

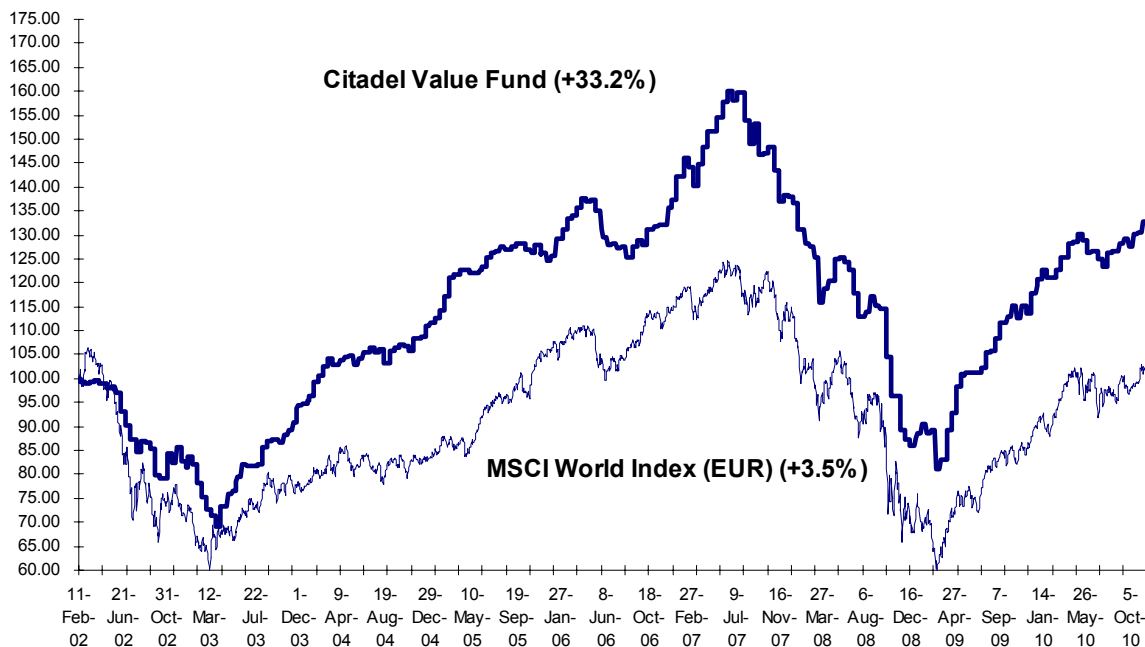


Dear Shareholders,

With the passing of November Citadel reached the half-way mark of its financial year and once again it is our pleasure to report on how it is faring. It has been a decent year thus far despite various jolts of a macro-economic and geo-political nature. As has been the case since mid-2007 stocks still show the propensity to move as one in line with the macro-economic news of the day. Currency and debt markets likewise fluctuated, sharply at times, on new economic headlines. On November 30th the NAV per share was EUR 133.17, which is 11.4% higher than on December 31st. The MSCI World Index in EUR rose by 15.3% (+4.6% local curr.) but the relative performance has fluctuated wildly as a result of differences in currency weightings. As it now looks the Fund should see a positive impact from currencies in 2010, albeit a fair bit less than that of the index. Nevertheless, this is a welcome change after eight years in which currencies depressed results year after year, at times by a lot. The business performance of the Fund's holdings was generally positive and several holdings responded with large share price rises. The portfolio continues to look very compelling as prices are still far too low in the context of the excellent balance sheets and good returns and cash generation which characterise Citadel's holdings. Since inception the Fund is ahead by 33.2% while the MSCI World is up modestly at 3.5%. Note as well this index figure unrealistically includes gross (i.e. untaxed) dividends; the taxed variant is still mired in negative territory at -1.2%.

Citadel Value Fund

(performance since inception to November 30th, 2010)



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 November 30th, 2010)

	Since inception (11/02/02)	2010 YTD	2009	2008	2007	2006	2005	2004	2003	2002
Citadel Value Fund	33.2%	11.4%	36.2%	-35.8%	-0.5%	9.7%	12.0%	17.2%	17.0%	-18.4%
MSCI World Index	3.5%	15.3%	26.7%	-37.2%	-1.2%	7.9%	26.8%	6.9%	11.3%	-29.9%
+/- vs. index	29.7%	-3.9%	9.5%	1.4%	0.7%	1.8%	-14.8%	10.2%	5.7%	11.5%

note: MSCI World Index based on total returns (including gross dividends excluding dividend withholding tax) in Euro's
 * annual returns are based on Citadel's estimated NAV as of Dec. 31st, out/underperformance figures may differ due to rounding
 source: European Fund Administration, MSCI Barra

Portfolio news

The portfolio is in broad lines very similar to that at the end of May, although we made a couple of additions and the weightings themselves changed due to price movements and new purchases. Two new companies were added in this period and none were sold which leaves the number of positions at an historic high of 35. The total number of holdings might grow in the short-time if we find other deep-value prospects though it is more apt to decline as a number of stakes are approaching our intrinsic value estimates. Furthermore there are several relatively small holdings which at some point we are likely to either increase, or dispose of. Despite having deployed cash into new and existing holdings the net cash position, (at 12.5%), is a bit higher than the average in the past reflecting inflows into the Fund in the last six months.

A sizeable new investment was the purchase of US clothing retailer **Aéropostale**. The stock was in the doldrums as investors fled from retail and other consumer discretionary stocks. Aéropostale is a mid-sized chain comprising approximately 1000 stores the bulk of which are in the United States, with the remainder largely in Canada. It sells clothing and accessories under its own brand name to a predominantly teenage target group and recently also launched a new sub-brand (*P.S. from Aéropostale*) to target younger children. The company's business model is based on an outspoken value proposition and it makes active use of planned promotions (2 for 1 sales, etc.) to generate traffic. This positioning served it very well in 2008 and 2009 when same-store sales grew by 8% and 10% respectively whilst many competitors saw big falls. Lately competition has intensified with wide-spread discounting as other retailers shored up their businesses by slashing prices. This has impaired the company's competitive advantage in the short-term, although not in the long-term we believe. The company's design, purchasing and logistics are focused on being as flexible as possible and its inventories are modest as a result. Markdowns are planned in advance rather than by the need to clear excess stocks. Despite lower prices per unit than its competitors its sales per square foot lead the industry by a healthy margin. The company recently announced a sizeable share buyback making use of its debt-free, cash rich, balance sheet. The Fund purchased shares at 4.8X 2009 EBIT. As a reference point another US clothing retailer was acquired several weeks ago for 11.7X EBIT.

A second new name in the portfolio is **BAE Systems**. BAE is one of the world's largest defence contractors with headquarters in the United Kingdom. Its £20 billion in annual sales are mainly generated in the United States, the UK, South Africa, Sweden, South Africa and India with the first two countries accounting for roughly 70%. It produces a staggering array of equipment necessary for those countries' defence including aircraft, naval vessels, armoured vehicles, electronic systems and others. With the wind-down of the conflict in Iraq, and budget conscious governments eyeing defence spending, investors have piled out of defence groups. Even in a beaten down sector BAE's valuation stood out, likely the result of its exposure to the UK where a new government is slashing government spending. It is hard to escape the fact that lower defence spending is not good for BAE. Still, all the major defence companies benefit from large and diversified order books. In BAE's case it is also geographically

diversified. Most programmes have multi-year lives, and some extend as long as 20 years. At any point in time some programmes are ramping up while others are running off. Furthermore a sizeable recurring revenue stream comes from repair, maintenance, upgrading and other services tied to platforms already in service and which, more often than not, have operational lives measured in decades. All this provides a certain visibility and stability to future sales and cash flows. Furthermore, national security demands provide a cap of sorts to the cutbacks that governments can, or want to, realise from defence spending. The Fund purchased BAE at 4.5X 2009 EBIT and a 15% Free Cash Flow yield. This is a valuation which makes sense only if sales were to drop precipitously. After analysing BAE's business we concluded that that scenario was very unlikely. In addition to the low valuation a further attraction is a rich dividend yield of just shy of 5%.

Portfolio Holdings (as of November 30th, 2010)		
company	activity	% of portfolio
Companhia Paranaense de Energia (COPEL), ADR	utilities (hydro-electric power)	5.6%
GS Home Shopping	speciality retail (TV home shopping network)	5.1%
SK Telecom, ADR	telecommunication services (mobile)	4.6%
Continental (Grupo) SA	consumer goods (soft-drink bottling)	4.4%
Aéropostale Inc.	speciality retail (casual clothing stores)	4.2%
Signaux Girod SA	industrial goods (traffic signs)	3.5%
BAE Systems PLC	industrial goods (defence)	3.4%
Toyota Industries	industrial goods (forklifts, engines, auto's & parts)	3.4%
Bristol-Myers Squibb Co.	pharmaceuticals	3.2%
Bijou Brigitte Modische Accessoires AG	speciality retail (costume jewellery stores)	3.1%
Dewhurst PLC. -A- Non Voting	industrial goods (lift panels & controls)	3.0%
Daekyo, preferred	consumer services (education)	3.0%
Village Super Market Inc	retail (supermarkets)	2.9%
Zwack Unicum	consumer goods (spirits)	2.9%
Pronexus Inc.	business services (printed & electronic filings/reports)	2.8%
Springer (Axel) Verlag AG	media (newspapers, magazines, internet)	2.6%
Zehnder Holding AG	industrial goods (radiators)	2.5%
Nongshim Co.	consumer goods (food & beverages)	2.5%
Heineken Holding NV	consumer goods (brewing)	2.3%
Nongshim Holdings Co.	holding co. (Nongshim, packaging, ingredients)	2.1%
Thorpe, (FW) PLC	industrial goods (lighting)	2.0%
Clinton Cards PLC	speciality retail (card shops)	2.0%
Hanil Cement	materials (cement production)	2.0%
Family Mart Co. Ltd.	retail (convenience stores)	1.9%
Bull SA	information technology (computers, services)	1.8%
Kuoni Reisen Holding -B-	consumer services (travel agents)	1.8%
Tamedia AG Reg.	media (newspapers, magazines)	1.7%
Telecinco, Gestevisión SA + Rights	media (TV)	1.4%
Coltene Holding AG	healthcare (dental products)	1.3%
Circle K Sunkus	retail (convenience stores)	1.2%
Wolters Kluwer NV	media (professional publishing)	1.1%
Royal Reesink NV (CVA)	wholesale and trade	1.0%
Molins PLC	industrial goods (tobacco machinery & packaging)	1.0%
Johnston Press PLC	media (regional newspapers, internet)	0.3%
Telegraaf Media Groep NV	media (newspapers, magazines, radio, TV, internet)	0.2%
Cash and other assets and liabilities		12.5%
		100.0%

In addition to these two new companies we added to existing holdings in four other companies: German costume jewellery retailer **Bijou Brigitte**, French traffic sign producer **Signaux Girod**, industrial conglomerate **Toyota Industries**, and financial information provider **Pronexus**; the latter two headquartered in Japan.

Finally, the attentive reader may have noticed that the **Telecinco** position includes 'rights'. These are rights the Fund received ahead of a share issue the company is undertaking to finance its acquisition of competitor *Cuatro* and a 22% interest in digital TV network *Digital+* for which the company just received approval. In the meantime these

rights have been exercised allowing the Fund to boost its stake in Telecinco at attractive prices. The transaction was completed in the first half of December.

Japan – the promised land for value investors?

Having invested in Japan for several years now we thought shareholders might find it interesting to read about Citadel's experience and our perspective on the Fund's investments in that country. Currently the Fund owns four Japanese companies which comprise in total somewhat less than 10% of the net assets. While stock prices of the Japanese holdings suffered during the financial crisis the overall result has been reasonably good. This was helped by the take-over of one holding and recently by the strength of the yen versus the Euro. The Fund's four holdings are amongst the most undervalued in Citadel's collection of very undervalued companies. And, based on our day-to-day work analysing and valuing companies, we suspect that the weighting in Japanese companies will increase further.

The reason for this is that if there is one major stock market in the world where cheap valuations literally jump out at you it is Japan. Perhaps this is unsurprising when, after a twenty year period, the key Nikkei index trades at almost a quarter of its 1989 peak. There are pages and pages of companies trading below book value. Our own experience corroborates the value to be had. When screening for new ideas based on some multiple of market value to earnings, cash flow or assets we are usually thrilled to come up with 2 or 3 companies which appear attractive and worthy of further research. In Japan such an approach usually swamps you. Even finding companies where the net cash per share is worth as much or more than the stock price is not very challenging – there are tens of such examples today.

Many a reader will ask how this is possible. And indeed this is a question we've often asked ourselves. Situations like these almost never arise in North America or Europe, and if they do they are usually snapped up within a fairly short time span. It's difficult to know for sure why Japan has such a preponderance of these cases but a couple of factors undoubtedly play a role. The first is inertia. During their careers Japanese investors and analysts have had little experience with anything else - or at least that's true for the bulk of the young men populating the Japanese investment community. The equity culture of Japan likewise seems to be much weaker than in Western markets where seasoned, sharp investors are trawling the market daily for 'inefficiencies'. The well known barriers to M&A are a related and significant issue. Finally, another factor of which we've gradually become aware is how Japanese analysts approach company valuation, and in particular the valuation of cash. Take the example of a company holding 1 million yen in net cash. If we were to ask anybody what 1m yen in cash was worth, most, after puzzling over whether it was a trick question or not, would eventually answer 1m. An obvious answer? Not so for the intelligent, highly educated professionals in the hallowed halls of Japan's leading investment institutions. More often than not the answer would be a variant of the following. On 1m cash a Japanese company would earn interest income after-tax of 6,000 yen assuming an interest rate of 1% (probably less in reality) and a tax rate of 40%. This 6,000 yen is then valued by applying an arbitrary earnings multiple to it, often the average Price/Earnings (P/E) multiple for the market or a derivative thereof. Taking a multiple of 10X would mean our interest earnings would be worth 60,000 yen. To us it defies common sense to say that 1 million in cash is worth only 6% of its nominal value or 60,000 yen. Yet we've seen research report after research report with exactly that sort of conclusion. Little wonder then that valuations are sometimes shockingly low.

This brings us to a very important related topic. If this is the reality of Japan, and nothing changes, undervalued companies may very well remain undervalued. Fortunately there are some glimmers of hope. Foreign investors like ourselves are increasingly attracted to Japan for the bargains that exist. Furthermore the number of foreign and even domestic investors agitating for change seems to be inextricably on the rise. Companies themselves, led by a new generation of management, seem more aware of their own valuation and also care enough to do something about it. The take-over of a Fund holding by management in 2009 is a case in point. Unsurprisingly situations of extreme undervaluation can lead to financial engineering (sometimes of a very dubious sort) by company managements and others. Return to our example of the company with 1 million in net cash. Management at this firm wishing to improve the share price and generate growth might for instance decide to undertake an acquisition. Let's assume that management is not at all value conscious and decides to acquire a company at a very high P/E ratio of 30 times. On a 1m yen investment this would imply the company acquired net earnings of 33,333 yen. If analysts were to value those earnings at the same 10X P/E we described above it would translate into a market value of 333,333 yen.

Voilà, in one transaction management would have transformed cash valued by the market at 60,000 into earnings valued at almost 6 times as much, and all things being equal the share price would rise. Naturally the logic of permanently transforming cash worth 1 million into an asset worth only a third as much is completely skewed. Shareholders would enjoy a positive return however. Smarter managements are turning this state of affairs to their advantage. Share buy-backs at very low prices are occurring with increasing frequency and dividends are rising. The mathematics of such operations is very favourable for shareholders and will hopefully increasingly serve as an example for others in consensus-driven Japan.¹

The preceding likely goes a way to explaining why corporate acquisitions in Japan are often done at ridiculous prices. Misdirected capital allocation on low yielding investments or acquisitions is one of the major risks we face as investors and it is probably a greater risk in Asia in general, and in Japan specifically, than in other regions of the world.

All these issues bear on how we select stocks in Japan. We take it for granted that even more patience will be required in Japan compared to other markets where Citadel owns stocks. We are always looking for a large margin of safety between the market price of a company and what we think it is worth. In Japan our standards are higher. Consequently the balance sheets of our Japanese holdings are even stronger than other companies in the portfolio, with the possible exception of a few firms in South Korea. While a huge cash position provides an excellent starting position for an investment it is, by itself, not enough to base a case on. This is particularly true when you assume that you may need to hold a position for a considerable time before it re-values; time in which poor capital allocation or operating losses may shrivel the cash position and the margin of safety with it. Therefore we want to see a strong, and preferably growing, earnings stream. If a company is able to generate strong earnings and cash flow its cash position is more likely to be secure, and even grow. And earnings provide an additional impetus to why the stock price should rise, even in the absence of markets suddenly re-rating a company's business and balance sheet.

Returns on Capital Employed (ROCE) are an invaluable tool in assessing the strength of a business. High after-tax returns on the capital invested in a company are one of the best indicators of a good company, or at a minimum a decent one operating in an attractive industry. In Japan the importance of high ROCE's is accentuated by the fact that returns on capital were often seen as of only minor importance compared to growth. This primacy of growth versus returns has led to many a large but mediocre company. Filtering out low return on capital companies means we can cast aside firms where earnings and earnings growth are often solely the result of ploughing huge amounts of money back into the business and earning little on it. A high-return business in Japan is definitely more unique than elsewhere in the world. High returns also provide additional assurance that a company is well run and most probably a reasonable capital allocator.

Finally, we like to see signs that companies don't just exist to exist, (a shockingly common phenomena), but that shareholders reap the rewards. High dividends and stock buy-backs are welcome indicators of this.

While Japan has its peculiarities as well as its practical obstacles such as language, the size of the market and the sheer number of bargains available make it an obligatory stop for value investors. We are excited by the companies Citadel holds and have high expectations for them. One of these is **Pronexus** which we describe in more detail below.

¹ To illustrate assume our company with 1m net cash is valued at 1m based on 10X earnings (net earnings of 100,000 yen). It decides to use half its cash to buy back stock. If the stock didn't rise the company would now be valued at 0.5m and enjoy almost the same earnings it did previously (97,000 to be precise: 100,000 less the 3,000 yen previously earned on the 500,000 used to buy back stock). The company would then be valued at a P/E of 5.2X. However, the stock would almost *double* were it to maintain, which it most likely would, the same 10X earnings multiple.

Pronexus

Pronexus is hard to sum up in a catchy phrase although its products and services are used by more than half of all Japanese listed companies. It publishes and prints a wide variety of financially oriented documents for companies and investment funds including annual reports, AGM notices and invitations, prospectuses, marketing documents and the like. It also has digital products like software and services enabling companies to meet regulatory requirements by electronically filing earnings reports, IPO & securities documentation, and other disclosures. Finally it provides a series of related products such as financial seminars, investor relations products, financial guidebooks, legal services and others. In its key products the company has market shares of 50% or more.

The company held JPY 13,830m in net cash and investments based on its most recent balance sheet. Coincidentally this is, for all intents and purposes, the market capitalisation of the company at current prices. When the price of each share is equal to the cash per share it provides an extremely solid back-stop to the business and a huge margin of safety for the stock. We've seen it in Japan before yet we still marvel at how healthy firms can be valued at nothing.

Pronexus's results have suffered in the past three years as IPO activity dried up which had the corollary effect of shrinking the number of listed companies as those acquired or de-listed were not replenished by new ones. Furthermore the economic climate and the cyclical downturn have led to heated up competition and lower prices, despite what is essentially an oligopoly. One of the highly attractive features of the company's business model is that almost 70% of its sales are steady, recurring and driven by financial regulation. While more cyclical products fell sharper the overall sales decline was rather modest as result. Profits, however, declined at a faster pace as costs are largely fixed and marginal profitability is consequently extremely high. Each yen of sales lost led therefore to a disproportionately large impact on profits. Of course this is an aspect which works both ways. When sales recover profitability will surge. We are also encouraged by management's efforts to reduce fixed costs which will leave the company in a very healthy state in what is probably the nadir of its earning cycle. For all its recent difficulties the company is still solidly profitable and cash generative. Operating profits this year - by far the lowest in the past 5 years - are likely to come in at around JPY 1,600m on margins just under 10%. A stock market value of zero seems downright preposterous in this context.

We estimate the firm's after-tax ROCE will be around 11% this year which is very respectable. However, in the past 10 years returns averaged a whopping 25%+. This sort of return is rare anywhere, let alone in Japan, and highlights the attractiveness of Pronexus as a business.

Fortunately management appears aligned with the interests of shareholders – perhaps not surprising as they themselves are major shareholders. Although earnings plunged the dividend was maintained, leading to a huge payout ratio and a yield which now hovers around 5.6%. In 2007 and 2008 the company bought back substantial amount of its stock and we are cautiously optimistic that management will again propose a buyback. With the valuation of the stock where it is this would be a fantastically value enhancing action.

In conclusion

Up until now 2010 has been a favourable year for the Fund. More significantly perhaps we have good reasons to be positive heading into 2011. Overall the portfolio trades at a little more than 5X 2009 EBIT – EBIT which at least in some cases is depressed as a result of the economic downturn and which should improve in future. Versus capital employed the Fund's see-through valuation is close to 1X, while the average after-tax return on capital of the portfolio companies has never been higher at roughly 14%.² The vast majority of the 35 companies you own through your shareholding in Citadel hold net cash and are paying decent or downright high dividends. A couple of holdings have already been re-rated by the market and are approaching our value estimates. Nevertheless there are

² As a quick reminder Capital Employed refers to all the investments in fixed assets, inventories, receivables, and cumulative goodwill in a business after taking account of depreciation. For a more extensive explanation please refer to the latest May 2010 letter and also that of November 2007.

quite a number of startlingly cheap stocks in the portfolio, such as Pronexus, whose valuations literally beg disbelief. These have the potential to propel returns in the years to come.

Thank you for your investment in the Fund and your trust. We wish you and your families the Merriest of Christmas's and a Happy, Healthy and Profitable 2011!!

Kind regards,

The Board of Directors
Citadel Value Fund SICAV

December 15th, 2010