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November 14th, 2019

Dear investor,

The main reason for writing a letter to our investors is to illustrate how we work to deliver returns. As you know, and as we have said many times before, in an ideal world, this letter ought to be written every five years as this is our minimum investment horizon. However, we believe that our investors should have all the necessary information to judge our work. It is in this spirit that we address these quarterly missives.

Our funds' performance at the end of the third quarter of 2019 is reflected in the tables below.

The individual return of each investor depends on the net asset value at which they subscribed.

	Jan-Sep
Azvalor Internacional FI	**4.3%**
MSCI Daily Net TR Europe Euro**	19.2%
Return vs Index	-14.9%

***Includes dividends*

	Jan-Sep
Azvalor Iberia FI	**-2.3%**
85% IGBMT** / 15% PSI 20 TR	10.4%
Return vs Index	-12.6%

***Includes dividends*

From a longer-term perspective, the table below shows our funds' performance compared with their benchmarks, since their launch at the end of 2015:

	ITD*
Azvalor Internacional FI	**11.4%**
MSCI Daily Net TR Europe Euro**	19.2%
Return vs Index	-7.8%

*** Includes dividends*

	ITD*
Azvalor Iberia FI	**10.6%**
85% IGBMT** / 15% PSI 20 TR	7.9%
Return vs Index	2.7%

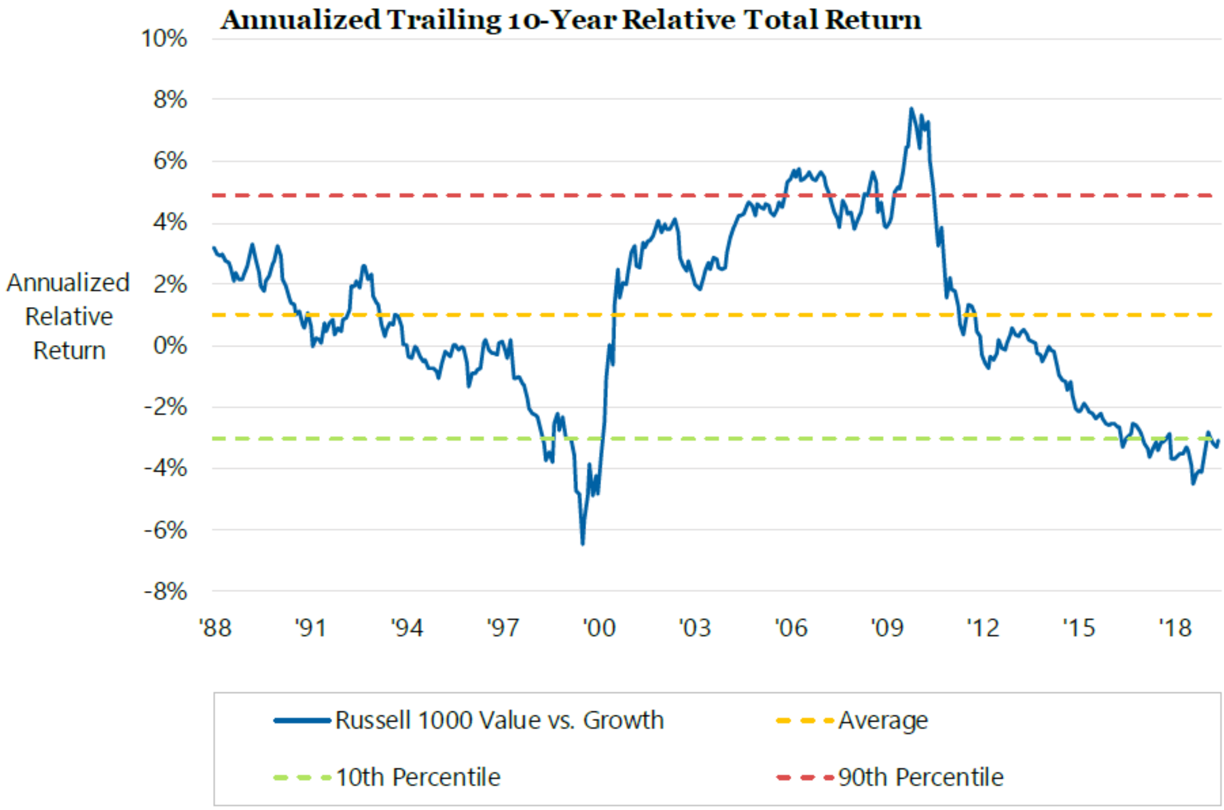
*** Includes dividends*

It has been 4 years since we launched our main funds and the results obtained have still not met our expectations. Despite the positive returns, we have not managed to beat the market. Moreover, the international and the Iberian portfolio are 12% and 18%, respectively, below their mid-2018 highs.

However, we are absolutely convinced that they represent a historic opportunity, with a strong upside potential, and that we will eventually outperform the market (which, unlike our portfolios, we think is expensive).

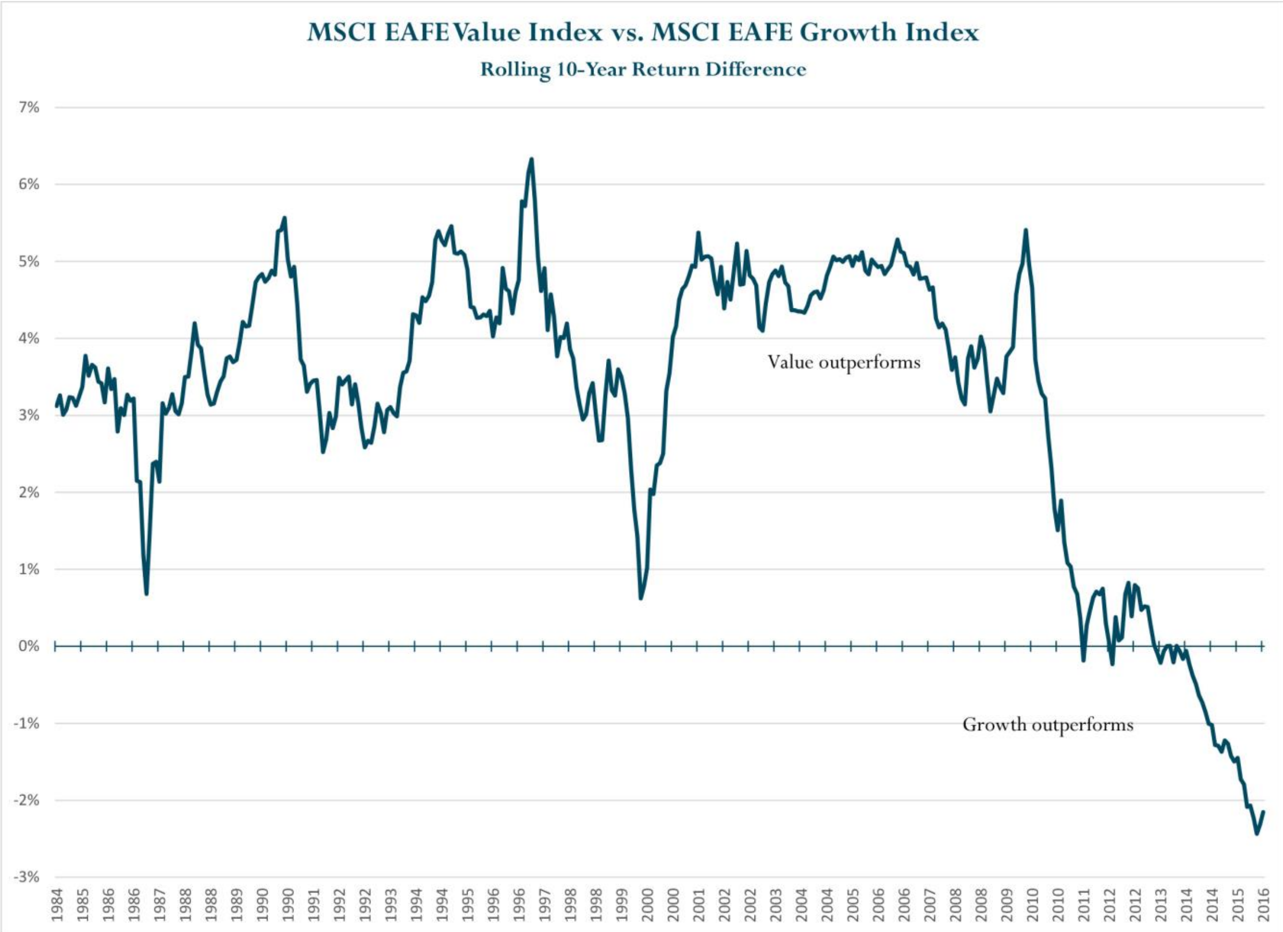
We are well aware that we have been giving the same message for some time, particularly in 2019 when we are not coming out well in the "photo finish" vs. the indices. Value investing achieves extraordinary returns but requires something fundamental in exchange - to maintain conviction when the market seems to contradict us. Periods of underperformance are very frequent, yet the period we are going through (which affects the majority of internationally renowned value investors) has been particularly trying.

To give you a historial reference, the chart below shows two US sub-indices. One would be a more or less "clumsy" (unrefined) representation of the value universe, and the other its supposed "nemesis" - the universe of growth companies which tend to be much more expensive. Indeed, we see how the value index has been underperforming growth companies for almost 9 years. Therefore, the period we are currently going through is already the longest since the one which started in 1992 and peaked in 2000 when the dotcom bubble finally burst. Note, that in the following 10 years the value index yielded an annualized return 8% higher that the growth companies index, which informed a cumulative return 2.1 times higher at the end of the period, in 2010.



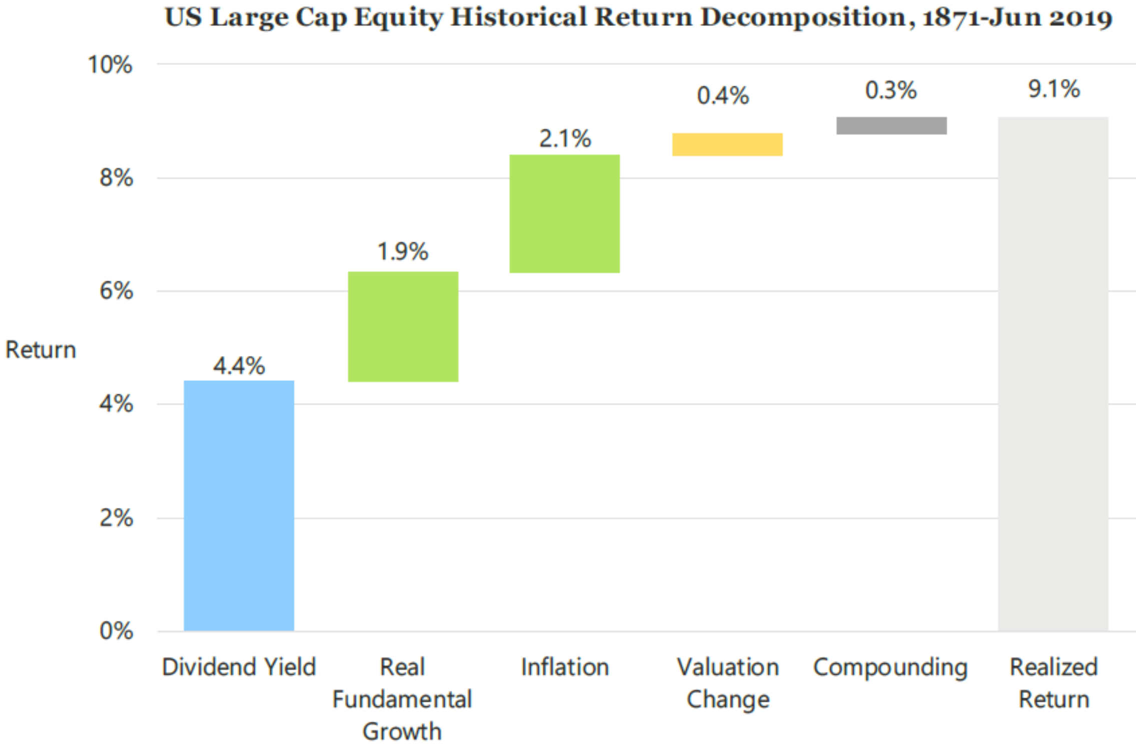
Source: Research Affiliates, LLC, using data from FactSet. Data as of 6/30/2019.

If we choose indices outside the US (the chart below shows a comparison of the sub-indices of MSCI EAFE, which includes developed countries in Europe and Asia), the current period is unprecedented in the last 36 years (note that the data only goes up to 2016, so if we were to update the chart to 2019, the result would be even more remarkable). In other words, since 2011, this is the first time that in 10-year periods, value performs worse than growth, and continues to crash to new records. This occurs, precisely coincident with the launching of a new round of quantitative easing by the main central banks.



As we have expained on other occasions, this has, in turn, led to the largest discrepancy in valuation between the most expensive and the cheapest companies in the last 20 years. And we pointed to what we think may be the reasons: the explosive growth in passive investment, the growing phenomenon of ESG (or corporate social responsibility) and the lack of returns from fixed income investments, which has prompted the search of “substitutes” in the stock market. All these factors have led to the stratification of the market into “castes”, with an elite group of companies trading at vertiginous valuations and “invisible” companies in scorned sectors trading atlow valuations that we have rarely seen before.

This divorce between the fundamentals of the companies and their stock market valuation is NOT sustainable in the long term. The following chart reflects this idea well. The bars disaggregate the different factors that explain the historical return of the US market (large companies) since 1870.



Source: Research Affiliates, LLC, based on data from the Robert Shiller database. Data as of June 30, 2019.

As we can see, the (nominal) return is explained almost entirely by the dividend, real earnings growth and inflation. The earnings multiple has hardly changed. In other words, the value of "past", "present" and "future" companies is a nearly constant earnings ratio in the long term (although with very large variations in the short term).

Be wary then of what may seem like a solid upward trend in a company's share price when it rises faster than its earnings (or worse, with earnings falling). This has happened, in our view, with a large number of companies with characteristics that seem to assimilate their performance to that of a bond: they tend to be apparently solid and not very volatile businesses that have achieved sustained growth rates in recent years and, many of them, pay "bulletproof" dividends in the eyes of some investors. Think of the numerous examples of companies whose share prices have doubled, tripled or quadrupled in the last 3-5 years, their valuation "sprinting" much faster than their earnings.

The sense of security generated by these type of companies is a dangerous "mirage" when they trade at exaggerated valuations, and the descent from such high altitudes may be a forced landing. When the market wakes up to reality and realizes that companies do not run as smoothly as Swiss watches and are not immune to surprises or problems, their valuations often suffer a violent shock. The following table lists a number of companies which, for some reason (such as issuing a profit warning) have suffered very strong stock market corrections in a single day! (In fact, it usually occurs in an instant, for example at the very opening if the announcement is made outside market hours). This group of companies had the common feature of being businesses trading at "sky-high" valuations.

Company	Daily variation (%)
DBV Technologies	-70%
At Home Group	-57%
Diplomat Pharmacy	-56%
Farfetch Limited	-44%
GrubHub	-43%
Myriad Genetics	-43%
Pivotal Software	-41%
Cloudera Inc	-41%
Covetrus Inc	-40%
Pluralsight Inc	-40%
Mallinckrodt	-39%
Casa Systems	-36%
WW International	-34%
Cision Ltd	-32%
Tivity Health	-32%
Ulta Beauty	-30%
Perrigo Co	-29%
Nektar Therapeutics	-29%
Expedia Inc	-27%
Beyond Meat	-25%
Temenos	-23%
Wirecard	-13%

Source: Bloomberg

The higher the valuation, the greater the risk. And yet, in recent years, we have not ceased to perceive the opposite identity: the higher the valuation, (it implicitly follows that the higher the quality of the company/business, and therefore) the lower the risk. The "lesson in reality" need not necessarily be a "shock"; it may also be a slow and steady re-evaluation of the value a company deserves. For example, firms such as Kraft Heinz, L'Brands, Tapestry, Arista Networks, Under Armour, Twitter, Walgreens Boots, Capri Holdings, Altria, Hasbro, Netflix, Conagra, 3M, Molson Coors, Public Storage, Ball, Glanbia, Bunzl, Interpump, Evotec, Colruyt, Ubisoft, CHR Hansen, Anheuser Busch, Schibsted, Demant, Thales or Lagardere are all between 20% and 50% below their recent highs. The list is not exhaustive and includes only a small selection of companies in the S&P500 and Stoxx 600 that traded (and many still trade) at high multiples.

This also happens in the opposite direction with those companies that nobody seems to want and whose stocks are very cheap. Note, for instance, that on the same day that GrubHub or Beyond Meat suffered the sharp falls shown on the table above, National Oilwell Varco, one of our investments, was up 14%

directly at the opening, after the results were published. We believe we will witness many more such examples in the future.

Many investors and savers have placed a great deal of their trust in the group of companies known as FANGMAN (Facebook, Amazon, Netflix, Google, Microsoft, Appel and Nvidia). We are not going to analyze them or advise you against investing in them, but we do want to warn you that these are companies in which many will have invested inadvertently (passive management) and which have been lifted by a virtuous circle that has been powerfully reinforcing itself through a feedback loop for a long time, a phenomenon that may have led to dangerous levels of valuation. Keep in mind that class probability clearly plays against them. Those companies that reach the top of the world market capitalization ranking tend to perform much worse than the market over the next 5-10 years (the top 10, about -4% annually from 1982 to 2017). Notice in the table below how much what the market considers to be the most valuable companies in the world changes from decade to decade.

Ten Largest Market Capitalization Stocks in the World, at the Beginning of Each Year

2019	2010	2000*	1990	1980
Microsoft	**PetroChina**	Microsoft	**Nippon Tel and Tel**	IBM
Apple Inc.	Exxon Mobil	General Electric	**Bank of Tokyo-Mitsubishi**	AT&T
Amazon	Microsoft	**NTT DoCoMo**	**Industrial Bank of Japan**	Exxon Mobil
Alphabet Inc.	**ICBC**	Cisco Systems	**Sumitomo Mitsui Banking**	Standard Oil
Berkshire Hathaway	Wal-Mart	Wal-Mart	**Toyota Motors**	Schlumberger
Facebook	**China Construction Bank**	Intel Corporation	**Fuji Bank**	Shell
Tencent	**BHP Billiton**	**Nippon Tel and Tel**	**Dai-Ichi Kangyo Bank**	Mobil
Alibaba Group	**HSBC**	Exxon Mobil	IBM	Atlantic Richfield
Johnson & Johnson	**Petrobras**	Lucent Technologies	**UFJ Bank**	General Electric
JPMorgan Chase	Apple Inc.	**Deutsche Telekom**	Exxon Mobil	Eastman Kodak

Legend:	New Addition to List	Drops off List Next Period	Flip-Flop: New Then Drops
Black = US Company	**Teal = Emerging Markets**	**Blue = European Company**	**Green = Japan/Australia**

Source: Research Affiliates, LLC, using data from *Financial Times*, Wikipedia, and Gavekal Research. Rankings shown represent beginning-of-year rankings.
*Year 2000 represents holdings as of March, three months late.

We do not mean by this that some of the "FANGMAN" cannot be exceptional businesses and companies that can grow and generate great value for a long time. But, again, the probability of finding a "franchise" company (which can reinvest for the very long term at rates of return well above its cost of capital thanks to a lasting competitive advantage) is extremely low. Remember, for example, the group of 50 US stocks in the 1970s which were called the 'Nifty Fifty' because they were considered "franchise" businesses and reached towering valuations. Well, the overall performance of this group was ruinous in the following decade, incluing 14 or so which proved to be exceptional businesses. Moreover, among the rest, almost a dozen ended up disappearing or going bankrupt, including household names such as Digital Equipment, Eastman Kodak, Emery Air Freight, MGIC Investments, Polaroid, Hebleuin or Kmart.

Our portfolios

After 10 consecutive years of bullish stock markets and record valuations (see previous letter), it is all the more relevant and special that our portfolios trade at such cheap valuations. Again, we have mentioned this on a number of occasions. But the disconnection between the valuation and the fundamentals of the companies in our portfolio is even greater than just a few quarters ago, as they are barely reflecting the gradual but clear improvement in their businesses (with the exception of the gold mining and shipping sectors which have had a positive stock market performance). In some cases, we have even witnessed falls in stock prices with improvements in the fundamentals. Let us look at just a few examples of these improving fundamentals in our portfolio companies.

- Uranium: The interest and the number of negotiations for forward contracts has recovered to levels unseen since 2011, when the Fukushima disaster occurred and, for the first time, Cameco is in talks with Chinese utility companies (which traditionally only bought on the spot market or were supplied by Chinese-owned mines). Moreover, the recovery in the prices of services and intermediate products in the uranium fuel value chain continues, which usually indicates a subsequent recovery in the price of the metal.

- Oil and Gas: We are witnessing a clear slowdown in US shale oil investments which the market seems to ignore. For the last several years, shale has unleashed a revolution, having met 100% of global demand growth needs and, what is more, compensating for the sharp declines in countries such as Iran, Venezuela or Mexico. Hundreds of billions of investments in the US have caused the opposite effect in the rest of the producing regions, with a drastic reduction in investments which has been going for 5 years now.

- Oil rigs: They are achieving the first increases in prices, in the duration of contracts and in the overall fleet utilization. The number of customer requirements has also grown to levels not seen for several years. However, the sector accumulates an average fall of 50% in 2019.

- Coal: International prices have already bounced back 22% since the recent second quarter lows, and world supply is reacting to low price conditions, even with production cuts and losses in some of the lowest cost areas, such as Colombia and Indonesia. In the US, the supply adjustment process continues, and we are witnessing cuts in production and investments, as well as some bankruptcies. Gas production in the US, coal's main competitor, continues to grow strongly, but depressed gas prices are causing serious financial difficulties for companies and leading to significant cuts in investments. Meanwhile, such cheap gas is a great stimulus for exports and all kinds of industrial uses, which is creating new markets that are likely to demand more gas for many years. Yet in spite of the above, Consol's shares have hit historic lows.

- Shipping: After several years of freight rates at all-time lows, the tanker sector is experiencing a real explosion, reaching, on some days, price levels never seen before. Although the price of many of our investmens has risen sharply, we believe there is room for further upside. Moreover, the other shipping companies in our portfolio (liquefied gas, chemicals and bulk) have barely recovered yet and, therefore, their potential remains virtually intact.

We are familiar with the pessimistic theses of our companies. The biggest concern right now is a recession and/or a trade "war" that could damage demand. We are not going to defend that we would be totally immune to such a scenario, at least temporarily. However, in our view, it seems much more likely that much (or even all) of what these scenarios could bring is already discounted, given the enormous pessimism that emerges from the valuations at which they are traded. In any case, the key of what will happen in their markets over the long term is the analysis of what has happened to supply. And the conclusion we draw from this analysis is that this is a clear investment opportunity. The fact that the market is ignoring the improvements in the fundamentals of our portfolio companies only serves to reinforce our conviction. Only a severe and prolonged recession (or depression) could justify their share prices, a scenario that strikes us as very remote and which, we think, would be much more negative for most investment alternatives.

Azvalor News

Socially Responsible Investing/Corporate Social Responsibility or ESG (Environmental, Social and Governance)

At Azvalor we are fully aware of the social and solidarity dimension of the company and we are firmly committed to ESG, as evidenced by our initiatives Davalor (solidarity with the most disadvantaged), the Stella project (support for people with Down syndrome), and the agreement with Auara (solidarity with developing countries and environmental sustainability). I particularly encourage you to visit our website once again to learn more about Davalor, an initiative you may contribute to, if you wish, and which is developing wonderful projects with which we are very proud.

We are also fully committed to good corporate governance. Consequently, we have endeavoured to turn the principles of alignment of interests, correct incentives and having 'skin in the game' (or full commitment) into core values in which Azvalor's culture is rooted - both in the selection of investments and in the management of the company. The fact that two thirds of our portfolios are invested in companies whose owners "risk their necks" with us, as well as the fact that Azvalor's employees, as a group, are by far the largest investor by size in our funds, provide an unequivocal proof.

Trying to honor this and renewing our commitment to disseminate financial literacy, we have had the small initiative of launching a custom edition of the book "Skin in the Game", by Nassim Nicholas Taleb. One of the most brilliant thinkers of recent times, Taleb culminates in this new release a whole body of knowledge developed in a series of five books which the author titles "*Incerto*". Simplifying it greatly, his work has allowed us to better understand the risk and the correct calculation of probabilities, the nonlinearity of most social phenomena and the importance of second-order effects, it has given us ideas to make our portfolios more "antifragile" and to benefit from volatility, and it has instructed us and reinforced our conviction of the vital importance of incentives and the asymmetries they produce. I strongly recommend you to read it.

Azvalor Managers

We are deeply saddened by the recent passing of Donald Smith. Donald was a legendary investor, among the best in history, who applied his investment philosophy consistently and successfully for nearly 50 years. Richard Greenberg, Co-Chief Investment Officer and 38 years at Donald Smith & Co, takes over as Head of the firm and, along with the rest of the team, we are convinced that he will ensure continuity in the quality of management.

With its first anniversary just around the corner, the fund continues to grow steadily, with 321 co-investors and over 20 million euros in assets.

Once again, I would like to thank you for the trust you have placed in Azvalor.

In return, we guarantee you the utmost dedication to our work and, most importantly, the utmost commitment to what we do, a commitment that we renew and periodically increase with new contributions to the funds.

Kind regards,

Fernando Bernad