

MARGIN OF SAFETY FUND

SICAV

Annual Report (Audited)
at December 31, 2004



SECURITIES SERVICES



MARGIN OF SAFETY FUND

Audited annual report

at 31/12/04

MARGIN OF SAFETY FUND

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Subscriptions can only be received on the basis of the latest prospectus accompanied by the latest annual report as well as by the latest semi-annual report, if published after the latest annual report.

MARGIN OF SAFETY FUND

Management and Administration

REGISTERED OFFICE

39, Allée Scheffer
L-2520 Luxembourg

PROMOTOR

Crédit Agricole Investor Services Bank Luxembourg S.A.
39, Allée Scheffer
L-2520 Luxembourg

CUSTODIAN AND

CENTRAL ADMINISTRATION AGENT

Crédit Agricole Investor Services Bank Luxembourg S.A.
39, Allée Scheffer
L-2520 Luxembourg

INVESTMENT MANAGER

Pastel & Associés S.A.
27, rue de Marignan
F-75008 Paris

CO-PROMOTOR

Pastel & Associés S.A.
27, rue de Marignan
F-75008 Paris

AUDITOR

KPMG Audit S.à r.l.
31, Allée Scheffer
L-2520 Luxembourg

Board of Directors

Chairman of the Board

M. Jean-Marie RINIE, Senior Sales Manager - Financial Services, Vice-President
Crédit Agricole Investor Services Bank Luxembourg S.A

Members of the Board

M. José-Benjamin LONGREE, Head of Sales CRM & Head of Fund Structuring - Europe,
First Vice-President, Crédit Agricole Investor Services Bank Luxembourg S.A. (until 18/10/04)

M. Hervé SHUNKE , Sales Manager, Crédit Agricole Investor Services Bank Luxembourg S.A. (from 18/10/04)

M. John MILLS, Managing Director, Maitland J. Co. Sàrl

M. David PASTEL, CEO of Pastel & Associés S.A.

MARGIN OF SAFETY FUND

Manager's Report

Investment performance Margin of Safety Fund – Fund 1

(Cumulative figures after all fees and expenses)

Class B shares

In 2004, the Fund's NAV per B share increased by 21.2%, resulting in a cumulative performance since inception on February 2nd, 1998, of 173.3%. Its out-performance against its peers, as measured by the cumulative return differential with the MSCI World index since inception, has reached, at year-end 2004, 136.1%.

Class A shares

The Fund had only one class of investors shares until August 16, 2002, on which date the first Class A shares were issued. From August 16th, 2002, to December 31st, 2004 the performance of the Class A shares was 61.8% in USD and 16.7% in €. The performance of the Class A shares for the year ended December 31, 2004 was 20.2% in USD and 11.5% in €.

Review of operations

2004 was also a significant year with regard to changes brought to the portfolio structure:

New stakes were built in companies such as L'Oréal (France), WM Morrison (UK), Charles Schwab (US), Coca-Cola (US) and Colgate-Palmolive (US). At the same time, we increased the size of existing positions in Carpetright (UK), Electrocomponents (UK), and Ryanair (Ireland) and in the US, Ethan Allen, Target and TJX.

A number of positions were entirely disposed of, of which for the UK, Abbey, Dixons, HBOS and Lloyds TSB and for the US, Home Depot, Leucadia National and Manpower. Several positions were downsized, such as Randstad (Netherlands), and Premier Farnell (UK).

In early 2004, a significant position in Kmart Holding was set up and then disposed of at mid-year following a sharp appreciation in its stock price. However rewarding these transactions have turned out to be for the Fund's investors, one should not expect such "round trip" trades to repeat in the future as the Fund is truly managed on a long term basis and as a result most positions tend to remain in the portfolio for a number of years.

As was already mentioned in previous reports, Euro and Sterling-denominated portfolio assets are partially hedged back into the US Dollar through forward currency sales.

Portfolio structure

The portfolio structure by asset class was on December 31st, 2004, as follows (2003 figures were provided herein for comparison purposes):

	2004	2003
- Euro Zone:	32%	36%
- United Kingdom:	30%	34%
- United States:	33%	24%
- Fixed income:	5%	6%

MARGIN OF SAFETY FUND

Manager's Report

The breakdown by sector of the equity portion of the Fund's portfolio was on December 31st, 2004, as follows (2003 figures were provided herein for comparison purposes):

	2004	2003
- Business to business services:	23%	39%
- Non food retailing:	20%	19%
- Food retailing:	13%	5%
- Consumer goods manufacturing:	12%	—
- Financial services:	11%	14%
- Transportation:	9%	3%
- Light manufacturing:	7%	11%
- Lodging – Restaurants:	5%	5%
- Conglomerates:	—	4%

Outlook

Although we have no opinion about the rate of return the Fund will achieve in 2005, we trust that, barring any adverse development, its performance, over the next five years, will be quite satisfactory.

This outcome should primarily result from the implementation of our investment methodology whose core principles we shall now reiterate:

- We focus on a few, carefully screened and researched companies that tend to share some common features such as a good and historically profitable business and a competent and honest management.
- We demand that a significant margin of safety be present, at the time of purchase, in every one of our investments.
- We do not shift course and dispose of or increase some of our holdings because of changes in macro-economic or financial market expectations. In fact, we do not harbor any kind of expectations as to where the economy or the markets are supposed to go.

For additional information regarding the Fund's portfolio's structure at year-end and its evolution during the last quarter of 2004, please refer to the quarterly report attached to this letter.

Please let me thank you for your support and continuing trust.

David Pastel
Pastel & Associés S.A.

MARGIN OF SAFETY FUND

Independent Auditor's Report

To the Shareholders of
MARGIN OF SAFETY FUND
39, Allée Scheffer
L – 2520 LUXEMBOURG

We have audited the financial statements, which consist of the statement of net assets, the securities portfolio, the statement of operations and changes in net assets and the notes to the financial statements of MARGIN OF SAFETY FUND (the "SICAV") at December 31, 2004. These financial statements are the responsibility of the Board of Directors of the SICAV. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors of the SICAV in preparing the financial statements, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the attached financial statements give, in conformity with Luxembourg legal and regulatory requirements, a true and fair view of the financial position of MARGIN OF SAFETY FUND at December 31, 2004 and the results of its operations and changes in its net assets for the year then ended.

Supplementary information included in the annual report has been reviewed in the context of our mandate but has not been subject to specific audit procedures carried out in accordance with the standards described above. Consequently, we express no opinion on such information. We have no observation to make concerning such information in the context of the financial statements taken as a whole.

Luxembourg, April 14, 2005

KPMG Audit S.à r.l.
Réviseurs d'Entreprises

Nathalie Dogniez
Partner

Patrice Perichon
Director

MARGIN OF SAFETY FUND - Fund 1

Financial Statements at 31/12/04

Statement of net assets at 31/12/04

Expressed in USD

Assets			45,437,714.33
Securities portfolio at market value	Note 2	42,280,923.27	
<i>Cost price</i>		34,747,102.41	
<i>Unrealised profit on the securities portfolio</i>		7,533,820.86	
Cash at banks and liquidities		1,718.37	
Time deposits		3,075,000.00	
Interest receivable		341.67	
Other assets		79,731.02	
Liabilities			1,436,966.84
Unrealised loss on forward foreign exchange contracts	Note 6	1,125,302.68	
Accrued management fees		104,756.27	
Other liabilities		206,907.89	
Net asset value			44,000,747.49

Changes in number of shares outstanding from 01/01/04 to 31/12/04

	Shares outstanding at 01/01/04	Shares issued	Shares redeemed	Shares outstanding at 31/12/04
Class A				
Capitalisation shares	224.80	0.00	204.80	20.00
Class B				
Capitalisation shares	11,858.95	11,763.39	7,541.67	16,080.67

Key figures relating to the last 3 years

	<i>Year ending at:</i>	31/12/04	31/12/03	31/12/02
Total Net Assets	USD	44,000,747.49	27,214,205.93	17,495,797.86
Class A		USD	USD	USD
Capitalisation shares				
Number of shares		20.00	224.80	107.94
Net asset value per share		2,558.40	2,128.38	1,548.45
Class B		USD	USD	USD
Capitalisation shares				
Number of shares		16,080.67	11,858.95	11,115.71
Net asset value per share		2,733.07	2,254.48	1,558.93

MARGIN OF SAFETY FUND - Fund 1

Securities portfolio at 31/12/04

Expressed in USD

Quantity	Denomination	Quotation currency	Market value	% of net assets
Transferable securities admitted to an official stock exchange listing			42,280,923.27	96.09%
Shares			42,280,923.27	96.09%
	<i>Belgium</i>		<i>1,793,607.83</i>	<i>4.08%</i>
11,010	COLRUYT SA	EUR	1,793,607.83	4.08%
	<i>Finland</i>		<i>1,357,729.57</i>	<i>3.09%</i>
17,460	KONE OY -B-	EUR	1,357,729.57	3.09%
	<i>France</i>		<i>3,367,000.87</i>	<i>7.65%</i>
46,400	ACCOR SA	EUR	2,035,718.38	4.63%
17,500	L'OREAL SA	EUR	1,331,282.49	3.03%
	<i>Ireland</i>		<i>3,801,370.47</i>	<i>8.64%</i>
531,584	RYANAIR HOLDINGS PLC	EUR	3,801,370.47	8.64%
	<i>The Netherlands</i>		<i>2,068,289.53</i>	<i>4.70%</i>
52,451	RANDSTAD HOLDING	EUR	2,068,289.53	4.70%
	<i>The Netherlands Antilles</i>		<i>1,759,983.03</i>	<i>4.00%</i>
32,920	HUNTER DOUGLAS	EUR	1,759,983.03	4.00%
	<i>United Kingdom</i>		<i>13,329,281.69</i>	<i>30.29%</i>
86,600	CARPETRIGHT PLC	GBP	1,907,268.43	4.33%
727,558	ELECTROCOMPONENTS PLC	GBP	4,002,399.45	9.10%
916,000	MORRISON SUPERMARKETS PLC	GBP	3,663,151.62	8.33%
626,140	PREMIER FARNELL PLC	GBP	2,068,505.29	4.70%
432,000	SAGE GROUP LTD	GBP	1,687,956.90	3.84%
	<i>United States of America</i>		<i>14,803,660.28</i>	<i>33.64%</i>
31,164	AMERICAN EXPRESS CO COM.	USD	1,756,714.68	3.99%
224,500	CHARLES SCHWAB CORP	USD	2,685,020.00	6.10%
47,900	COCA-COLA CO	USD	1,994,077.00	4.53%
37,660	COLGATE-PALMOLIVE CO	USD	1,926,685.60	4.38%
49,290	ETHAN ALLEN INTERIORS INC	USD	1,972,585.80	4.48%
38,800	TARGET CORP	USD	2,014,884.00	4.58%
97,640	TJX COS INC	USD	2,453,693.20	5.58%
Total securities portfolio			42,280,923.27	96.09%

MARGIN OF SAFETY FUND - Fund 1

Statement of Operations and Changes in Net Assets from 01/01/04 to 31/12/04

Expressed in USD

Income		638,291.73
Net dividends		618,964.61
Bank interest on cash account		13.33
Bank interest on time deposits		19,313.32
Other income		0.47
Expenses		801,656.06
Management & advisory fees	Note 4	395,790.99
Custodian & sub-custodian fees	Note 5	25,362.22
Taxe d'abonnement	Note 3	16,542.02
Administrative expenses	Note 5	32,247.67
Incentive and performance fees	Note 4	159,892.96
Domiciliation fees		8,600.00
Professional fees		18,795.99
Bank interest on overdrafts		18.18
Legal fees		11,284.74
Other expenses		133,121.29
Net loss from investments		-163,364.33
Net realised profit on sales of investment securities		6,252,549.52
Net realised profit on foreign exchange		311,052.98
Net realised loss on forward foreign exchange contracts		-899,934.29
Net realised profit		5,500,303.88
Movement in net unrealised appreciation / depreciation on forward foreign exchange contracts		-338,290.13
Movement in net unrealised appreciation / depreciation on investments		809,760.78
Increase in net assets as a result of operations		5,971,774.53
Subscription capitalisation shares		31,524,576.14
Class B		31,524,576.14
Redemption capitalisation shares		-20,709,809.11
Class A		-457,302.94
Class B		-20,252,506.17
Increase in net assets		16,786,541.56
Net assets at the beginning of the year		27,214,205.93
Net assets at the end of the year		44,000,747.49

MARGIN OF SAFETY FUND

Notes to the financial statements

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2004

1. General

MARGIN OF SAFETY FUND is a “société anonyme” with the status of a “société d’investissement à capital variable” under the Luxembourg law of December 20, 2002 on Collective Investment Undertakings and under the law of August 10, 1915 on Commercial Companies. The Fund is incorporated with limited liability for an unlimited duration. The Fund is submitted to Part I of the Law.

The Fund was incorporated under the name “Margin of Safety Fund Limited” with limited liability on January 19, 1998 in the British Virgin Islands as an open-ended investment company. The decision to transfer the Fund’s head office to the Grand Duchy of Luxembourg was taken by way of a resolution of the Board of Directors dated 15 May, 2002, and the Fund was transformed into a Luxembourg SICAV by way of an extraordinary General Meeting held on 14 August, 2002. At the same time, preference shares of the Fund were converted into Class B shares of the SICAV.

The Fund is registered under the number B 88649. Its registered office is in Luxembourg, 39, Allée Scheffer, L-2520 Luxembourg.

As at December 31, 2004, only the sub-fund MARGIN OF SAFETY FUND - Fund 1 is open. This sub-fund has issued two Classes of Shares: Class A and Class B. Both Classes A and B may be issued as accumulation shares or distribution shares at the investor’s discretion.

2. Summary of significant accounting principles

The financial statements have been prepared using accounting principles generally accepted for funds in Luxembourg including the following significant accounting policies :

1. Valuation of investments

The value of any transferable securities which are listed on a Stock Exchange or dealt on a regulated market shall be determined according to their last available price. If such prices are not representative of the fair value, securities will be valued at a fair value at which it is expected that they may be resold, as determined in good faith by and under the direction of the Board of Directors.

In the event that any transferable securities held by the Fund at the valuation day are neither quoted on a Stock Exchange nor dealt in on another regulated market, they are valued at their probable realisation value on the relevant Valuation Date, determined prudently and in good faith.

2. Realised profit and loss on investments

The profits and losses on sales of investments are determined on the basis of average cost.

3. Foreign exchange

The combined financial statements of the Company are established in USD. The combined financial statements are the sum of the sub-fund’s financial statements converted into USD at the rates of exchange ruling at the year end.

The market value of the investments and other assets and liabilities expressed in currencies other than the base currency of each sub-fund have been converted at the exchange rates as at the year end date.

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2004

2. Summary of significant accounting principles (continued)

The costs of investments in currencies other than the base currency have been converted at the exchange rates as at the purchase date. Gains and losses arising on foreign exchange transactions are included in the result of operations.

As at December 31, 2004, the following significant exchange rates were used:

1 EUR	=	1.3621000 USD
1 GBP	=	1.9319197 USD

4. Income from investments

Dividends are recognised as income on the date securities are first quoted ex-dividend, to the extent that information thereon is available to the Company. Interest is accrued on a weekly basis.

3. Tax Considerations

Under legislation and regulations currently prevailing in Luxembourg, the Fund is subject to a capital tax on its net assets at an annual rate of 0.05 % ("Taxe d'abonnement"), calculated and payable quarterly on the basis of the value of the net assets of the Fund at the end of the relevant quarter.

4. Management and Performance fees

For its services the Investment Manager receives from the Sub-Funds a management fee payable quarterly, at an annual rate calculated on the Class's quarterly average Net Asset Value.

The maximum rate for Class A is 1.70% and for Class B is 1.15%.

The Sub-Fund shall pay to the Investment Manager an annual performance fee of up to 20% of the annual increase in the aggregate net assets of the Class A shares and Class B shares over a 15% annual benchmark as defined in the prospectus. For the year ended December 31, 2004 an incentive fee amounting to 159,892.96 USD was charged for the Class A and Class B shares.

5. Custodian and administration fees

The Custodian may receive from the Company a custodian fee accrued monthly and payable monthly in arrears based on the monthly Net Asset Value of the Company.

The Administrator receives from the Company an administration fee accrued monthly and payable monthly in arrears based on the monthly Net Asset Value of the Company.

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2004

6. Open positions on forward exchange rate contracts

At 31/12/04, MARGIN OF SAFETY FUND - Fund 1 had the following open positions:

Purchase	Sale	Agreement date	Maturity date	Unrealised Appreciation/ Depreciation in USD
USD 5,420,950.00	GBP 2,995,000.00	22/07/2004	24/01/2005	-358,798.88
USD 6,287,063.87	EUR 5,140,690.00	22/07/2004	24/01/2005	-715,749.54
USD 178,820.00	GBP 100,000.00	30/07/2004	24/01/2005	-14,162.48
USD 251,660.00	EUR 200,000.00	21/10/2004	24/01/2005	-20,787.20
USD 672,100.00	EUR 500,000.00	06/12/2004	24/01/2005	-9,022.65
USD 967,350.00	GBP 500,000.00	06/12/2004	24/01/2005	2,523.40
USD 840,180.00	GBP 440,000.00	22/12/2004	24/01/2005	-8,880.40
USD 144,300.00	GBP 75,000.00	24/12/2004	24/01/2005	-424.93
			TOTAL	-1,125,302.68

7. Co-management

In order to reduce operational and administrative charges while allowing a wider diversification of investments, the Company may decide that part or all of its assets will be co-managed with the assets belonging to other collective investment schemes.

Each Co-Managed Entity holds a proportion of the Co-Managed Assets corresponding to the proportion of its net assets to the total value of the Co-Managed Assets.

In 2004, the SICAV did not use the co-management's facility and has no plans in the near future to do so.

8. Statement of changes in Portfolio

The statement of changes in portfolio is available free of charge at the SICAV's head office.

