Annual Letter to Investors
December 31, 2015
MAGALLANES VALUE INVESTORS, S.A. SGIIC

Dear Investor,

I am very glad to write our first Annual Letter coinciding with the first anniversary of Magallanes.

Magallanes was founded in December 2014 with the firm purpose of becoming a reference within the asset management industry. Excellence in customer service and added value are our signs of identity. We are convinced that success comes when the client becomes a priority. At Magallanes the client comes first.

We began managing two mutual funds with 30 million Euros of assets under management and a team comprised of four people. Twelve months later, Magallanes manages and advices six investment vehicles, out of which it is worth mentioning two funds in Luxembourg and a Pension Plan, assets under management grew to around 550 million Euros and the team increased from four to ten.

I am pleased to communicate that in November we launched the Magallanes Inside application, tool that facilitates the access via Internet to each client's global position. Moreover, in response to the demand of our clients the latter can now make transactions online.

The year 2015 was full of economic and political events which caused sharp movements in the financial markets, especially in the second semester. As a summary: 2015 was an exercise which started in the high side and ended in the low side.

Within this complicated environment our funds performed well. Detailed performance data of each fund and class may be found in Annex 2. Taking into account all the classes that make up each fund, Europe closes the year with an average return of +4% while Iberia ended with +9%. Thus the balance of our first year of management at Magallanes was positive, achieving our main goal: preserving capital and increasing it in the long run.

We close the year at investment levels close to 87%, just when market sentiment is at its worst due to recent corrections. Nonetheless, it is worth to remember the contrast of current situation with what happened at the beginning of the year when the stock market reached highs of 2015 and our portfolios were "only" invested at 50% levels, by then we said:

> "A scenario of strong appreciations as the present one is not the most appropriate for the prudent investor, for whom the most important thing for the long run resides in the purchase price. This attitude may bring us to appear "away from the market" compared to the rest of participants."
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> *1st Quarter of 2015 Letter to Investors*

For information purposes, the key factors that affected the year were:

- Commercial sanctions and worsening of the warlike conflict between Russia and Ukraine
- Greek sovereign crisis, threat of Euro exit and default risk
- First sharp declines of the Chinese stock market, depreciation of its currency and slowdown of its economic growth rate to levels last seen in the 90s
- Crisis in emerging markets such as Brazil, in part affected by the situation in China
- Related to the previous point, sharp decline of raw materials, especially that of oil which is at its lows of the last ten years
- Emissions scandal of Volkswagen
- Crisis of refugees in Europe, as a result of terrorism threat in Middle East
- End of the "zero interest rate" era in the United States, with the first rise of the official interest rate in almost a decade
- Public debt record
- Closure of one of the most important high yield corporate funds
- Issuance of public debt at negative interest rates

As you can see, the world faces many uncertain factors. This situation is reflected in stock prices, which since last summer have initiated a remarkable correction, accelerating during the first days of 2016. Uncertainty provokes low prices, which will eventually rise again when the latter disappears.

The positive reading for investors like us is that we can benefit from the declines caused by such events to buy good businesses at attractive prices.

The interest of people for the stock market decreases as prices decline and increases as prices rise. I wonder, would these people be less interested in buying their "dream house" if purchase price would be half of that of last month? Now that the prices of certain assets have declined, some of them literally by half, we can see how the interest of many investors also disappears, but we think it can be the right time to buy some companies that previously were highly priced.

It is true that not everything is acceptable. Despite current negative sentiment, there is a great dispersion by asset type, where some countries and sectors are at their historic highs or lows. Some financial analysis firms speak about valuations of the stock market in aggregate terms, saying the latter are fairly, highly or low priced. I believe it does not make sense to talk about the stock market in these terms. Think that if I own 1 Euro and you own 20 million Euros it could be said that in average you and I are millionaires, but the reality is very different.

We are possibly facing one of the biggest valuation divergences in recent history. For example, in the last three years the US stock market has doubled while Brazil, China and Russia have declined more than -30%. Over the last decade the German stock market has also doubled its value while the Greek stock market collapsed, accumulating a decline of more than -80%. Businesses related to the beverage, consumer staple and pharmaceutical sectors have reached new historic highs in 2015. On the other hand, businesses related to the energy, oil, mining or electricity sectors are currently trading at historic lows.

Investors feel comfortable within sectors and countries that are mostly favored and expensive. On the other hand investors seek to avoid those stocks that belong to sectors or countries mostly negatively affected. It is a natural and instinctive reaction of human being. During times of uncertainty the easiest and most comfortable decision (buying what goes up) prevails over the difficult and uncomfortable decision (buying what goes down).

Nonetheless, when prices are high the possibility of losing money increases, and vice versa. As in life, extremely positive or negative situations never last forever.

The recent past is full of examples about assumptions that seemed solid at the time but that over time changed unexpectedly. We all sometime listen to things like: "real estate prices can never decline", "now it is time to invest in China or Brazil, countries in which their economic growth rate will continue to be high over the next decades", or for example, "at current growth rate we will soon run out of oil and raw materials" (when crude oil price was close to $150 per barrel).

Today everything has changed: real estate prices sharply declined, Brazil is at its worst economic moment since the 30s, China grows at half and oil prices trade at its last-decade-lows.

We tend to extrapolate in a straight line what happens to us today into the future, the good and the bad, without considering that along the way there can be important fluctuations. Sometimes the path between two points may not be a straight line.

Regarding our analysis process, along the year we had over 130 meetings, which is the same as to 2 meetings for each company in our portfolio or, in other words, to nearly 3 meetings per week. We read more than 12,000 pages of annual reports which translates into the analysis of 300 years of annual income statements of the companies in which we invest. The result is a total conviction level of each and every business which comprises our funds.

We are permanently focused on the search of companies with unique and specific businesses, with their own risk factors and opportunities. I honestly think this is our main asset: we do not focus on beating the market but on identifying discrepancies between price and value.

We have continued to increase exposure in Antofagasta (look at the commentary on page 4 of the 3rd Quarter Letter to Investors of 2015). Nowadays we are not able to think of a world without copper nor do we conceive an alternative could arise in the short term. Furthermore, Antofagasta is debt free and owns Los Pelambres, possibly the best copper mine in the world both per unit of cost and in terms of average life of exploration.

Continuing with more examples of our investment activity we could emphasize the case of Hornbach. The Do-It-Yourself German company Hornbach Baumarkt presented in mid-December an advance of their third quarter results, which turned out to be a disappointment considering the market was expecting better figures, with the stock declining -10% on the day.

As a result of our conviction on the stock and given the information available, not only did we not sell but decided to take advantage of the sharp decline and increased the holding.

In a world where the immediate result prevails over the long term, where stock holding is comparable to lottery tickets, if you do not win the lottery the normal thing is to throw the ticket away.

For us Hornbach is not a lottery ticket but a business that makes profit, whose intrinsic value is far above its current market price. We are aware such value does not have to be materialized in the short term. Short term investors completely lack the patience and capacity to suffer that long term value investors do have. It is like running a marathon in which the rest of participants are 100-metre sprinters.

Another stock to emphasize would be the purchase of Conzzeta AG, Swiss industrial conglomerate and world reference within the different divisions in which it operates.

Perhaps the name Conzetta does not say much to you but you are probably a user of some of its products. If you are a fan of mountain climbing you would be surprised to know that Conzzeta owns the prestigious sportswear Mammut, competitor of brands like Columbia or The North Face. Mammut is a world reference within the premium sector, number 1 in Germany, Austria and Switzerland and present in more than 50 countries.

Its conglomerate structure makes it difficult to identify the real value of each one of the businesses that comprise the group. Taking into consideration the market prices of its main competitors in each of its divisions the valuation of Conzzeta as a whole would be pretty much twice its current market price.

Among the sales for the year it should be noted both TNT Express and Norbert Dentressangle, as a result of takeover bids received by international competitors. During the second semester we sold the whole position of Temenos Group AG, with accumulated total return of more than +50% in less than a year.

The discipline of our investment process led us to the sale of the whole position as its market price reached our intrinsic valuation. A good company at a high price can turn into a bad investment.

Our communication channels are continuously opened for you all whenever you need it. In this regard I encourage you to attend our first Investors Day which will take place on the 2nd of March in Madrid. Every attendant will have the opportunity to chat with the team of Magallanes and we will be glad to meet your needs and answer any given questions.

As we begin our second year our passion is as strong as in the first day. We are fortunate to work in something we love. We keep working on preserving and increasing your capital alongside with ours.

Thank you on behalf of the whole team of Magallanes for entrusting us the management of your money.

Kind regards,

Iván Martín Aránguez, CFA
Chief Investment Officer

ANNEX 1. STRUCTURE OF THE FUNDS

MAGALLANES IBERIAN EQUITY FI

The fund closes the quarter with an investment level of 86.6%, with its portfolio comprised of 26 Spanish and Portuguese companies.

The portfolio continues to have a clear bias towards the consumer and industrial sectors, where we could emphasize among others: Barón de Ley, Semapa SGPS SA, Iberpapel Gestión, Prosegur and Miquel y Costas. Top ten holdings account for 52.1% of the fund.

Portugal accounts for 22.5% of total investment of the fund.

The predominant size of the companies in our portfolio does not exceed €3,500 million of market cap, accounting for 75.1% of the fund. A 3.9% of the fund is invested in companies with a market cap of over €10,000 million.

Current investment level of the fund seems to be adequate for us. The number of companies in our portfolio will not significantly change in the medium term.

MAGALLANES EUROPEAN EQUITY FI

The fund closes the quarter with an investment level of 86.6%, comprised of 35 companies.

The portfolio has a clear bias towards the industrial manufacturing, distribution and consumer staple sectors; sectors which are represented, for example, by stocks like Orkla ASA, C&C Group Plc, Buzzi Unicem SPA, Thermador Holding SA and Tarkett SA. Top ten holdings account for 39.2% of the fund.

As a result of the stocks in our portfolio the exposure to France, Germany and Switzerland is greater compared to that to other countries, with an aggregated weight of 45.8% for the latter countries.

The predominant size of the companies in our portfolio does not exceed €3,500 million of market cap, accounting for 54.3% of the fund. A 13.5% of the fund is invested in companies with a market cap of over €10,000 million.

Current investment level of the fund seems to be adequate for us. The number of companies in our portfolio will not significantly change in the medium term.

ANNEX 2. RETURNS BY FUND AND CLASS

MAGALLANES IBERIAN EQUITY, FI

FUND	1 MONTH	3 MONTHS	6 MONTHS	SINCE INCEPTION	INCEPTION DATE	INVESTMENT LEVEL
Magallanes Iberian Equity FI "M"	**-0,14%**	**7,77%**	**3,42%**	**8,04%**	29/01/2015	86,6%
Iberian benchmark	-7,13%	1,22%	-9,43%	-5,73%		
Magallanes Iberian Equity FI "P"	**-0,10%**	**7,90%**	**3,68%**	**6,32%**	26/02/2015	86,6%
Iberian benchmark	-7,13%	1,22%	-9,43%	-11,27%		
Magallanes Iberian Equity FI "E"	**-0,03%**	**8,11%**	**4,07%**	**12,72%**	09/01/2015	86,6%
Iberian benchmark	-7,13%	1,22%	-9,43%	2,57%		

Returns net of fees. Iberian benchmark: 80% Ibex35 Net TR + 20% PSI20 Net TR. Data as of 31/12/2015

MAGALLANES EUROPEAN EQUITY, FI

FUND	1 MONTH	3 MONTHS	6 MONTHS	SINCE INCEPTION	INCEPTION DATE	INVESTMENT LEVEL
Magallanes European Equity FI "M"	**-3,40%**	**4,15%**	**0,36%**	**3,47%**	27/01/2015	86,6%
European benchmark	-5,28%	5,31%	-4,01%	0,42%		
Magallanes European Equity FI "P"	**-3,36%**	**4,28%**	**0,61%**	**4,23%**	29/01/2015	86,6%
European benchmark	-5,28%	5,31%	-4,01%	0,43%		
Magallanes European Equity FI "E"	**-3,30%**	**4,48%**	**0,99%**	**4,29%**	09/01/2015	86,6%
European benchmark	-5,28%	5,31%	-4,01%	9,77%		

Returns net of fees. European benchmark: MSCI Europe Net TR. Data as of 31/12/2015