stock prices were the largest detractors from the Fund’s three-month performance.

- **Vivendi**: Closed purchase of controlling interest in Cegetel, restructured debt for better financial flexibility, worked on further divestitures to reduce debt, and attracted bidders for entertainment assets.
- **Renault**: Continued to reap handsome returns from its Nissan investment in terms of both Nissan’s profit growth and Renault’s own operations.
- **Fairfax**: Continued to improve combined ratios in underwriting business, posted strong investment returns, and had credit ratings at ongoing subsidiaries affirmed by A.M. Best.
- **Nippon Broadcasting**: Company’s primary asset, Fuji TV, had stable performance awaiting an improvement in advertising revenues.
- **NipponKoa Insurance**: Retired shares, strengthened investment management, and continued underwriting profitably.

Two of the Fund’s biggest disappointments in 2002 had the largest positive impact on Longleaf International in the first three months of this year. Amdocs won several new contracts despite the dearth of telco capital spending. The market began to acknowledge the strategic importance of this business, its financial and competitive strengths, and the capabilities of its management team. Cable & Wireless, led by a new, properly incented management team that resolved a key tax liability issue, has nearly doubled from its lows, and has been the leader in the FTSE index after being the worst performer last year. Our experience with these two companies illustrates the importance of having patience and using appraisals to determine sell decisions. Others might have sold these last year after disappointing results reduced their intrinsic values and caused the stocks to fall. In spite of the bad news we continued to hold both companies because their lower business values remained far above their market prices, and we believed their intrinsic values would grow and be recognized. Our long-term
perspective has thus far enabled us to recoup some of our losses at Cable and Wireless. Thanks to the large margin of safety in our original purchase price, Amdocs is now one of the Fund’s most profitable investments.

Although prices were volatile, our holdings remained largely unchanged. We eliminated our stake in Fuji Fire and Marine and closed our short position in Nissan Motor because Nissan’s value grew to approach its market price. Renault owns 44% of Nissan, but trades at a discount to the market price of its Nissan investment, i.e. the market assigns no value to parent Renault. We shorted Nissan to create a Renault “stub.” The value growth at Nissan and Renault along with declines in the prices of each make an outright investment in Renault more attractive than the stub. Renault now trades at 4x current earnings which are expected to rise as new products roll out this year.

We are disappointed with our stocks’ performance over the quarter and the past two years. However, as the Fund’s largest shareholders, we are optimistic for several reasons.

1) Our price-to-value ratio is below 50% compared to over 60% at this time last year.

2) The quality of the businesses we own is higher than in prior years.

3) Current prices reflect the disappointments we have encountered at a few holdings.

4) Though it is cold comfort to recent shareholders, since inception in 1998 the Fund has compounded annually at 7.7%, outperforming EAFE’s annual loss of (7.1)% by 14.8 percentage points. Preserving capital during a tremendous bear market is testament to the importance of insisting on a large margin of safety between price and value and to picking good businesses and managements.

5) Many international markets are cheap. In the UK, France, and Japan, dividend yields exceed long-term government bond yields.

6) We have the strongest, most stable shareholder group in the industry. Your support, including net inflows of almost $40 million in the first quarter, has enabled us to discount cash flows for years, rather than days, and to buy when others are selling.

Shareholders have recently inquired about both our policy of hedging foreign currencies and our large exposure to Japan. The most important part of our approach to hedging currencies is the honesty it imposes on our appraisals. We
consider not only a company’s price-to-value ratio, but also the cost to hedge the currency before making an investment. For this reason, we have not invested in many emerging markets: after considering the country risk reflected in the cost to hedge the corresponding currency, most emerging market stocks are not cheap enough for us. We hedge only the portion of our portfolio that has meaningful economic exposure to a specific currency. Currently 60% of the portfolio is hedged. Most of our hedges have been against the Japanese yen, a currency that has remained within a narrow band over the last several years, despite a few violent moves. Longleaf International’s key driver of performance has been, and will continue to be, our security analysis. While our currency hedging neither detracts from nor contributes to our absolute returns, it may impact our returns relative to an unhedged index or to a similarly constituted, unhedged portfolio.

We have a large exposure to Japan because we are finding the most attractive companies there. We do not have a macro view on when Japan will exit its many current difficulties, but we do think that Japan’s macro problems are more than priced into our holdings. To the extent that we do look at macro measures, we are intrigued by two statistics listed in a recent Financial Times article:

In 1989 Japan’s GDP was 20.4 per cent of worldwide GDP, while the country’s market value accounted for 39.6 per cent of the global total. Now GDP is 16.9 per cent of global product but Japanese stocks account for a mere 8.9 per cent of total market value. . . Operating profit at Japan’s 1,000 largest companies is estimated by Toyo Keizai, the corporate data provider, to have grown by 24.3 per cent in the fiscal year to March 31 and is forecast to grow by 11.7 per cent in the current fiscal year.

Japan’s equity markets are hitting multi-decade lows at the same time that Japanese companies are getting serious about making money. These trends are linked because the main driver of market declines is forced selling by Japanese banks and insurers to investors who demand a real return. This creates a virtuous circle in which companies become more accountable to shareholders as prices decline and profits improve. We do not know when the market will turn, but we do know that the highest return, lowest risk investments will be made before it does.

Thank you again for your continued support during a difficult period. We are confident that your patience will be rewarded.

Longleaf Partners International Fund lost 16.5% in 2002 after gaining 5.9% in the fourth quarter. The EAFE Index gained 6.5% during the quarter, and declined 15.9% for the year. The Fund fell far short of management’s absolute return goal of 10% over inflation. Only one stock provided meaningful positive returns during the year: Brierley Investments. With the exception of SKY Perfect and Cable & Wireless, most stocks in the portfolio appreciated significantly in the fourth quarter. Despite this rebound, the Fund’s 12-month performance disappointed us as both managers and shareholders.

International markets fell across the board in 2002. Unlike the tech-driven declines of 2000 and 2001, last year’s drop was broad-based. In the short term, widespread market declines can impact our performance. Over the long term, bad markets cannot excuse poor absolute returns. Despite last year’s poor returns, we feel better about the portfolio today than we have at any time since March, 2000.

The bear market provided us with a rare opportunity to reposition the portfolio. We started the year with 20% cash that grew to 30% as we sold Molson, Diageo, and Lagardere, three fully valued businesses that provided great returns. Our price-to-value ratio rose above 60%, and new ideas that qualified for investment were scarce. Starting in the second quarter, we were able to use these proceeds and cash inflows to initiate five positions (Nippon Telegraph, Amdocs, Cable & Wireless, Shaw Communications, and Vivendi) and to buy more of our most undervalued holdings. We ended the year fully invested with a price-to-value in the mid-50’s. Perhaps more important, the overall quality of the portfolio improved. We own more companies that combine high value growth with numerous, expanding competitive advantages.

Appraisals declined at Cable & Wireless, Fiat, Amdocs, and Trizec Properties. By no coincidence these stocks were among the largest contributors to our negative performance. In each case, we paid a performance price that exceeded the value decline, a frequent development in bear markets. We have held on to these names because, despite lower values, these businesses are worth more than we paid and far more than current prices.

The portfolio’s long term value growth is paramount to our investing success. The overall portfolio’s value grew in the low single digits last year. That number is not good long term, but is great compared to the Fund’s 2002 return and in light of the difficult conditions every business faced last year. It is also an improvement over the value decline that we experienced in 2001. Most important, the rise in intrinsic worth combined with lower prices imply a promising future.
Longleaf Partners International Fund fell 19.6% in the third quarter, in line with the (19.7)% return of the EAFE Index. Recent sharp declines in U.S. markets have been matched or exceeded by most international indices. The Nikkei’s 19% year-to-date drop through the beginning of October makes it one of the world’s best performing major indices. Several European markets are down over 40% year-to-date. Emerging markets that strengthened earlier this year have fallen dramatically, particularly when measured in U.S. dollars. Technology, telecommunications, and media stocks continued to lead declines, but few sectors were spared during the third quarter.

The Fund’s poor short-term performance reflected a drop in almost every holding’s price. Highlighting recent volatility, Vivendi was the Fund’s worst performer in the third quarter after being the largest contributor to second quarter returns. Cable & Wireless, Shaw Communications, and Fairfax Holdings hurt the portfolio the most after Vivendi, though several other names experienced double-digit percentage declines. The only positive contributors were Lagardere, Taisho Pharmaceutical, and Fuji Fire. We sold Lagardere and Taisho, as well as O&Y Properties, early in the quarter to fund additional purchases of substantially more attractive portfolio names.

Longleaf Partners International Fund has never experienced negative performance of this magnitude. Our focus on absolute returns reflects our position as fellow shareholders. We take no comfort from the fact that most broad indices exceeded our losses. We do recognize, however, that these global declines reflect a sea change in investor sentiment from the unbridled optimism that reigned in early 2000 to a pessimism not seen in many years, if not decades. Such negative sentiment always creates opportunities for long-term investors who focus on value in relation to price. As your partners, we have two objectives in this environment: to ensure that our appraisals are as realistic and objective as possible, and to ensure that we own the most qualified investments, even if this requires painful portfolio repositioning. We are confident that this intelligent behavior, in combination with support from shareholders, will pay handsome rewards.

The quarter’s best news is that the Fund’s price-to-value ratio now stands below 50%, a level breached only twice before — at the Fund’s inception and in March of 2000. The low P/V indicates that values have remained stable or even grown during the quarter, despite price declines. In addition, our confidence in our management partners at several holdings has increased. Vivendi’s new management team, lead by Jean-Rene Fortou, has already dealt with most of the company’s short-term liquidity issues and is moving the company from a defen-
sive stance to an offensive position. At Fairfax, Prem Watsa’s investment portfolio has been heavily weighted towards long-term bonds and against equities. During the quarter, he harvested gains that strengthened Fairfax’s capital base and facilitated the repurchase of Fairfax shares. At NTT, Norio Wada recently bought back shares from the government.

A few of our companies face short-term difficulties that accounted for much of their negative performance in the quarter. Cable & Wireless has experienced continued weakness in its global telecommunications business, and Fiat’s auto losses have mounted in the face of sustained competition and a weak European car market. Most of our companies, however, have shown stable or even solidly growing values as they have emerged from the uncertain year following September 11th. Our conservative appraisals reflect the short-term problems that we can measure and don’t assume a quick return to growth. The sub-50% price-to-value ratio would be even lower if we either took into account a rapid return to normal profitability or lowered our discount rates to reflect current interest rates.

We own a portfolio of outstanding businesses run by good partners. We acquired many of these companies at low prices in the midst of a global equity meltdown. Our buy list far exceeds our capacity to accommodate new names. We do not know when the markets will turn, and we share your unhappiness with recent performance. We are extremely optimistic, however, about future returns and hope you will follow us by adding to your investment in the Fund.
Longleaf Partners International Fund declined 5.32% in the second quarter compared to a -2.12% return for the EAFE Index. The Fund’s year-to-date performance was -1.94% versus -1.62% for EAFE. The dollar’s recent weakness neither meaningfully helped nor hurt the Fund’s absolute performance because we hedge our currency exposure.

Three months ago, we held over 25% of assets in cash, the price-to-value ratio exceeded 60% for the first time in the Fund’s history, and we faced great difficulty finding new ideas. Today, we are almost fully invested, our price-to-value ratio is below 60%, and the portfolio’s quality is near an all-time high. Our newest investments have been in the technology/telecommunications/media world that supposedly belongs to “growth” investors. Vivendi, Shaw, NTT, Cable and Wireless, and Amdocs are recently purchased holdings that had declined between 60% and 90% from their highs in 2000. These declines do not guarantee that the stocks are cheap, but they do highlight that the difference between Longleaf and many growth investors is not the businesses we own, but the prices we pay.

Assembling today’s portfolio carried a cost in short-term performance. The largest detractors from the quarter’s return were two new positions: Shaw Communications and Amdocs. Shaw’s Canadian cable business is worth considerably more than today’s price and CEO Jim Shaw, a partner we know well from Longleaf Partners Small-Cap’s previous successful investment, is working to close this gap. We cannot predict when the market’s disdain for all things communications related will reverse. We are content to wait for this shift as long as Shaw’s value continues its double-digit growth.

Amdocs suffered from the same negative sentiment that battered Shaw, NTT, and Cable & Wireless. Our initial Amdocs appraisal was too high because we underestimated the impact of wireless industry turmoil on Amdocs’ new business. The market’s overreaction to Amdocs’ reduced prospects, however, created a more attractive buying opportunity. Amdocs trades at around $8 per share today. The company has over $2.50 per share in net cash and a solid recurring revenue base that accounts for two-thirds of sales. The business generates free cash operating margins in the high teens and dominates the critical niche of telecommunications billing software, an area where spending can be deferred, but not abandoned. At today’s price, Amdocs trades at less than eight times reduced forward cash earnings. Management is heavily invested, and the company is repurchasing shares.

Vivendi, another holding added during the quarter, contributed positively to performance. We have owned many of Vivendi’s assets previously, first at MCA and then at Seagram, and are confident that even the most conservative asset
appraisals comfortably exceed Vivendi’s liabilities. Recent changes to manage-
ment and the board have been positive, and we believe that short-term liquidity
concerns are overblown.

BIL International and our Japanese investments also made positive contributions
during the quarter. Collectively, these investments were the most out of favor
names in our portfolio as little as six months ago.

For the first time in many months the Fund has more ideas than cash. We
encourage you to join us in adding to your investment.
Longleaf Partners International Fund rose 3.6% in the first quarter compared to a 0.5% return from the EAFE Index. Most international markets, with the exception of Japan, have followed the U.S. into overvalued territory. Even Japan’s Nikkei average rallied nearly 30% after reaching a multi-year low in February. The weakness in telecommunications stocks, which weigh heavily in the calculations of most non-U.S. indices, has obscured a steady upward trend in prices and valuations in most major markets.

Our portfolio companies performed well during the quarter — in most cases corporate values grew steadily. Prices, however, outstripped the improvement in business conditions. The result was the sale of fully-valued holdings such as Molson and Diageo and an increased cash position due to the challenge of finding new opportunities.

Diageo and Molson exemplify why we focus on business, people, and price at the Longleaf Funds. Both businesses are bulletproof: Molson has a nearly 50% share in Canada’s duopoly beer market, and Diageo boasts the world’s highest quality branded spirits portfolio. No amount of capital could dent these franchises even if they were poorly managed. Fortunately for us, Dan O’Neill at Molson and Paul Walsh at Diageo each possess the rare combination of superb operational skills and exceptional capital allocation abilities. Each partner has raised margins at his core business while simultaneously increasing value through the disposal of non-core assets, intelligent add-on acquisitions, and/or share buybacks. Because of their superior management our appraisals grew at a high double digit rate over the last two years, despite the slowdown in most economies.

The final element of our approach is price discipline. The buy and sell decisions for the two companies focused on our own appraisals and ignored short-term market sentiment. Both franchises were available in early 2000 at 60% of our conservative appraisals as the rest of the world chased overvalued tech/media/telecom stocks because they were assuming ever larger roles in indices. Today, both businesses sell above their values because this process has reversed: indices are stagnating as telecommunications stocks drop, but non-tech companies are reaching extended valuations with index-oriented managers racing to “re-weight” portfolios. We achieved a total return of 71% at Diageo and 139% at Molson while taking minimal risks.

Other than the sale of Molson and Diageo, the portfolio was mostly unchanged. We sold MOS Food and Tenma as part of our ongoing effort to focus on companies where we can build full positions. We also sold short Taiwan Semiconductor, which we own indirectly through Philips’ Electronics. As in all
of our short sales, this is not a “naked” short, but a hedge that lowers the price-to-value of Philips’ remaining businesses.

The largest contributor to the quarter’s performance was Brierley Investments. The announced sale of several London hotels at a price far higher than the market expected confirmed our appraisal. Nippon Broadcasting and Hollinger also made solid contributions as the market recognized their extreme undervaluation, even in the face of the difficult advertising conditions that also contributed to NewsCorp’s decline. Other decliners included Fiat, which suffered from continued delays in executing its turnaround plan, and Nissan Fire, which negotiated a disappointing merger agreement with Yasuda Fire.

At quarter-end our cash position (net of short sales) was approximately 25%. Cash reflects our difficulty in finding qualifying names, not a top-down asset allocation policy. We have found that patience is rewarded, particularly when overall market levels are excessive.
Longleaf Partners International Fund returned 10.5% in 2001 after gaining 3.4% in the fourth quarter. The EAFE Index gained 6.9% during the quarter, but declined 22.6% for the year. The Fund topped most international fund performance for the second year in a row, but its absolute return fell short of our goal of 10% plus inflation. We focus on absolute returns because we invest our money alongside yours. We would happily trade our top relative ranking for five more points of absolute return and value growth.

Our portfolio’s overall appraised value declined while the aggregate price of our common stock holdings appreciated. This decline reflected a slowdown in every industry represented in the portfolio. Indicators as diverse as Japanese TV spot advertising rates, European auto sales, London hotel REVPARs, and insurance underwriting profits all fell during the second half of 2001. The September 11th attacks accelerated these trends, particularly in our insurance and travel related holdings.

In some cases, our appraisals fell because we made mistakes in our assessments of management or of our investee’s ability to withstand a downturn. Fiat, Nissan Fire, Fairfax, and Brierley hurt our performance in 2001, but our value markdowns for these companies were more painful than their short-term price declines. We maintain these positions because today’s prices represent excellent discounts on more conservative appraisals. With the exception of Nissan’s management, which is being replaced, we trust our corporate partners to build value from today’s base.

2001 validated our approach to international investing in several important areas. First, we demonstrated the benefits of a partnership approach with international managements despite the barriers raised by distance, language, and disparate corporate governance frameworks. Our greatest success was DeBeers, not only because we nearly tripled our original entry price, but also because our efforts helped increase the takeover bid for all shareholders. In Japan, Ezaki Glico repurchased 10% of its shares in a single day after three years of discussions with us regarding the merits of buybacks. Our partnership with NipponKoa has helped CEO Ken Matsuzawa implement share repurchases and introduce an investment committee that will include outside advisers.

Second, we showed that waiting for qualifying investments makes sense when opportunities are scarce. Our 20% cash position blunted the impact of September 11th and positioned us to purchase excellent companies such as Philips and Lagardere at bargain prices.
Third, we demonstrated the depth of our international research effort. Normally, we buy only a few names per year. In 2001, we initiated ten major positions and invested nearly a quarter of the Fund in a one-week period in September. Our investment team’s prior analytical work and knowledge of managements enabled us to quickly buy five previously owned companies, including Ezaki Glico, NewsCorp, and Nippon Broadcasting, when their prices dropped. Jim Thompson’s work from our recently established London office helped update old research and find new investments on short notice. We could not have acted so quickly with such confidence five years ago.

Fourth, we delivered outstanding returns in the three-year period ending in 2001. Three years is not a long-term track record, but it has been enough time to test our approach in widely varied markets. Our three year compounded annual return of 20% nearly doubled our absolute return objective and far surpassed the EAFE Index’s annual loss of 6% over the same period. We believe that our record demonstrates that intelligent international investors can generate excellent absolute returns while taking less risk than the market.

Thank you for your support. Your long-term partnership helps ensure our success.
Longleaf Partners International Fund lost 7.7% in the third quarter compared to a 14.3% decline in the EAFE Index. For the year-to-date the Fund remains one of the only international funds in positive territory, up 6.8% versus a 27.6% loss for EAFE.

Prior to September 11th, international equity markets were already down, and we had begun to purchase new businesses. The attacks and associated tragedies were felt around the world. International markets declined more sharply than U.S. markets as most foreign markets remained open during the days immediately following the attacks. An often-indiscriminate flight from equities accompanied the strong outpouring of emotional support for America in most parts of the world. Three outcomes are reasonably clear:

- The attacks immediately hurt the appraisals of a small number of portfolio holdings.
- Our 20% cash position both cushioned the blow to our short-term performance and, more importantly, enabled us to purchase some excellent businesses at attractive discounts to appraisal.
- Despite markdowns to several appraisals, we end the quarter with a portfolio that is substantially cheaper and more fully invested than one month ago.

The stocks of most of our businesses declined during the quarter, although Molson and Nissan Fire and Marine helped performance. The four companies that impacted our return the most were Brierley Investments, Hollinger, Fairfax, and a new holding, Fiat. Brierley’s ownership of 30% of Air New Zealand and 46% of London’s Thistle Hotels made the company vulnerable after the attacks. Air New Zealand was already in critical condition, and the aftermath of September 11th substantially worsened the situation. CEO Greg Terry has done everything possible to unload Brierley’s position in the airline at attractive prices for two years, but he has been blocked by the government regulators who have contributed to Air New Zealand’s problems. Our Brierley appraisal declined substantially, though not nearly as much as the 49% price drop in the quarter. Brierley remains attractive at today’s price.

Fears of longer and deeper recession hurt the prices of many media related companies including Hollinger, which owns several newspapers including the London Telegraph and the Chicago Sun Times. Advertising revenues will be lower until the economy rebounds, but the company still generates valuable free cash flow, and Conrad Black has an outstanding record in building value. The stock’s 23% decrease in the quarter leaves the price at less than half our appraisal.
Fairfax fell with most insurers of U.S. corporations after the attack. Our Fairfax appraisal, however, did not decline, largely due to Prem Watsa’s conservative investment stance, which included S&P puts that should offset initial loss estimates from the disaster. The market’s overreaction to the impact on Fairfax’s balance sheet allowed us to add to our Fairfax position at attractive prices.

Fiat is an Italian conglomerate in the midst of a transformation led by a Jack Welch protégé, Paolo Fresco. A series of transactions in recent months have reduced Fiat’s exposure to the automotive business while creating tremendous value for shareholders from non-earning assets such as Fiat’s electricity business. We began buying Fiat in late July and added to our position after September 11th, at even more attractive prices.

We bought three other new positions: Sky Perfect, Philips Electronics, and News Corp. The portfolio’s broader geographic diversity partially reflects the fruitful results of Jim Thompson’s efforts in Europe. If current volatility continues, we will soon see another period in which we have more ideas than cash. We encourage you to take advantage of the Fund’s significant discount at 55% of our appraisal and add to your investment in Longleaf Partners International Fund.
International Fund - MANAGEMENT DISCUSSION
by Mason Hawkins, Staley Cates, and Andrew McDermott

Longleaf Partners International Fund remains near the top of most international fund rankings after ending the second quarter up 6% versus a 1.7% decline in the EAFE Index. Year-to-date the Fund is up 15.7% against a 15.5% decline for the EAFE, and for the twelve months ended June 30 the International Fund rose 29.6% while the EAFE fell 24.9%. These results far exceed our absolute annual return objective of 10% plus inflation, and we advise our partners that this level of absolute and relative performance is not sustainable.

De Beers contributed the most to our performance in both the second quarter and the year. The De Beers experience illustrates the market’s long-term tendency to properly weigh value in sometimes surprising methods. De Beers had traded at a substantial, clearly identifiable discount to its liquidation value for decades. When we initiated our position at $14 per share nearly two years ago, we had no idea that management would eventually offer us over three times our initial cost in a buyout. We simply knew that we were buying a world-leading diamond business combined with a portfolio of public securities for much less than half of our appraisal. We knew that management had its own money in the business and that the value was growing as diamond inventories turned into cash and as Anglo American, the largest of De Beers’ public securities, appreciated in value. Some investors are perplexed that we have no idea how or when value will be recognized. De Beers exemplifies that the best buys are often made when a catalyst is unclear but margin of safety, value growth, and management incentives favor us.

Our De Beers return exceeded the proceeds made on the stock because we sold short De Beers’ holding in Anglo American each time Anglo traded at or above fair value. This technique reduced our capital commitment to the De Beers position, increased our exposure to the diamond business at an even cheaper price, and reduced our risk by selling the fully valued Anglo. We have used the same strategy with our new Renault position and its huge holding in Nissan Motor.

The remainder of the International Fund’s portfolio provided broadly based solid returns. Two of our Canadian investments, Fairfax and TrizecHahn, made meaningful performance contributions. Fairfax sold shares in Odyssey Re, its reinsurance subsidiary, at 1.5 times book value during the quarter. This sale provided Fairfax with additional liquidity while demonstrating the company’s extreme undervaluation. Despite its recent rise Fairfax continues to trade for less than its hard book value. The Odyssey Re sale also demonstrated the capital allocation skills of Fairfax’s CEO, Prem Watsa. Watsa is the best positioned of any of our CEO partners for a broad economic downturn, and we are delighted
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that Fairfax remains one of the Fund’s largest positions. No specific events drove performance at our other holdings; good businesses with stable cash flows seem to attract more attention now than they did at this time last year.

This recognition of value over the last twelve months partially explains the Fund’s large cash position. The sale of De Beers along with consistent inflows has given us larger cash resources than we normally hold. We have identified new qualifying investments, primarily in the very depressed Japanese markets. Many of our new ideas have appreciated faster than we could build full positions while others will take more trading time to complete. We view our cash position as an asset because we are confident that investment opportunities will come our way in the near future, particularly with Jim Thompson now in Europe full time.

Last quarter we mentioned operating problems at Sea Containers. These problems worsened during the second quarter while financial leverage increased. A similar story unfolded at United Global Communications. We suspect that both these companies will ultimately succeed, but we sold both positions after financial leverage eroded our margin of safety.

We welcome the many new partners who have joined us this year. If this is your first quarterly letter, we encourage you to visit our website at www.longleafpartners.com and familiarize yourself with our operating principles, particularly our focus on long-term, absolute returns.
The International Fund ended the first quarter up 9.1% versus (14.0)% for the EAFE Index. Over the past twelve months, the Fund has returned 34.6% while EAFE has fallen 26.8%. This 61% relative performance difference is irrelevant to us as your fellow investors in the Fund, as is the fact that for the moment, Longleaf sits atop most international fund performance charts. Our objective is an absolute annual return of 10% over inflation, and we are pleased that we continued to exceed this goal in the first quarter.

De Beers, our largest position, contributed over half of the Fund’s net gain during the quarter after management proposed a buyout of the diamond business. The outcome of this bid remains unclear, but whatever the result, the proposal highlights the attractiveness of the De Beers diamond franchise.

Our investments in Nippon Fire and Nissan Fire both generated good returns as the benefits from each of their upcoming mergers became clearer. These two stocks’ outperformance of their peers rewarded our strategy of focusing on only the best managed of the very undervalued Japanese non-life companies. Olympia & York’s strong performance reflected solid underlying growth throughout its Canadian real estate portfolio as well as plans to realize value by separating higher-risk development projects from the stable, high-yielding commercial portfolio. Despite their appreciation, all three of these positions remain undervalued.

Diageo, Fairfax, and Sea Containers were the only stocks that meaningfully detracted from the Fund’s performance during the quarter. Diageo reported excellent results in its core spirits business, but declined in response to its Burger King subsidiary’s weak U.S. and European sales. Burger King’s problems will become clearer as we learn more about the impact of foot and mouth disease in Europe. Whatever happens will have a minor impact on our appraisal because Burger King represents less than 10% of Diageo’s earnings.

Operational problems at Fairfax and Sea Containers were more serious. We have lowered our appraisals of both companies as Fairfax’s underwriting results suffered and Sea Container’s passenger transport and container leasing business slowed during the second half of 2000. Although we are watching these positions carefully, we have confidence in the capability of Prem Watsa at Fairfax and Jim Sherwood at Sea Containers. Both men have spent their lives building these companies and have invested most of their net worth in the stocks.

We added positions in Ezaki Glico, a Japanese confectionery company, and Tokyo Style, a Japanese fashion retailer. Ezaki Glico’s snack business has grown and margins have improved despite the Japanese economy’s weakness. The company trades at less than two times cash flow and has significant cash reserves.
on its balance sheet. Tokyo Style’s retail business margins have expanded on flat sales. More important, we are buying the company for less than its net cash per share.

We sold two railroad companies: Wisconsin Central and Canadian Pacific. Our experience with these two companies illustrates the importance of exceptional management partners: our appraisal grew at Canadian Pacific under David O’Brien’s stewardship while our value declined at Wisconsin Central as management turmoil conspired with bad luck to reduce earnings. The ultimate profitability of both positions underscores the importance of buying with a large margin of safety between price and value.

We enter the second quarter with over 25% cash. Our price-to-value ratio remains compelling at 54%, but for the first time since the Fund’s inception we have more money than ideas. Despite the carnage evident in the double digit declines of the indices and the bubble’s favorite companies, we are having difficulty finding qualifying investments because many undervalued stocks appreciated over the past year. We cannot predict the market’s behavior over the short term, but we are confident that continued inefficiencies in the global equity markets will bring good businesses back within our reach. We view our cash position as a tremendous advantage in this context.
Longleaf Partners International Fund returned 25.9% in 2000 after gaining 2.2% in the fourth quarter. The EAFE Index lost 3.2% during the quarter on its way to a 15.2% decline for the year. In U.S. dollar terms, every major index in the world outside of China ended lower in 2000. In most cases, declines were significant double-digit drops driven by the bursting of an overseas technology bubble even more inflated than that in the United States. From the March 10th NASDAQ peak, EAFE fell 14% while Longleaf Partners International Fund gained 32%.

According to several publications our Fund was the best performing International Fund during 2000. We are certain of few things, but know that our relative performance has nowhere to go but down. We are focused on absolute return and are gratified that, for the second consecutive year, we nearly doubled our objective of 10% over inflation without taking currency risk.

Our success in 2000 was largely due to the perseverance of our exceptional partners. Our shareholders deserve credit for staying the course during the last quarter of 1999 and the first quarter of 2000 when our approach was wildly out of favor. In a year with massive outflows at most international funds, you contributed cash that allowed us to take advantage of extraordinary opportunities to buy quality businesses at steep discounts. Our management partners also deserve credit for growing and crystallizing values in an environment that encouraged them to throw common sense to the wind and transform their companies into the Wall Street flavor of the month.

Our largest new positions in 1999 were Safeway, Sampo, and Bemrose. All three companies reached our appraisals during 2000 and were sold. In each case, management worked to realize our value — through aggressively repurchasing shares at Sampo, executing strongly at Safeway, and breaking up the company at Bemrose.

In the first quarter we sold Nippon Broadcasting, the largest contributor to the Fund’s performance in 1999 and the second largest in 2000. We used the proceeds from Nippon and Bemrose along with inflows to purchase Molson and Diageo. At the time, Wall Street disdained food and beverage companies because they did not provide double-digit revenue growth. Dan O’Neill at Molson and Paul Walsh at Diageo have tremendous, cash-generating brands and a rare combination of operational and capital allocation skills. We bought their companies near all-time lows, significantly below our appraisals. Both have nearly doubled in less than a year, substantially adding to the Fund’s performance. Despite these gains, Molson and Diageo remain attractive because their values have also grown substantially during our holding period.
Our insurance holdings contributed to Longleaf Partners International Fund’s return in 2000. After nearly two years of steady declines in stock prices despite value-enhancing moves by management, our Japanese non-life investments generated positive returns. Nippon, our largest holding and the fifth largest contributor to the Fund’s performance, has become the most shareholder-oriented non-life insurer in Japan. Despite rising from its low of ¥245 to over ¥400 by year-end, Nippon remains at less than a third of our appraisal. President Ken Matsuzawa is focused on building value like no other manager we have met in Japan. Nissan, our other Japanese non-life position, also rallied from its lows after announcing a merger with Yasuda Fire and Marine. Prem Watsa’s Fairfax, which is benefiting from industry pricing trends as well as Watsa’s skillful investment policies, rose dramatically during the year but remains far below its intrinsic worth.

The continuing rally in oil and gas stocks helped our investments in Gendis, the third largest contributor to the Fund’s performance, and Gulf Canada, which we sold to fund more undervalued businesses. We are grateful to Gendis’ Chairman, Albert Cohen, and President, Allan Mackenzie, who forced the market to recognize a portion of Gendis’ value by distributing part of Fort Chicago, a pipeline company that will bring much needed Canadian natural gas to the United States.

Not all of our investments appreciated in 2000. Brierley, Sea Containers, MOS Food, and TrizecHahn declined during the year. In each case management has taken specific steps to realize value, either by splitting up the company (Sea Containers and TrizecHahn), selling assets (Brierley), or revamping operations (MOS). At Sea Containers and MOS, deterioration in underlying business conditions somewhat explains the stocks’ poor performance, and we are closely monitoring the impact on our appraisals. Brierley and TrizecHahn’s shares remain cheap despite fundamentals that have consistently exceeded our expectations.

Our success in 2000 created an unusually high tax bill generated by distributed gains. As the largest taxable investors in the Fund, we are extremely aware of the importance of tax efficiency. We will not, however, compromise our margin of safety for tax deferral.

The positive results of our approach are that we enter 2001 with few imbedded gains in the Fund’s NAV and have a portfolio selling at a price-to-value ratio of 55%, roughly where we ended 1999. This low P/V indicates that we harvested gains when investments reached appraisal and reinvested in more undervalued names, and that the values grew at those companies we held. We are excited about every business we own, and we have a number of places to invest new cash.
Longleaf Partners International Fund rose 9.6% in the third quarter versus an 8.4% decline in the EAFE Index. Year-to-date, the International Fund is up 23.2% against a 12.6% decline for EAFE. Broad-based advances from across the portfolio drove performance. Fifteen of our twenty-three holdings made positive contributions during the quarter of continued weakness in most international markets.

Relative performance does not drive us, but when it is this strong, we remind our partners of our objective. We want to achieve returns of at least inflation plus 10% while taking little business risk and eliminating foreign currency exposure. Our foreign currency policy has not and will not impact absolute returns. Most of our peers do not hedge. As a result, hedging has helped our relative performance this year. We hope that our partners share our focus on the absolute performance of our underlying equity picks, because relative factors will not always swing our way.

The largest contributors to our performance this quarter were our investments in the non-life insurance industry. Nippon Fire and Marine, the Fund’s second largest holding, appreciated 39%. Ken Matsuzawa is transforming Nippon from a well-capitalized and well-operated Japanese non-life insurance company to one that is also focused on building shareholder value. To that end, Nippon has repurchased significant amounts of its undervalued shares, established share ownership requirements for management, and is reviewing a stock option plan and bringing outside members to its board. Meanwhile, many competitors have made capital allocation blunders by investing in undercapitalized banks and life insurance companies. While the market has partially recognized Matsuzawa’s operational and asset-management efforts, the company continues to trade at a dramatic discount to its liquidation and ongoing business values. Nissan Fire and Marine also advanced strongly during the quarter, helped partly by management’s decision to repurchase 2% of outstanding shares.

Fairfax Financial’s rise reflected both operational improvements driven by higher renewal policy rates and recognition of Fairfax’s extreme undervaluation. We sold our position in Sampo Insurance as it approached our appraisal after returning nearly 70% over the past year, thanks to the exceptional work of Sampo’s management team.

Several other companies made key contributions to the Fund’s performance. DeBeers continues to generate cash at an unprecedented rate while positioning itself to become the “supplier of choice” to the diamond market. Although DeBeers advanced over 10% during the quarter, almost all of this appreciation
reflected the price rise of its holding in Anglo-American, a global mining conglomerate that we believe is fairly valued.

Molson’s new management has cut costs and strengthened its beer brand faster than we had hoped. The stock advanced 18% during the quarter, but because management has built value at nearly the same pace, the company remains undervalued. Gendis resolved a key lawsuit that leaves the company with a hard asset value of nearly $12.00 per share and no financial risk. Even after a 27% rise during the quarter, the company continues to sell at a large discount to appraisal.

Two positions hurt our performance this quarter, Brierley Investments and Wisconsin Central. Public quotes for Brierley’s subsidiaries and Brierley itself declined during the quarter, even though Brierley reported results that surpassed our expectations. Operations at all three core investments are proceeding better than hoped, and CEO Greg Terry’s smart investments have offset the company’s structural exposure to weak economies and currencies in Southeast Asia. We remain excited about our opportunity at Brierley. At Wisconsin Central fuel prices hurt margins and growth in all three locations (North America, U.K., and New Zealand) slowed. New management at each rail is working to turn around results. The company is attractive to larger railroads which are prohibited by the Surface Transportation Board from executing mergers until June 2001. We have filed a 13-D to enable us to have open conversations with management and other large shareholders to chart an optimal outcome. The company remains at 50% of appraisal.

We used cash inflows and the proceeds from our Sampo sale to add to existing holdings and fund three new investments. Tricon Global Restaurants’ KFC, Pizza Hut, and Taco Bell brands are well known in the U.S. We bought the position in the International Fund because over a third of Tricon’s current value is in its international operations. More important, Tricon’s incremental investment dollars are going to international expansion, where the company consistently generates high margins and double-digit returns on capital. We also purchased Brascan, a Canadian conglomerate whose most valuable asset is Brookfield, one of the highest quality office real-estate companies we have encountered in North America. Finally, we also purchased Tenma, a Japanese manufacturer of household molded products run by an owner operator and available for less than the net cash on its balance sheet.

We are pleased with our performance this year and excited by our possibilities going forward. The Fund’s composite price-to-value ratio remains below 60%.
The International Fund ended the second quarter up 10.1% versus a 4.3% decline for the EAFE Index. According to Morningstar, Longleaf Partners International Fund was the second best performing international fund for the period. For the year-to-date, the Fund is up 12.4% while the EAFE has fallen 4.6%.

The Fund’s performance was broad-based: eighteen of the twenty positions we hold advanced. We are already benefiting from the opportunities we had in the first quarter to reshape the portfolio. We bought two of our strongest recent performers, Molson and Diageo, when, during the first quarter’s global disgorgement of branded consumer goods, portfolio managers abandoned these unassailable franchises to chase momentum stories. Corporate activity quickly eliminated much of the large imbalance between prices and values. The recently announced takeovers of Bestfoods and Nabisco in the U.S. have highlighted the values of these businesses, and our portfolio has benefited.

Our three largest contributors were positions that we have discussed previously: Gulf Canada, Safeway PLC, and Nippon Fire and Marine. Despite nearly doubling since our initial purchase, Gulf Canada remains undervalued relative to the asset value of its natural gas and oil reserves combined with its tremendous exploration potential. The continuing strength of energy prices has driven consolidation in the Canadian oil and gas market at prices that support our conservative appraisal.

Safeway and Nippon declined to inexplicable levels during the first quarter. We increased our positions because our partners continued to add value — Carlos Criado-Perez at Safeway grew both same store sales and market share, and Ken Matsuzawa at Nippon executed the company’s first stock buyback. During the second quarter, their efforts were partially recognized as the shares recovered. Prices of each, however, remain low, and our appraisals have risen.

Two of our largest positions, Brierley Investments and Fairfax Financial, declined during the quarter despite positive developments in their underlying businesses. Brierley CEO Greg Terry negotiated an attractive sale of a portion of the company’s Air New Zealand stake to Singapore Airlines. Brierley’s balance sheet has improved over the past year; progress at all businesses has been positive; and the company has bought in shares. Despite all this, the
stock trades near its all-time low and at its widest-ever discount to our appraisal. At Fairfax, both the underwriting cycle and the investment environment have turned in Prem Watsa’s favor. He is taking advantage of Fairfax’s low price by repurchasing shares at a discount to book value.

We added TrizcHahn to the Fund during the quarter. TrizcHahn is a Canadian real estate company run by Peter Munk, one of the best partners we have ever had at Southeastern. The company is liquidating its Canadian and non-core U.S. real estate portfolio at fair private market prices and repurchasing shares at a significant discount to intrinsic value in the public market. We funded this purchase by completing our extremely profitable sale of Bemrose as well as liquidating two small positions in Ezaki Glico and KFC Japan.

We enter the third quarter with a composite price-to-value ratio of 54% and with a number of exciting research ideas in the pipeline. We significantly increased our own investment in the Fund recently and encourage others to take advantage of the Fund’s compelling opportunities.
The International Fund ended the first quarter up 2.1% versus a 0.4% decline for the EAFE Index. International markets continue to track the U.S. market's infatuation with technology, media, and telecommunications stocks. In the U.K. and Japan, the focus is even more pronounced than in the U.S. This dichotomy, which began to reverse in the last weeks of the quarter, allowed us to substantially reshape the portfolio. We begin the second quarter with stronger brands, better partners, and greater discounts between price and value than we ever thought possible.

We bought Diageo, Molson, and Fairfax Holdings during the quarter. Diageo's brands include the world’s most popular collection of spirits (including Johnnie Walker and Smirnoff), as well as Pillsbury, Burger King, and Guinness. Molson has over 40% of the Canadian beer market and has been restructured by an exceptional new management team. Fairfax Holdings’ Prem Watsa has a reputation in the insurance industry matched only by Warren Buffett. Watsa has an outstanding long-term record as both an investor and an operator, and has substantially all of his net worth invested in Fairfax. We purchased all three businesses near their recent lows and at extreme discounts to intrinsic value.

We funded our purchases by selling appreciated holdings and through a process of painful pruning. Bemrose, the Fund’s fourth largest holding at year-end, nearly tripled on the announcement of its restructuring program. We sold a portion of our position at attractive prices. During the quarter we liquidated Wassall at our appraisal prior to its takeover by KKR, and we sold our holding in Nippon Broadcasting, another stock that tripled while we owned it.

In addition to realizing gains on these investments, we sold two small positions, Banco Hipotecario and Jarvis Hotels, to concentrate in our best ideas. We continued to emphasize those Japanese non-life investments with the best combination of discount from appraisal and intelligent partners by selling Dai-Tokyo and Yasuda Fire and Marine and increasing our stakes in Nippon Fire and Nissan Fire. We also liquidated a profitable short position in Anglo American. We rarely short securities in the Fund and will only do so as a hedge. We shorted Anglo because we own De Beers whose two assets are its diamond business and a 40% stake in Anglo. The short sale allowed us to lock in a low price for De Beers’ diamond business.

The same forces that provided us opportunities to buy Diageo, Molson, and Fairfax contributed to declines in many of the Fund’s financial, transportation, and consumer product stocks. With the exception of Sampo, our insurance investments declined. Our three transportation related stocks, Canadian Pacific,
Sea Containers, and Wisconsin Central, also fell. Our Japanese fast food investments, MOS Food Service and KFC Japan, lost ground as did UK grocer Safeway, despite dramatic improvements under new CEO Carlos Criado-Perez. Underlying operations have improved and our appraisals have grown at almost all of these companies, and many of our management partners are accelerating growth in value-per-share via stock buybacks.

The International Fund’s price-to-value ratio remains compelling. Price, however, is only one of the three determinants of a successful outcome. The quality of the companies we own is higher, with more competitively entrenched products and outstanding growth prospects. We also have an unprecedented group of management partners who understand the importance of building shareholder value and who act accordingly.
In 1999 Longleaf Partners International Fund gained 24.4% following a flat (-0.3%) fourth quarter. The EAFE Index gained 25.3% for the year after its impressive 16.6% gain in the last quarter. We comfortably exceeded our target of generating a 10% return over inflation, and perhaps more importantly, we achieved this return with a low-risk portfolio. We bought some of our best performers below liquidation value, and our foreign currency exposure was hedged. (Please refer to page 20 for specific contributions to the Fund’s 1999 performance.)

Nippon Broadcasting was the single largest contributor to the Fund’s performance. The company’s price rose to partly reflect the value of its 34% stake in Fuji Television, one of Japan’s three public broadcasters. Despite a near tripling from its lows, Nippon Broadcasting continues to sell at a discount to both its intrinsic value and its liquidation value. De Beers was our next-largest contributor; it has doubled since our purchase, but the company’s value has grown nearly as fast because management exchanged various minority ownership interests in commodity businesses for a larger controlling position in Anglo-American Corporation, and profitably turned large amounts of its diamond inventory into cash. De Beers’ diamond franchise remains undervalued.

We sold two of our large contributors, Highland Distilleries and Philips Electronics. Highland’s management confirmed our assessment of intrinsic value by taking the company private for cash at a slight premium to our appraisal. We sold Philips in the fourth quarter when we found other positions at more compelling discounts.

Several of the Fund’s largest positions declined during the year. Meanwhile, management built value, and made these holdings even more attractive than when we first purchased them. At Brierley Investments management successfully shed non-core assets, reduced debt, and built value through share repurchases. The company sells at half its liquidation value and at an even wider discount using recent comparable transactions to appraise its three major assets. Brierley’s stock fell primarily because it was removed from the New Zealand stock indices pending a move to Singapore. Index membership has nothing to do with intrinsic value, and we are confident that Brierley’s management will build value while short-term, non-fundamental factors impact the price.

Olympia & York Properties also suffered a significant decline, along with most of the Canadian real estate industry. Philip Reichmann, O&Y’s CEO, is the consummate owner-operator who is eager to close the nearly 50% gap between
the market price and stock’s value, which a number of private market transactions over the past year have confirmed.

We used sale proceeds and new assets to acquire a number of new positions, the most significant being Safeway, Bemrose, and Sampo Insurance. Safeway, our largest holding, is the UK’s fourth largest food-retailer. Its price declined after Wal-Mart’s decision to enter the UK market via the acquisition of a competitor. Safeway’s management team, led by CEO and Wal-Mart veteran Carlos Criado-Perez, has successfully improved operations and positioned the company to build value either independently or via merger in this consolidating industry. Our fourth largest position, Bemrose, is a UK promotional marketing and commercial printing company. The stock price suffered because of weakness in the printing business and problems integrating two small acquisitions. The promotional marketing side, however, continues to grow in double digits. Management has demonstrated its shareholder orientation by selling a portion of the business at a 70% premium to its implied market value and returning the cash to shareholders. Sampo is Finland’s largest non-life insurance company, and is our sixth largest holding. Analysts’ obsession with the company’s low reported return-on-equity gave us the opportunity to acquire a stake. Reported returns were low because Sampo holds most of its investments in equities, which depress reported returns, but are the key ingredient in rapidly building book value.

Our new positions became available partly for the same reason that the Fund’s relative performance declined in the second half of the year: a polarization in international markets that favored technology and telecommunications stocks at the expense of most others. In Japan, despite the Nikkei’s 37% rise, 80% of stocks actually finished down for the year. In Europe, 70% of returns were delivered by 12% of the market, mostly telecommunications stocks.

Our portfolio demonstrates the market’s current extremes. Our Japanese non-life insurers hold equities that have appreciated by 10-20% on average over the past year. This equity appreciation combined with profitable underwriting results has pushed up asset values faster this year than at any time in the past decade. In addition, three non-life companies have announced a merger, and four have initiated stock buybacks. Nevertheless, after a brief rally this summer, most non-life stocks are down for the year and sell at historic discounts to their liquidation values. Nippon Fire and Marine fell despite President Ken Matsuzawa’s consistent demonstration that he is one of Japan’s most shareholder-oriented CEOs.

In Europe, Nokia delivered one of the continent’s best performances and nearly doubled in the second half of the year. Sampo is Nokia’s third largest share-
holder, and Nokia’s increase at market value added nearly 33% to Sampo’s NAV. Sampo announced a buyback, a value-neutral merger, and a number of wise reinvestments of harvested Nokia gains, yet Sampo’s discount to NAV deepened.

We are thankful that the dichotomy in international markets has provided us the opportunity to steal great companies at discounted prices. Earlier in 1999, we wondered if we had missed the Japanese market. Now, many of the companies we analyzed last year are available at lower prices in an environment much more supportive of creating shareholder value. In Europe, some of the best consumer brands in the world are trading at new lows. Most important, the companies we already own are building value via share buybacks and other wise capital allocation decisions. We are excited about the implied long-term returns from our portfolio. Thank you for your partnership.
Longleaf Partners International Fund gained 1.8% in the third quarter versus the EAFE Index’s 4.0% return. In 1999 the Fund is up 24.8% versus 7.4% for the EAFE Index.

The quarter’s slight gain masked several significant portfolio successes that demonstrate the advantages of a disciplined, long-term approach to appraising businesses. Highland Distilleries and Nippon Broadcasting rose 33% and 51%, respectively, during the quarter. Highland rose upon a cash takeover bid that valued the company at 425p per share compared to our cost of 247p. Nippon Broadcasting’s rise reflects the market’s partial recognition of the value contained in Nippon’s large ownership of Fuji Television, one of Japan’s three primary television networks. When we bought our positions, many analysts recognized the companies were undervalued. Most analysts avoided the shares because they could not identify a “near term catalyst” that would force recognition of intrinsic value. Longleaf’s approach allows us to benefit from the market’s short-term focus while protecting ourselves from overpaying.

The Fund’s gains were tempered by declines in four positions: Wisconsin Central, our Japanese non-lifes excluding Yasuda Fire and Marine, Brierley, and Safeway PLC, a U.K. grocer added during the quarter. Wisconsin Central, the international rail operator gave up earlier gains as Wall Street took a bearish view of transportation stocks in general, and rails specifically. Our appraisal of WCLX has remained steady. Wisconsin Central’s managers own a significant amount of the company, have been successful rail operators, and have a track record of maximizing shareholder value. The performance of Japan’s non-life sector has stabilized since the end of the quarter, and we have seen increased consideration of shareholders, including the initiation of share buybacks by two companies. Brierley continues to sell for a substantial discount to the sum of its parts. Speculators hoping for an asset sale have been disappointed and sold shares. Chairman Selwyn Cushing continues to build value for shareholders and has capitalized on this sell-off by initiating a buyback of 13% of shares outstanding. Safeway declined in part because of competitive pricing fears related to Wal-Mart’s purchase of Asda. Safeway has locations that cannot be replicated in supply constrained markets and has hired Carlos Criado-Perez, a former Wal-Mart international retail expert, to improve cash flow from operations.

In addition to Safeway, we added Sampo Insurance Company to the portfolio. Sampo is a Finnish non-life insurance company with significant exposure to equities and rapidly improving underwriting results. The company has undergone a corporate restructuring which will enable operations and margins to improve. Management is shareholder oriented and incentives are tied to the performance
of the stock. Sampo contributed positively to the quarter’s result, and remains well below our appraisal.

We used cash inflows (the Fund now has $306 million in assets) and proceeds from two sales to purchase our new positions and increase ownership in existing holdings. During the quarter we sold the Canadian oil and gas company Anderson Exploration as it approached our appraisal. This investment appreciated over 38% in the year that we owned it. We also sold our stake in Dowa Fire and Marine after management grossly misallocated capital by issuing shares to Nippon Life at a steep discount to fair value. Subsequent to our sale, the stock has declined 21%.

The dramatic moves in the foreign exchange market over the past quarter have not impacted Longleaf Partners International Fund. Because we hedge currency to minimize foreign exchange risk, foreign exchange moves do not significantly help or hurt our performance. In the last three months, the yen has strengthened 12% and both the Euro and Pound have strengthened 4%. This weakening of the dollar partially accounts for the International Fund’s underperformance during the quarter relative to the unhedged EAFE Index and to unhedged international funds. We add value by appraising businesses and assessing managements, not by predicting currency movements. Our long-term results will reflect our abilities.

The Fund’s successful first year has not diminished our opportunity. Although many investments have appreciated, we have been able to rebalance the portfolio into our most undervalued holdings and add qualifying new names. The total portfolio is priced at less than 60% of our appraisal, and we are continuing to add to our personal stakes.
Longleaf Partners International Fund continued its strong performance in the second quarter. The Fund returned 15.7% versus 2.2% for the EAFE Index. Since inception last October, the Fund has grown from $27 million in assets to over $240 million while returning 33.6% against EAFE’s 14.4%.

The portfolio’s strength was broad-based with most positions positively contributing to performance. Gulf Canada, our second largest holding, provided over 20% of the Fund’s return. The stock has more than doubled from its low at the end of last year as the gross undervaluation of Gulf’s quality assets has been partially recognized. With Gulf included, our top ten positions at the quarter’s outset accounted for over 85% of the International Fund’s return.

The Fund’s largest contributors benefited from the recovery in both pricing and sentiment for various global commodities, particularly oil and diamonds. We are not commodity traders and do not pretend to know the long-term outlook for these products. We selected these companies because they were cheap, even using prevailing depressed commodity prices, and because they are run by exceptional partners who can build value during a downturn. Our appraisals have continued to rise and our partners are poised to take advantage of a more positive market. These companies, consequently, remain incredible values despite their stocks’ recent increases.

Japanese investments represent roughly one third of the portfolio, but contributed only 15% of the return. The Japanese market has continued to recover, outperforming most other developed world markets. We have two types of holdings: non-life insurance companies and industrials such as Nippon Broadcasting, Kentucky Fried Chicken Japan, and our newest position, MOS Food Services, which sells Japanese style hamburgers and is the most shareholder-oriented company we have met in Japan. The industrials have delivered high single digit or double-digit returns this year while the non-life’s are flat. This divergence has made the non-lifes even more attractive than they were when we began our research in Japan because they hold large portfolios of Japanese equities that broadly reflect the Nikkei Index. The Nikkei’s 26% rise this year has added nearly 10% to our average non-life’s appraisal before accounting for the growth in the underlying insurance businesses. With prices flat, the non-lifes’ discounts to intrinsic value have increased during a period in which we have become more knowledgeable about individual managements.

We added five new holdings in the second quarter. Despite the recovery of many world markets, we are finding numerous opportunities, particularly in Northern Europe, where we have added one name and are researching several
interesting ideas. We also added our first Latin American position: Argentinean sovereign U.S. dollar denominated bonds. A liquidity crunch combined with misrepresentations concerning the demise of Argentina’s currency board drove sovereign yields well over 13% during the quarter, despite Argentina’s demonstrated commitment to a sound currency, its political consensus on economic reform, a continuing privatization drive, and a recent history of real, domestic-led GDP growth without excessive leverage.

During the quarter many new partners joined us in the Fund, and the cash inflows benefited all shareholders by enabling us to buy some of the companies mentioned above and to increase our holdings in existing positions. Given the abundance of qualifying foreign investment opportunities, we are adding to our stakes in the International Fund. We encourage our partners to do the same.
Longleaf Partners International Fund gained 5.9% this quarter against a 1.0% return for the EAFE Index. We are pleased with this performance and with the continued growth of the Fund from $76 million in assets at year-end to $160 million today. We welcome our new partners.

International markets have continued to underperform most U.S. indices, especially when adjusted for the impact of a strengthening U.S. dollar against major world currencies. Our policy of hedging foreign currency exposure is designed to insulate us from the vagaries of the foreign exchange market and allows us to concentrate exclusively on company fundamentals.

In the first quarter, Japan was a notable exception to international underperformance; the Nikkei rose nearly 2000 points, or about 15%. Most of our Japanese holdings benefited from improved sentiment, and they contributed over $3 million to the Fund’s first quarter performance. Japanese restructuring announcements increased foreign investors’ confidence. We do not make macro calls on market levels, and we have seen few examples of real restructuring in our bottom-up analysis of Japanese companies, including the banks that have attracted much attention. Our Japanese holdings will benefit for a different reason — tax reform.

Japan lowered corporate taxes by 15% and personal income taxes by 20%. These changes help our Japanese investments in two ways. First, corporate values in Japan basically increased by 15% because of the tax savings, thus making our price-to-value ratios more attractive. Second, the lower tax rates should significantly improve aggregate demand at our Japanese businesses.

The dramatic increase in oil prices augurs well for several of our Canadian companies with significant oil and gas assets. During the quarter oil moved from around $12 to almost $17 per barrel. If prices remain at these higher levels, our investments should appreciate, as will our appraisals.

The U.K. market also turned in a strong first quarter performance, though the FTSE’s rise masks continued underperformance by small cap stocks. This two-tiered market resembles that of the U.S. and has created a number of opportunities for the Fund. We increased our existing positions in Wassall and Highland as their prices declined. We also added two new UK positions: Bemrose, a leading producer and distributor of corporate give-away items; and, Premier Farnell, the world’s largest maintenance and repair electronics distributor. Premier Farnell quickly rose to our appraisal and we sold our stake.
In addition to Premier Farnell, we sold three other businesses because they reached our appraisals. Shaw Communications benefited from renewed market confidence in cable companies’ ability to generate substantial cash flows from selling multiple services over their cable networks. Haw Par and Swire Pacific both bounced back quickly from their lows as investors realized the strength of their dominant brands even in slower economic periods. We sold our stake in FDX as we found foreign businesses which were even more undervalued and which had a higher portion of their values overseas. We also sold Seagram which we purchased when the Fund’s assets were only $25 million. As assets grew, Seagram became a smaller portion of the portfolio because its price had appreciated far above our buying level. We sold Seagram when we found significantly undervalued companies where we could own a meaningful stake. The combined appreciation of these liquidated companies added $2 million to the Fund’s first quarter performance.

Philips also contributed substantially to our first quarter results, adding $1.7 million to our return. Under the leadership of Cor Boonstra, this worldwide manufacturer continues to build shareholder value by improving operations in its successful businesses, eliminating unprofitable divisions, and wisely reallocating capital. Since Philip’s value has grown along with its stock price, a material gap remains between the price and our appraisal.

We used proceeds from our sales as well as cash inflows to add to existing holdings and to buy several new companies. In addition to the businesses mentioned above, we bought De Beers, the South African diamond company, and Wisconsin Central, a U.S. based company whose primary assets are overseas railroads in the United Kingdom, New Zealand, and Australia.

We continue to identify exciting overseas opportunities for long-term appreciation, and cash inflows are being invested. Our new partners should have a minimum commitment to the Fund of five years and expect volatility. We will focus on keeping the portfolio concentrated in our best ideas, and removing or minimizing the risks of owning foreign businesses. We have substantially added to our International Fund stake.
In 1998 Longleaf Partners International Fund laid an excellent foundation for future appreciation in addition to showing a strong initial performance. From its October 26th public offering, the Fund returned 9.0% versus an unhedged return of 10.9% for the EAFE index. The International Fund’s underlying equity performance was even stronger because we carried 10-20% cash balances during this period of rapid asset growth. Thanks to your support, the Fund grew from our initial $27 million investment to $76 million at year-end, and at January 31, 1999 has $135 million in assets. We expect continued growth because international markets offer an abundance of sound companies with good partners at tremendous discounts to intrinsic value. These deep discounts include the cost of hedging non-US$ currency risk. Over the past several months our hedging policy dampened returns as the US$ weakened against currencies such as the Japanese yen. As owner-operators we believe this is a small price for reduced currency risk across our portfolio. We want our long-term return to hinge on the performance of the undervalued businesses we own, not on the vagaries of the foreign exchange markets.

The International Fund benefited from corporate activity in the U.K. and from the rapid advance of Asian markets after their summer decline. BTR, a U.K. based industrial conglomerate, added $357 thousand to the Fund’s return. We bought BTR after extreme market pessimism had driven its price down over 50% in six months, despite management’s work to streamline the company and return capital to shareholders via a buyback of 20% of shares outstanding. We sold our stake when Siebe announced a takeover.

Swire Pacific added $611 thousand to the Fund. Swire’s exceptional assets include a controlling stake in Cathay Pacific (one of Asia’s leading airlines) one of two Coca-Cola bottlers in China, and prime Hong Kong commercial real estate. Macroeconomic concerns drove Swire’s shares to a steep discount to our conservative appraisal. The Fund acquired a position at the point of maximum market pessimism and subsequently benefited from Swire’s rapid rise when the Hong Kong market stabilized.

Singapore based Haw Par Brothers added $359 thousand to the Fund’s return for similar reasons. Haw Par owns a highly profitable sports medicine business called Tiger Balm, a number of leisure businesses, and approximately 60 million shares of UOB, one of Singapore’s best capitalized banks. Haw Par declined far below its value on overblown concerns about Singapore during the Southeast Asian currency crisis.
While the Fund benefited from many overseas holdings, its strongest contributor was Federal Express’s $1.5 million appreciation. Although Federal Express has been described recently as an Internet beneficiary, many ignore the company’s important growth story as the dominant player in the rapidly expanding international express market, particularly in Asia. Offshore turmoil often allows us to purchase U.S. headquartered companies like FDX which have material value overseas.

In many ways our companies that have not yet added to the Fund’s return excite us more than those that rapidly approached fair value. These undervalued businesses are managed by capable partners and offer the portfolio’s best opportunities for significant appreciation. Three Canadian natural resource companies, Canadian Pacific, Gulf Canada, and Anderson Exploration, declined considerably over the past quarter, driven by depressed oil prices. These companies are significantly undervalued, even if oil and gas prices remain near historic lows.

Brierley Investments also declined over the quarter. Brierley, a New Zealand based holding company, suffered from management turmoil, excessive debt related to its 1996 acquisition of a U.K. hotel chain, and the general downturn in Asian markets. Under the company’s new management led by Selwyn Cushing we believe these concerns will be short lived.

Our positions in Japan, on the whole, also negatively impacted our returns. Despite this short-term decline, the values in Japan, particularly in the non-life insurance sector, continue to have appeal. Our increased presence in Japan has helped us better identify those management partners most focused on shareholder return.

As we enter 1999, the combination of the Fund’s record low price-to-value ratio, our current management partners, and select opportunities in markets around the world encourage us. The companies in our portfolio have the margins of safety that Ben Graham sought because simply liquidating today’s assets would generate exceptional returns. At prices of less than half current net asset values, our performance does not depend on the businesses growing, though we believe they will.

We welcome those shareholders who have joined us. We anticipate a long and rewarding relationship.