Newsletter Q3 2005

Most recipients of this quarterly newsletter will also be receiving some other form of regular communication from us. We do monthly newsletters on Overstone Global Equity Fund and, henceforth, also on Overstone European Equity Fund; and a quarterly newsletter on Overstone Opportunity Multi Fund. This newsletter may repeat a little of what is in the monthlies; and it ranges more widely and bangs on for longer.

Overstone Global Equity Fund was launched on 1st June and has assets of $166 million. Overstone European Equity Fund started on 1st October with assets of $4 million; and Overstone Opportunity Multi Fund ("OOMF") will start on 1st November.

Our approach in the management of global equity portfolios is long-only, no leverage, value-focused, large-cap, index-ignorant, highly concentrated, and anti-short-term. The European Fund, under the management of Claus Anthon, has much the same features except that it digs deeper in terms of company size.

At the bottom of this page is a health warning which applies to everything that we do. OOMF deserves a special health warning: we are not trying to cover the waterfront and to provide a broad exposure with this fund. OOMF will be focused eclectically on just a few (6-12) funds with managers who have a philosophy similar to our own (value-focused, index-ignorant, highly concentrated), but who are operating in areas some of which are much too specialized for us to be investing in directly. At the start, we particularly want to have holdings in a Taiwanese fund, a Korean fund and a Russian fund; also a gold share fund, and a significant proportion in a Japanese fund.

It must therefore be emphasised that the object of OOMF is to make money not to control volatility. Given the volatility of these markets, there could be quite large moves up or down from month to month and we cannot be sure that there will be more up than down.

Oldfield Partners LLP, 144 Buckingham Palace Road, London, SW1W 9TR.
Telephone: +44 (0)20 7259 1000
www.oldfieldpartners.com

Newsletter Q3 2005

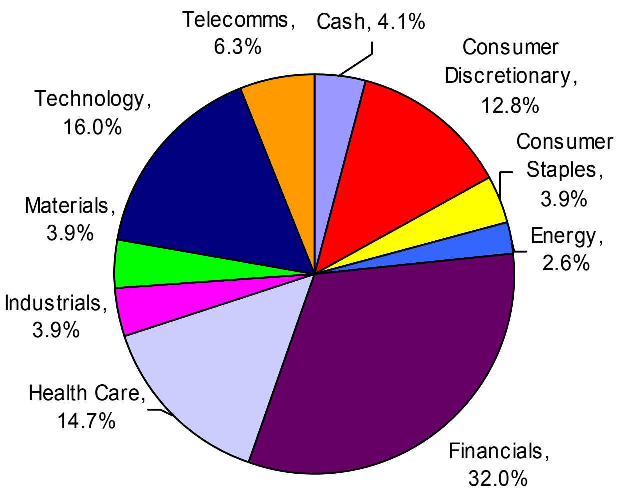
Performance Summary as at 30 September 2005

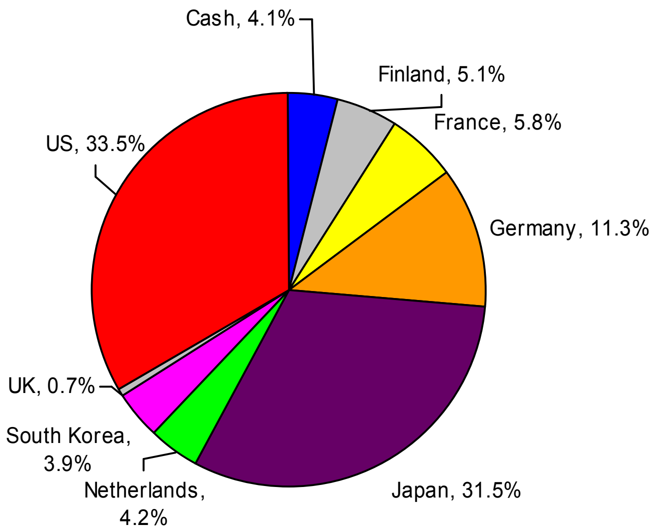
US$ terms	Global Equity Composite 1	MSCI World (NDR)
Q3 2005	+11.7%	+7.0%
Since 14/03/05	+7.2%	+4.8%
2005 to date	+14.1%	+6.2%
Since inception *	+215.5%	+68.8%
Since inception per annum *	+14.0%	+6.2%

1 The performance shown is of a composite of all US dollar denominated global equity portfolios managed by Richard Oldfield at Alta Advisers from 1997 to 11th March 2005 and at Oldfield Partners since 14th March 2005. Before 2000 the performance of two portfolios is excluded from the composite because their returns were inflated by the inclusion, in those portfolios only, of an unquoted investment which, following its flotation, had a large favourable impact on returns. All returns are gross of fees to 11 March 2005, then net of fees thereafter.

* Inception 01 Jan 1997. Source of data: Alta Advisers Ltd. and Oldfield Partners LLP

Sector and country breakdown as at 30 September 2005





Source of data: Oldfield Partners LLP. Representative global equity portfolio used.

Oldfield Partners LLP, 144 Buckingham Palace Road, London, SW1W 9TR.
Telephone: +44 (0)20 7259 1000
www.oldfieldpartners.com

Oldfield PARTNERS

Newsletter Q3 2005

Performance of Five Largest Holdings *

	Portfolio Weighting * %	Quarterly Performance (local terms) %	Quarterly Performance (US$ terms) %
Takeda Pharmaceutical	8.2	+23.8	+21.0
Morgan Stanley	7.2	+3.3	+3.3
Microsoft	7.0	+3.9	+3.9
Merck	6.5	-10.5	-10.5
Tiffany	6.3	+21.7	+21.7

* as at end of period. Representative global equity portfolio used

Source: Oldfield Partners LLP

Commentary

The Nobel Laureate Kenneth Arrow, employed as a meteorologist in the US air force during the Second World War, was expected to produce medium and long term weather forecasts. He quickly concluded that these were no better than randomly right and asked to be relieved of the responsibility. The response came back: “The commanding general is well aware that your forecasts are no good. However, they are essential for planning purposes”.

This sums up our own attitude to prediction. We are hesitant about predicting things ourselves, and also sceptical of other people’s predictions. That scepticism is sometimes the source of opportunity. Last year, we thought that the unanimity, more or less, of forecasters that the oil price would fall to $24 or so at a time when the current price was $32 was a strange anomaly. One only had to suppose instead that the oil price might remain where it was to conclude that the whole of the energy sector was greatly undervalued.

Oldfield Partners LLP, 144 Buckingham Palace Road, London, SW1W 9TR.
Telephone: +44 (0)20 7259 1000
www.oldfieldpartners.com
Oldfield Partners LLP is authorised and regulated by the Financial Services Authority

We now feel that this anomaly may have reversed entirely. Anyone in the investment world has become familiar over the past year with names such as Hubbert and Matthew Simmons who have written about the rundown in the world's reserves of oil and the limits of annual production capacity. There seems to us now to be a tremendous confidence that the price of oil will go higher over the next several years. But during the past year the facts have not changed; only the perception of them has. Without exactly predicting it, we think there is a decent chance of a fall in the oil price over the coming months.

The direct consequence of this scepticism of current bullishness is that we no longer see the opportunities that we did in oil companies. We therefore no longer hold Anadarko Petroleum, which used to be our largest holding, or Lukoil. More broadly and more indirectly, if oil is weak, and if that weakness is not caused by a marked economic slowdown (big ifs), that would be very good for economies and therefore for markets. We think that it is perfectly possible for stock markets generally to continue to perform well, given that the price earnings ratio of the MSCI World Index is only just above 14, lower than almost at any time since 1991. In various places, and in numerous stocks, we see value.

One of the reasons for this relatively low PE ratio for world markets is that Japan used to be a large part of the World Index and with itself a very high valuation. We have written in recent Overstone newsletters quite a bit about Japan. The level of valuation is reasonable. Companies have had to deal with more than ten awful years by cutting their levels of costs, and are now generating very high cash flow while many are paying much more attention to shareholders, with dividend increases and share buybacks, than hitherto.

The last piece in the Japan jigsaw puzzle is now in place: the end of deflation. Real estate prices, consumer and capital spending, and bank lending are all rising. Reflation will do an enormous amount of good both to revenues and to profit margins. It is usually sensible to be wary of a consensus, and there is a pretty strong consensus among investors now about Japan. But just occasionally changes are so major and long-cycle in nature that consensus is fine. The position of the Japanese stock market now reminds us of the position of the US stock market in August 1982, when comments by Dr. Henry Kaufman were the catalyst that started what turned out to be a long bull market – 18 years. Within a few weeks, nearly all investors felt that this was indeed a bull market. That is the feeling about Japan now.

We pointed out in the last quarterly newsletter that, while the Standard & Poors Index for the US stock market had given a return of 50% since March 2003, a portfolio made up of Coca Cola, Microsoft, Walmart, IBM, Pfizer and Colgate-Palmolive would have given a return of zero. The average price earnings ratio of that portfolio would now be 20 compared with 50 in 1999. Although not strikingly cheap, this level of valuation is at least intriguingly different. The part of markets, especially the US market, categorized as "quality growth" looks strongly undervalued, more than almost at any other time in history. We have been patient holders of Microsoft for three years. In recent months we have bought both IBM (covered in an Overstone newsletter) and Walmart which still manages to produce growth in its domestic market, has international activities with scope for higher growth, and is on a PE in the mid teens.

The Overstone funds which we manage are so named partly because there was a notable 19th century banker called Overstone but mainly because he gave his name to a road in Hammersmith where one of the partners at Oldfield Partners bought a house in 1976 for £13,225, an investment which has good value associations. Lord Overstone was quoted by John Plender in the Financial Times on 17th October, referring to "a slight premonitory movement of the ground under our feet". It was Lord Overstone who characterised the cycle of markets: "quiescence, improvement, growing confidence, prosperity, excitement, overtrading, convulsion, pressure, stagnation, distress, ending again in quiescence."

In stock markets we are now somewhere in the first half of this cycle: generally somewhere in or near prosperity, but in Japan more like growing confidence. Since March 2003, and especially since April 2004, the decline in volatility of equity markets has been quite striking. In the last few weeks there have been glimmerings of a reversal of this, which should indeed be expected. "Volatility" is often used as a euphemism for going down; but volatility in investment terms means up and down. Our own view is that there is a good probability, despite the odd rumble, that there will be strong returns from equities over the next twelve months or so; but that there will be some nasty offputting bumps.

Oldfield Partners LLP, 144 Buckingham Palace Road, London, SW1W 9TR.
Telephone: +44 (0)20 7259 1000
www.oldfieldpartners.com
Oldfield Partners LLP is authorised and regulated by the Financial Services Authority