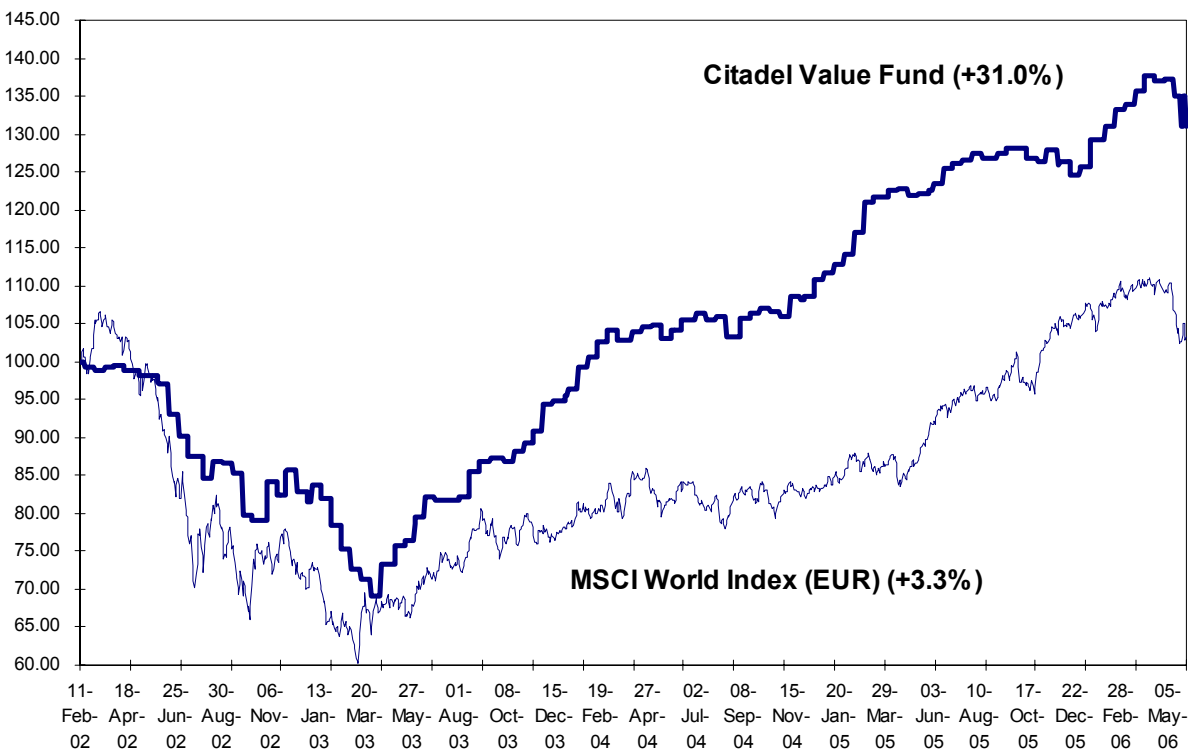




Dear Shareholders,

Your Fund ended its fiscal year on May 31st with an NAV of EUR 130.99 per share versus EUR 122.69 a year ago. Citadel's NAV is up by 4.6% since the beginning of 2006¹. After a sharp rise in the first few months of the year, the share price gave back some of its gains due to the global equity downturn in May. Since inception – a period spanning a little more than 4 years – Citadel's NAV has risen by 31.0%. This performance remains well above the returns achieved in global equities generally during that period as is reflected by the MSCI World Index which rose by 3.3%.

Citadel Value Fund
(performance since inception to May 31st, 2006)



¹ To May 31st versus an estimated (but not official) NAV per share of EUR 125.20 on December 31st 2005

IMPORTANT: An investment in the Fund carries with it a degree of risk. The value of your investment may go down as well as up, and you could lose money on your investment. Past performance provides no guarantee for the future. Investors should read the Fund's prospectus before deciding whether to invest. The opinions and commentary expressed herein should in no way be construed as personal investment advice, they are intended solely to illustrate the Fund's investment strategy and performance.

Citadel Value Fund Performance (as of May 31st, 2006)								
	Cumulative returns			Annual returns				
	Since inception	3 year	1 year	2006* YTD	2005*	2004*	2003*	2002*
Citadel Value Fund	31.0%	66.5%	6.8%	4.6%	12.0%	17.2%	17.0%	-18.4%
MSCI World Index (Euro)	3.3%	50.8%	14.0%	-2.3%	26.8%	6.9%	11.3%	-29.9%
Out/under-performance	27.7%	15.7%	-7.2%	7.0%	-14.8%	10.2%	5.7%	11.5%

* annual returns based on estimated (but not official) NAV on Dec. 31st of each year; first NAV Feb. 11th 2002
source: European Fund Administration, MSCI

Portfolio Holdings (as of May 31st, 2006)		
company	activity	% of portfolio
Altria Group Inc.	consumer goods (food & tobacco)	1.0%
Batenburg Beheer NV	business services (technical installation)	4.8%
Bristol-Myers Squibb Co.	pharmaceuticals	4.9%
Carclo PLC	industrial goods (plastic components)	3.8%
Clinton Cards PLC	speciality retail (card shops)	3.7%
Continental (Grupo) SA	consumer goods (soft-drink bottling)	2.5%
Dewhurst PLC	industrial goods (lift panels & controls)	2.6%
Grolsch (Koninklijke) NV	consumer goods (brewing)	0.2%
Havas SA	media (advertising)	1.6%
Heineken Holding NV	consumer goods (brewing)	5.9%
Lambert Howarth Group PLC	business services (clothing supply & distr.)	5.2%
LandAmerica Financial Group Inc.	insurance (title insurance)	3.0%
Metall Zug AG (part. Scheine)	consumer durables (appliances)	0.8%
Molins PLC	industrial goods (tobacco machinery)	2.2%
Natuzzi SpA	consumer durables (furniture)	3.6%
Nedschroef Holding NV (Koninklijke)	industrial goods (fasteners)	5.0%
Reesink NV	wholesale and trade	0.7%
Sasa Industrie SA	industrial goods (baking utensils)	1.9%
Signaux Giroud SA	industrial goods (traffic signs)	1.4%
Springer (Axel) Verlag AG	media (newspapers)	1.6%
Tamedia AG	media (newspapers)	2.5%
Telegraaf Media Group NV	media (newspapers)	8.0%
Ultraframe PLC	consumer durables (conservatories)	3.0%
Unilabs SA (incl. call warrants 0.01%)	health services (laboratories)	0.8%
Village Super Market Inc.	retail (supermarkets)	5.2%
VLT AB	media (newspapers)	1.7%
Wegener NV	media (newspapers)	5.0%
Wolters Kluwer NV	media (professional publishing)	3.8%
Zehnder Group AG	industrial goods (radiators)	3.0%
Zwack Unicum Rt.	consumer goods (spirits)	3.8%
Cash and other assets and liabilities		7.1%
		100.0%

note: as percentages are rounded to 1 decimal point the sum of the percentages shown differs from 100

Portfolio News

Befitting the Fund's long-term investment strategy, the portfolio companies have not changed dramatically since the semi-annual letter to shareholders for the period ending November 30th 2005. Nevertheless the weighting of various holdings has changed due to both price changes, and new purchases. For example, the holding in **Telegraaf** was expanded significantly. That, together with a recent share price run-up, has made this the single largest holding in the Fund. The investments in **Clinton Cards, Dewhurst, Carclo, Natuzzi, Batenburg, Lambert Howarth and Village Super Market** were also increased. In a number of cases, the shares of these companies had already performed very well. Pleasingly though the underlying businesses are performing such that new purchases were still warranted. Two of the Fund's holdings, both in pharma, were sold in the last half year. In an interesting coincidence they share the same name although they are otherwise unrelated. **Merck KGaA** – the German pharma and chemicals company - proved to be a successful investment with a return of almost 145% including dividends. The US pharma company **Merck & Co**, also a long-standing name in the portfolio although the bulk of the investment was made in the past 12 months, returned 21%. The sole new holding is **LandAmerica Financial Group**. This is a noteworthy stake as it is the first investment in a financial firm since the Fund began. Later in this letter we describe in some detail the latest addition to the portfolio and the rationale behind its purchase.

Global markets rose steadily in the first months of 2006, at least until May when they suddenly reversed themselves and ended the period with a year-to-date loss of 2.3%. While the Fund has been affected by the broad market downturn, it has held up better than markets overall. Generally speaking the broad-based advance in shares seen in the past couple of years had greatly reduced the number of deeply undervalued companies, a fact we have lamented in past letters. Despite this the last six months - before the recent correction - were actually very encouraging. The good performance of many companies has led their intrinsic values to rise, and we have been able to put substantial funds to work in the existing portfolio. Furthermore, we have a number of excellent ideas in the pipeline in addition to LandAmerica which is now in the portfolio. Finally the downturn that began in May is also welcome, at least from the perspective of the new opportunities that it creates.

Anatomy of an investment

In addition to reporting back to shareholders on developments at the Fund, we traditionally take the opportunity in these semi-annual letters to shareholders to delve into more detail about exactly how your money is invested. Long-term performance clearly says a great deal – superior performance over many years is often indicative of a superior approach. However, we also believe that better understanding an investment strategy (assuming that strategy is followed in a disciplined fashion as is the case at Citadel) is instrumental in understanding the risks and returns of an investment.

As referred to above, the Fund sold its holding in Merck KGaA earlier this year, after holding the shares for almost exactly four years. Merck was the first holding in the Fund, and provides an excellent illustration of how Citadel's value philosophy is implemented in practice.

The Fund bought its first shares in Merck in late February 2002, and more in May 2002, at an average price of EUR 32. The shares had fallen dramatically from their high in 2001 as the patent on its large diabetes drug *Glucophage* approached expiry. What drew our attention to the company was the thought that while losing its major pharma product was not good news, the market might have over-reacted by chopping a whopping 40% off its market capitalisation. Certainly on the basis of various valuation multiples such as Enterprise Value to EBITDA or EBITA the shares looked cheap.

As our research progressed a number of facts became clear. Financially the company was in excellent shape, the balance sheet was healthy, and cash flows would remain positive even in a 'worst case' scenario. Furthermore, while the majority of its pharmaceutical profits were derived from *Glucophage*, the remaining products were profitable, showed some growth potential, and were backed by a surprisingly robust new product pipeline. In fact one of these pipeline products had the potential to be a blockbuster (\$1bn+ seller). It was clear that the market was assigning little or no value to this future pipeline. Moreover, the firm's large speciality chemical businesses (LCD

chemicals, pigments, electronic chemicals) and laboratory distribution arm also had substantial market positions, quite reasonable returns and decent growth prospects. The conclusion to our work was that the stock market was ‘throwing the baby out with the bathwater’, i.e. it was more than fully pricing in the loss of one product, but paying little heed to the value in the rest of the business. We attempt when calculating a value for a company to err on the side of conservatism. Thus, in Merck’s case we did not build-in hugely optimistic scenarios for its pharma pipeline, or strong growth at its remaining businesses. Rather, using modest assumptions, we calculated a ‘going-concern’ value for the company of EUR 70 per share several years hence, after the negative impact of *Glucophage* had already been felt. This estimate of intrinsic value was supported by a sum-of-the-parts analysis which showed that the individual pieces of Merck could be sold (assuming going market transaction prices) at a similar or even higher value.

Roughly around the same time that Citadel began accumulating Merck, markets began to plunge. In July 2002, less than 6 months after first purchasing shares, Merck’s stock had fallen by 22% to less than EUR 25. What had seemed to be ‘deep value’ at EUR 32 was now worth a lot less – at least according to the stock market. We were naturally inclined to ask whether our earlier analysis still held. We revisited the case, updated our figures, and spoke again with management. Things had changed but the basic premise still held. The large ‘margin of safety’ which we seek to find in every investment was, as a result of the share decline, even larger. Our estimate of intrinsic value was amply supported by the firm’s assets and their cash generative nature. Even were events to turn out worse than we thought, the company’s shares were demonstrably worth more. We added to the position.

With the benefit of hindsight we could have waited a bit longer as markets plummeted further, dragging Merck with them, albeit at a slower rate. On the 1st of October 2002 the stock hit its historic low of EUR 18.04. This was almost 45% less than what we had paid in February. Although it is an extreme example, it demonstrates the manic-depressive nature of stock markets. Within the space of a year and half from its high in 2001 to its low in 2002, with little new information or unexpected change in its business, Merck’s market value had swung between EUR 9bn and EUR 3bn. This example also demonstrates the futility of attempting to predict stock prices in the short-term. We clearly would have preferred to have bought at the absolute bottom. However, the long-term success or failure of this investment ultimately depended on the correctness of our long-term view concerning Merck’s intrinsic value, and not on our skill (or lack thereof!) at predicting short-term stock price movements.

In its 2002 results, as expected, Merck’s profits fell sharply as *Glucophage* went generic. In 2003 profits recovered somewhat as the rest of the company performed well. A sale of its laboratory distribution business at a reasonable price was announced. This good news was marred by the inexplicable and unnecessary decision to issue new stock at very low prices thereby severely diluting shareholders. 2004 saw a further improvement in its business with some successes from the pharma pipeline including the new cancer product referred to earlier. In 2005 profits and cash flows were well ahead of those in 2001 despite the loss of its key pharma product. These developments were not ignored by the stock market. By January 2006 the stock had hit EUR 76, or more than twice the Fund’s first purchase price, and we sold Citadel’s holding. This was modestly above our initial value estimate of 2002 which had indeed proved overly conservative. While we had by no means predicted exactly how Merck’s business would develop after investing in it, the broad lines of the investment case did prove correct. The stock had been clearly undervalued at EUR 32, and even more so at lower levels. In the short-term this did not prevent a painful, but temporary, loss. In the long-term though it resulted in a successful investment.

This concentration on the fundamentals of individual businesses and assessing their value independently of the stock market is one of the key threads to your Fund’s investment policy. By digging deep into a company and its business, avoiding obvious financial risks, demanding a large ‘margin of safety’ between estimated intrinsic value and share price, and taking a long-term view, we think the odds of continuing to generate good returns are excellent.

LandAmerica Financial – Citadel’s first financial holding

LandAmerica Financial is the third largest title insurer in the United States. Title insurance is a product which is relatively unknown outside North America; however, in North America it is an integral part of real estate transactions. When properties are bought, sold or refinanced, title insurance is required. Title insurance essentially

provides the assurance that the title to a property is correct, without unknown liens, inaccuracies, etc. which might lead to problems for the owner and/or lender.

One of the attractive characteristics of the business is that unlike traditional insurance which is forward-looking, providing insurance against events that may occur in the future, title insurance is backward-looking. It is based on examining the ownership title to a property and ensuring that it is correct. With sufficient due diligence a title insurer has little risk that large claims will need to be paid. Furthermore, the absolute insured value per transaction is relatively low and uncorrelated with other policies. As a result claim costs are only some 4-6% of paid premiums. In contrast traditional insurance policies written today can look profitable for many years, but suddenly be loss making if a particular event occurs. In fact, one of the major problems for investors in evaluating traditional insurance companies is whether past and current pricing adequately reflects the risks assumed. Often many years pass before this can be evaluated with any degree of reliability. Title insurance is much simpler and more transparent for the investor.

Because claims form only a relatively minor part of premiums paid, the cost of title search and examination is the critical factor to a title insurer. Changes in the number of policies (rising and falling essentially in-line with the number of issued mortgages) have a large impact on profits. Beyond achieving certain economies of scale in processing titles, management must keep an exceptionally close eye on costs. When the number of transactions fall, title insurers must quickly cut their cost base if they are not to see their profits melt away. However, even quick and deep cuts to the cost base cannot completely insulate title insurers from sharply falling revenues. This is due to the fact that many costs are truly fixed, and difficult to cut even when business is bad. The industry is cyclical and highly dependent on the health of the real estate market. Nevertheless, over long periods of time and through numerous cycles, the industry has shown itself to be very profitable with high returns and excellent cash generation.

LandAmerica was valued at 90% of its book value when purchased. This seemed extremely low when considering that the company's long term, post-tax, average return on equity was more than 11%. On other valuation measures the conclusion was similar. The company's balance sheet is pristine with a net cash balance, even after excluding the cash held in reserve to fund possible future claims. In an environment of rising interest rates and amidst talk of a housing bubble the market appears to be discounting a sharp tumble in the real estate market. Having analysed the situation in extensive detail several conclusions can be drawn. In certain local markets there is quite probably a housing bubble, but that is considerably less clear-cut for the United States in general. Rising interest rates will certainly slow the housing market, although the number of mortgage refinancings has already fallen off a cliff after reaching its peak in 2003. Encouragingly, LandAmerica has coped well with this fall-off in refinancing business. This is partly due to a successful expansion of its commercial title insurance operations in which it is now one of the few companies able to undertake large complex transactions.

Without having any particular wisdom (unfortunately!) as to what the housing market will do in the short-term, a focus of our analysis was in assessing what the impact would be to the company's intrinsic value *were* a severe downturn to occur. The result was reassuring. The company's value well exceeds Citadel's purchase price even if the US real estate market contracts significantly, providing us with a thick margin of safety. Needless to say the stock price would likely not perform well in such an environment, but the company's value is such that a reasonable return can be expected even with a multi-year wait. However, if a serious slump in the market does not occur, our estimate of LandAmerica's value will likely prove too low.

Uncertainty has returned to equity markets yet we are confident on the prospects for your Fund based on its current portfolio and the new ideas which we are uncovering. We look forward to updating you as the year progresses. Thank-you for your confidence in entrusting your investments to Citadel.

Kind regards,

The Board of Directors
Citadel Value Fund SICAV

June 14th, 2006