



MARGIN OF SAFETY FUND

Société d'Investissement à Capital Variable
R.C.S. B 88649

Audited annual report

at 31/12/10

MARGIN OF SAFETY FUND

Table of Contents

	Page
Management and Administration	3
Board of Directors	3
Information to the Shareholders	4
Manager's Report	5
Report of the Réviseur d'Entreprises agréé	8
MARGIN OF SAFETY FUND - Fund 1	10
Notes to the financial statements	15

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

5, Allée Scheffer
L-2520 Luxembourg

INVESTMENT MANAGER

Pastel & Associés S.A.
9-11, Avenue Franklin D. Roosevelt
F-75008 Paris

PROMOTOR

Pastel & Associés S.A.
9-11, Avenue Franklin D. Roosevelt
F-75008 Paris

AUDITOR

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

CUSTODIAN AND CENTRAL ADMINISTRATION AGENT

CACEIS Bank Luxembourg
5, Allée Scheffer
L-2520 Luxembourg

MANAGEMENT COMPANY

Luxcellence Management Company S.A.
5, Allée Scheffer
L-2520 Luxembourg

Board of Directors

Chairman of the Board

M. John MILLS, Managing Director, Maitland Luxembourg S.A.

Members of the Board

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

M. Yves-Pascal PELCENER, Member of the Board of Pastel & Associés S.A.

M. Antoine GILSON DE ROUVREUX, Managing Director, Luxcellence Management Company S.A.

MARGIN OF SAFETY FUND

Information to the Shareholders

Supplementary information to Shareholders on Savings Directive 2003/48/EC

The Board of Directors resolves that the following Sub-Fund is out of the scope of the Law for the realised and distribution income:

MARGIN OF SAFETY FUND - Fund 1 with 2.5% of its assets invested in debt-claims.

This update has been effective from May 1, 2010 and will remain in force until April 30, 2011 date at which the status will be updated again.

MARGIN OF SAFETY FUND

Manager's Report

Investment performance Margin of Safety Fund – Fund 1

(cumulative figures after all fees and expenses)

Class P shares

In 2010, the Fund's NAV per share increased by 16.2%, resulting in a cumulative performance since inception on February 2nd, 1998, of 295.1%. As a result, while \$1,000 invested at inception in Margin of Safety Fund P Class (USD) would now be worth \$3,951, the same \$1,000 invested in the MSCI World index in USD (with dividends reinvested) would now equal \$1,749.

Class I shares

In 2010, the Fund's NAV per share increased by 17.3%, resulting in a cumulative performance since inception on February 2nd, 1998, of 279.8%. As a result, while \$1,000 invested at inception in Margin of Safety Fund I Class (USD) would now be worth \$3,798 the same \$1,000 invested in the MSCI World index in USD (with dividends reinvested) would now equal \$1,749.

Management report

In 2010, despite turbulence in the financial markets, your fund generated substantially positive returns, thereby increasing its long-term outperformance compared to major stock market indices. This result confirms the value that our management style, based on consistency, long-haul investing and independence, brings to patient and rational investors, whether individual or institutional ones. Therefore, to use a terminology dear to consultants and professional fund selectors, your fund, instead of being "satellite" holdings, truly belongs to the "core" of our investors' portfolios.

Once again, 2010 provided an opportunity to demonstrate the superior effectiveness of an approach favoring **concentration**, a concept we apply at all levels of our work:

- concentration on our profession as corporate financial analysts,
- concentration of our research on companies we understand, and with which we have been familiar, in most cases, for a long time,
- concentration on our principles: independence, importance of high margins of safety, monitoring of the intrinsic value of investments made in order to maintain a reasonably valued portfolio,
- concentration of the portfolio around several key positions (usually between 15 and 30 positions).

The returns achieved in 2010, on the heels of those obtained in 2009, were the direct result of our staying the course in 2009 as well as 2010: no changes were made to the portfolio structure unless justified by some truly attractive arbitrage opportunities. No ad-hoc or knee-jerk decision interfered with our investment process. Hence, rather than listening to the doomsayers who predicted the large-scale collapse of economies in April-May this year, then again over the summer, and while your fund went from a positive return of approximately 20% in the spring to a negative return of a few percentage points in the fall, we stuck with our investments, confident in the validity of our analyses and our approach.

MARGIN OF SAFETY FUND

Manager's Report

In sum, the portfolio of your fund is currently made up of companies that tend to share some common features:

- They have sound financial structures and their debt levels are reasonable in relation to their capacity to generate cash flows across economic cycles.
- Their business models have proven their effectiveness at generating profits over long periods, reflected in average operating margins, returns on equity and on invested capital, generally higher than those of their competitors.
- They enjoy strong and sustainable competitive positions likely to allow them to maintain, or gain, market shares against competitors weakened by the consequences of a potentially extended economic downturn.
- They are headed by experienced management teams, who most often also hold equity interests in their companies and are thus committed to their development over the long term.

The shares of these high-quality companies are trading today at prices that remain attractive when compared to our intrinsic value estimates.

Finally, it is important to note that the gains made by your fund in the last two years merely confirm, in our view, the extreme undervaluation of its portfolio at the height of the crisis and do not detract in any way from its future upside potential*.

Evolution of the portfolio structure in 2010

In 2010, the structure of the portfolio underwent a certain number of changes.

During the year, new positions were built or reinforced such as Best Buy, Charles Schwab, Cintas Corp. and Leucadia National Corp..

At the same time, a number of positions were entirely or partially disposed of, such as Johnson & Johnson, Lowe's and USG Corp..

As a result of these transactions, the Fund's equity portion represented 87.7% of the net asset value. 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.

As of December 31th, 2010, the geographic breakdown of the Fund's portfolio, before currency hedging, was as follows (2009 figures are provided for comparison purposes):

	2010	2009
- Euro Zone:	19.0%	36.3%
- United Kingdom:	33.1%	25.1%
- United States:	47.9%	38.6%

MARGIN OF SAFETY FUND

Manager's Report

As of December 31th, 2010, the breakdown by industry sector of the equity portion of the Fund's portfolio was as follows (2009 figures are provided for comparison purposes):

	2010	2009
- Business to business services:	39.6%	41.7%
- Durable goods:	15.8%	17.2%
- Financial services:	9.0%	0.0%
- Industrials:	5.6%	17.2%
- Healthcare:	0.0%	4.7%
- Holdings:	9.3%	4.2%
- Media:	0.0%	1.3%
- Non-food retailing:	20.7%	13.7%

Regards,

David Pastel,
Pastel&Associés S.A.

* This report does not contain any forecast of future rates of return. It only conveys the opinions of its author at the time of writing this report. These opinions may change at any time without any notice to be given. Moreover, they may be proved wrong as circumstances change and as additional facts become publicly known. In addition, they are not meant to be used as elements in making a decision to buy or sell shares of the Fund or any other securities.

MARGIN OF SAFETY FUND

REPORT OF THE REVISEUR D'ENTREPRISES AGREE

To the shareholders of
MARGIN OF SAFETY FUND
5, allée Scheffer
L-2520 Luxembourg

We have audited the accompanying financial statements of **MARGIN OF SAFETY FUND**, which comprise the statement of net assets and the securities portfolio as at December 31, 2010 and the statement of operations and the statement of changes in net assets for the year then ended, and a summary of significant accounting policies and other explanatory information.

Board of directors of the SICAV responsibility for the financial statements

The board of directors of the SICAV is responsible for the preparation and fair presentation of these financial statements in accordance with Luxembourg legal and regulatory requirements relating to the preparation of financial statements, and for such internal control as the Board of Directors of the SICAV determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Responsibility of the Réviseur d'Entreprises agréé

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 as adopted for Luxembourg by the Commission de Surveillance du Secteur Financier. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the judgment of the Réviseur d'Entreprises agréé, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the Réviseur d'Entreprises agréé considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board of Directors of the SICAV, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

MARGIN OF SAFETY FUND

REPORT OF THE REVISEUR D'ENTREPRISES AGREE

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of **MARGIN OF SAFETY FUND** as of December 31, 2010, and of the results of its operations and changes in its net assets for the year then ended in accordance with Luxembourg legal and regulatory requirements relating to the preparation of the financial statements.

Other matter

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. However, we have no observation to make concerning such information in the context of the financial statements taken as a whole.

Luxembourg, April 29, 2011

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



Nathalie Dogniez
Partner



Patrice Perichon
Director

MARGIN OF SAFETY FUND

- Fund 1

MARGIN OF SAFETY FUND - Fund 1
Financial Statements at 31/12/10

Statement of net assets at 31/12/10

Expressed in USD

Assets			17,825,053.72
Securities portfolio at market value	Note 2		15,515,445.28
<i>Cost price</i>			<i>13,814,976.50</i>
<i>Unrealised profit on the securities portfolio</i>			<i>1,700,468.78</i>
Cash at banks and liquidities			25,333.27
Time deposits			1,961,000.00
Brokers receivable			31,385.80
Unrealised profit on forward foreign exchange contracts	Note 6		265,389.36
Other assets			26,500.01
Liabilities			125,029.89
Brokers payable			35,959.43
Accrued management fees	Note 4		42,088.96
Other liabilities			46,981.50
Net asset value			17,700,023.83

Changes in number of shares outstanding from 01/01/10 to 31/12/10

	Shares outstanding at 01/01/10	Shares issued	Shares redeemed	Shares outstanding at 31/12/10
Class I Capitalisation shares	5,763.77	102.00	1,569.00	4,296.77
Class P Capitalisation shares	299.67	94.27	45.00	348.94
Class HI Capitalisation shares	-	-	-	-
Class HP Capitalisation shares	-	-	-	-

MARGIN OF SAFETY FUND - Fund 1

Key figures relating to the last 3 years

	<i>Year ending at:</i>	31/12/10	31/12/09	31/12/08
Total Net Assets	USD	17,700,023.83	19,688,818.48	15,993,851.10
Class I		USD	USD	USD
Capitalisation shares				
Number of shares		4,296.77	5,763.77	7,610.77
Net asset value per share		3,798.49	3,239.19	1,943.49
Class P		USD	USD	USD
Capitalisation shares				
Number of shares		348.94	299.67	577.71
Net asset value per share		3,951.42	3,399.99	2,058.26
Class HI		EUR	EUR	EUR
Capitalisation shares				
Number of shares		-	-	6.82
Net asset value per share		-	-	1,274.55
Class HP		EUR	EUR	EUR
Capitalisation shares				
Number of shares		-	-	0.64
Net asset value per share		-	-	1,348.76

MARGIN OF SAFETY FUND - Fund 1

Securities portfolio at 31/12/10

Expressed in USD

Quantity	Denomination	Quotation currency	Market value	% of net assets
Transferable securities admitted to an official stock exchange listing and/or dealt in on another regulated market			15,515,445.28	87.66%
Shares			15,515,445.28	87.66%
	<i>Finland</i>			
44,566.00	UPONOR OYJ	EUR	824,159.39	4.66%
	<i>France</i>			
10,356.00	CIMENT VICAT SA	EUR	864,855.45	4.89%
	<i>The Netherlands</i>			
23,934.00	RANDSTAD HOLDING	EUR	1,263,234.13	7.14%
	<i>United Kingdom</i>			
63,589.00	CARPETRIGHT PLC	GBP	5,140,539.35	29.04%
174,569.00	ELECTROCOMPONENTS PLC	GBP	788,720.65	4.46%
420,500.00	HAYS	GBP	720,305.17	4.07%
23,625.00	NEXT PLC	GBP	841,421.01	4.75%
130,100.00	PERSIMMON PLC	GBP	724,324.80	4.09%
274,822.00	PREMIER FARNELL PLC	GBP	841,781.63	4.76%
	<i>United States of America</i>			
25,000.00	BEST BUY CO INC	USD	1,223,986.09	6.91%
81,800.00	CHARLES SCHWAB CORP/THE	USD	7,422,656.96	41.93%
47,300.00	CINTAS CORP	USD	857,250.00	4.84%
49,200.00	LEUCADIA NATIONAL CORP	USD	1,399,598.00	7.91%
33,796.00	LOWE'S COMPANIES INC	USD	1,322,508.00	7.47%
13,778.00	MOHAWK INDUSTRIES INC	USD	1,435,656.00	8.10%
25,400.00	PATTERSON COS INC	USD	847,603.68	4.79%
			782,039.28	4.42%
			778,002.00	4.40%
Total securities portfolio			15,515,445.28	87.66%

MARGIN OF SAFETY FUND - Fund 1

Statement of operations and changes in net assets from 01/01/10 to 31/12/10

Expressed in USD

Income		325,044.97
Net dividends		323,144.60
Bank interest on time deposits		873.06
Other financial income		1,027.31
Expenses		367,776.75
Management & management company fees	Note 4	219,114.72
Custodian & sub-custodian fees		13,913.69
Taxe d'abonnement	Note 3	8,708.85
Administrative expenses		18,312.06
Domiciliation fees		10,225.18
Professional fees		22,415.56
Legal fees		18,784.52
Brokers fees		44,236.21
Other expenses		12,065.96
Net loss from investments		-42,731.78
Net realised profit / loss on:		
- sales of investment securities		1,474,832.53
- forward foreign exchange contracts		441,962.41
- foreign exchange		-508,496.73
Net realised profit		1,365,566.43
Movement in net unrealised appreciation / depreciation on:		
- investments		1,516,574.67
- forward foreign exchange contracts		47,724.16
Increase in net assets as a result of operations		2,929,865.26
Subscription capitalisation shares		706,086.46
Class I		357,304.98
Class P		348,781.48
Redemption capitalisation shares		-5,624,746.37
Class I		-5,473,542.77
Class P		-151,203.60
Decrease in net assets		-1,988,794.65
Net assets at the beginning of the year		19,688,818.48
Net assets at the end of the year		17,700,023.83

MARGIN OF SAFETY FUND

Notes to the financial statements

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2010

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 May 15, 2002, and the Fund was transformed into a Luxembourg SICAV by way of an extraordinary General Meeting held on August 14, 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, 5, Allée Scheffer, L-2520 Luxembourg.

As from April 28, 2006, the Fund has designated Luxcellence Management Company S.A. as management company in the meaning of article 13 of the Luxembourg law dated December 20, 2002.

As at December 31, 2010 only the sub-fund MARGIN OF SAFETY FUND - Fund 1 is open. This sub-fund has issued two Classes of Shares: Class I (in USD) and Class P (in USD) All Classes may be issued as accumulation shares or distribution shares at the investor’s discretion. Class I and Class P shares are also expressed in EUR for the purpose of subscriptions and redemptions.

The sub-fund is expressed in USD, consequently, the financial statements of the SICAV consist in the financial statements of the Fund 1 sub-fund.

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.

Forward foreign exchange contracts are valued at the previous day closing price.

2. Realised profit and loss on investments

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

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2010

2. Summary of significant accounting principles (continued)

3. Foreign exchange

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.

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, 2010, the following significant exchange rates were used:

1 EUR	=	1.3362 USD	1 CAD	=	1.0030 USD
1 GBP	=	1.5524 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 Management company fees

For its services the Investment Manager receives a management fee payable quarterly, at an annual rate calculated on each Class's quarterly average Net Asset Value. The annual management fees are as follows:

Class I:	maximum 0.90%
Class P:	maximum 2%
	effective 1.80%

In addition to the management fees, the Fund shall pay a management company fee to the Management Company, payable monthly, at an annual rate of 0.05% per annum with a minimum of EUR 40,000.00 per annum which shall be calculated on the Fund's average Net Asset Value.

5. Performance fees

The 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 I shares and Class P shares over a 12% annual benchmark as defined in the prospectus. For the year ended December 31, 2010, no performance fee was paid by the Fund.

MARGIN OF SAFETY FUND

Notes to the financial statements at December 31, 2010

6. Open positions on forward foreign exchange rate contracts

At December 31, 2010, MARGIN OF SAFETY FUND - Fund 1 had the following open positions:

Sale	Purchase	Maturity date	Unrealised Appreciation/ Depreciation in USD
-1,565,100.00 EUR	2,224,476.63 USD	04/02/2011	133,283.92
-1,845,500.00 GBP	2,989,710.00 USD	04/02/2011	125,510.81
-150,000.00 GBP	233,880.00 USD	04/02/2011	1,081.37
-100,000.00 USD	76,057.20 EUR	04/02/2011	1,623.07
-264,780.00 USD	200,000.00 EUR	04/02/2011	2,448.00
-31,503.94 USD	23,942.80 EUR	04/02/2011	486.99
-371,140.00 USD	280,000.00 EUR	04/02/2011	2,979.20
-100,000.00 EUR	131,590.00 USD	04/02/2011	-2,024.00
	TOTAL		265,389.36

7. Statement of changes in Portfolio

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