Southeastern Asset Management, Inc.®

Advisor to Longleaf Partners Funds

To Longleaf Shareholders

After delivering strong returns in 2009 and 2010, we are disappointed to report weak results for 2011. We prefer every year be outstanding, but our multi-year orientation focuses us on longer investment time horizons. Over Southeastern's 36 year history, most five year holding periods have been rewarding. Currently, however, our five year returns are burdened by the unprecedented 2008 price declines. Unfortunately, 2011 did nothing to offset our most challenged year.

Cumulative Returns at December 31, 2011

	Since Inception[1]	20 Year	Ten Year	Five Year	Three Year	One Year	4Q
Partners Fund (Inception 4/8/87)	**1102.46%**	**612.03%**	**44.35%**	**(13.48)%**	**75.92%**	**(2.85)%**	**10.53%**
S&P 500 Index	657.84	350.12	33.35	(1.24)	48.59	2.11	11.82
Small-Cap Fund (Inception 2/21/89)	**817.43**	**754.61**	**130.85**	**7.21**	**85.91**	**1.79**	**9.11**
Russell 2000 Index	558.51	413.44	72.76	0.75	54.59	(4.18)	15.47
International Fund (Inception 10/26/98)	**152.31**	**na**	**33.76**	**(22.27)**	**11.61**	**(20.29)**	**0.55**
EAFE Index	47.60	na	57.78	(21.48)	24.75	(12.14)	3.33
Inflation + 10%	[2]	953.31	224.06	78.30	41.97	12.96	na

(1) *During the inception year, the S&P 500 and the EAFE Index were available only at month-end; therefore the S&P 500 value at 3/31/87 and the EAFE value at 10/31/98 were used to calculate performance since IPO. All returns include reinvested dividends and distributions but not the deduction of taxes. Current performance may be lower or higher. Prior to 2010 the Partners and International Funds used currency hedging as an investment strategy. The U.S. Bureau of Labor Statistics compiles the monthly CPI-U values used to calculate inflation. Past performance does not guarantee future results, fund prices fluctuate, and the value of an investment at redemption may be worth more or less than the purchase price. The annual expense ratios for the Longleaf Partners, Small-Cap, and International Funds are 0.91%, 0.92% and 1.37%, respectively. The risks associated with an investment in the Longleaf Partners Funds are detailed on pages 15 to 17 of the Prospectus. These risks include stock market risk, investment selection risk, corporate ownership risk, non-diversification risk, non-US investment risk, small cap risk (particularly with respect to the Small-Cap Fund), focused geographic risk, and derivatives risk.* ***Call (800)445-9469 or go to southeasternasset.com for current performance information and southeasternasset.com/misc/prospectus.cfm for the Prospectus and Summary Prospectus, both of which should be read carefully before investing to learn about Fund investment objectives, risks, and expenses.***

(2) *Inflation + 10% since inception for the Partners, Small-Cap and International Funds was 1896.82%, 1464.43% and 373.27%, respectively.*

Average Annual Returns at December 31, 2011

	Since Inception[1]	20 Year	Ten Year	Five Year	Three Year	One Year
Partners Fund (Inception 4/8/87)	**10.58%**	**10.31%**	**3.74%**	**(2.85)%**	**20.72%**	**(2.85)%**
S&P 500 Index	8.53	7.81	2.92	(0.25)	14.11	2.11
Small-Cap Fund (Inception 2/21/89)	**10.18**	**11.32**	**8.73**	**1.40**	**22.96**	**1.79**
Russell 2000 Index	8.60	8.52	5.62	0.15	15.63	(4.18)
International Fund (Inception 10/26/98)	**7.27**	**na**	**2.95**	**(4.91)**	**3.73**	**(20.29)**
EAFE Index	3.00	na	4.67	(4.72)	7.65	(12.14)

As the largest shareholder of the Longleaf Partners Funds, we are not pleased with these results. We are, however, highly confident future returns should be exceptionally rewarding because of the quality of the businesses we own, their prospects over the next five years, and the compellingly low prices we are paying for them. This unique collection of opportunities would not exist had there not been the macro fears and resulting high market correlations in the third quarter that damaged 2011 results.

Because our future returns will be determined by the companies in the Longleaf portfolios, we have summarized the investment case for the five largest holdings in the three Funds. These names are representative of the caliber of our portfolio components. The qualified merits of "business, people, price," including the current free cash flow (FCF) yield at each, will illustrate why we are convinced we should deliver positive, excess performance over the next few years.

Building Blocks for Future Performance

Partners Fund

Five Largest Holdings	%
Dell	8.9
Chesapeake Energy	7.7
Loews	6.6
Aon	6.1
DIRECTV	5.7

Dell: Based in Austin, Dell has transformed its business by offering a combination of servers, services, storage, and software to provide enterprise solutions which now dominate and complement the desktop and laptop computing segment. As the world becomes "unplugged," demand for solutions to manage hardware, software, and security will grow. With Dell's product mix change, the company has delivered substantially higher margins and earnings. Michael Dell, founder and CEO, is a multi-billion dollar owner and has been a major insider purchaser over the last year. The market continues to focus on the "dying" PC business even though it is only 35% of our appraisal value, and analysts persist in evaluating the company against the consumer market which represents only about 10% of revenues. In assigning a multiple to the earnings, most analysts also disregard the large net cash that generates virtually no earnings and equals over a quarter of the share price. As long as the market ignores the growing free cash flow coupon, Dell should continue to use much of it to repurchase shares and build value even faster. Using expected 2012 FCF, the company's FCF yield is 16.2%, but adjusted for the net cash, is over 20%.

Chesapeake Energy: Based in Oklahoma City, Chesapeake has assembled at low cost the best set of natural gas assets in the U.S. and a rapidly growing portfolio of oil reserves and production. Aubrey McClendon, co-founder and CEO, has been controversial but has consistently monetized assets at far above cost through either joint ventures like the most recent Utica transaction in late 2011 or the full sale of the Fayetteville holdings in early 2011. The stock sells for less than half of our NAV in part because the market doubts McClendon's willingness to spend less than cash flow on additional lease acreage, but mostly because natural gas has declined to under $3/mcf due to oversupply and the current warm winter. At these prices, drilling is unprofitable, and supply will eventually decline as gas drilling commitments are met and rigs move to much more profitable oil wells. Longer term, LNG (liquefied natural gas) facilities are preparing to export gas to Asia and Europe where prices are over $10/mcf and transportation, industrial, and electricity generation demand is accelerating. Natural gas assets continue to attract large offshore buyers at substantially higher prices than Chesapeake sells for in the market. The free cash flow yield with $3/mcf gas and flat production in 2012 is 7.6%, but if adjusted for a higher gas price a year or two out as the futures curve suggests, the yield is well into the double digits. These numbers are also before backing out $10-15 per share for assets such as drilling carries, oil service company investments, and pipelines that provide little in earnings today but will probably soon be monetized at good prices.

Loews: Based in New York, Loews is a diversified holding company sagaciously stewarded by Jim Tisch and his management team. In addition to $4 billion in cash available to deploy opportunistically, the company's primary assets are CNA, a dramatically improved property/casualty insurer led by talented Chubb alum, Tom Motamed, Diamond Offshore, an offshore drilling rig operator with substantial cash flow and a history of acquiring, leasing, and disposing of rigs successfully in a volatile industry, and Boardwalk, a natural gas pipeline and storage company with a growing cash coupon. The Tisch family owns approximately 25% of the stock and has intelligently allocated capital and delivered value growth for investors over decades. The company sells for roughly half of appraised value, in large part due to the mispricing of publicly traded CNA and the resulting conglomerate discount on Loews. Not only does insurance remain out of favor, but the results of Motamed's turnaround have not been given credit, and earnings are highly volatile with the unpredictability of insured events. CNA shares sell for half of book value. As long as Jim Tisch is making capital allocation decisions, whether for large share repurchases at these discounts or for high-return acquisitions, we believe value will grow materially. Using consensus 2012 earnings, the company's current FCF yield is 9.0%, but adjusted for the net cash, is 11.6%.

Aon: With a planned headquarters move from the U.S. to London, Aon is the top global insurance broker in an oligopoly. The company also is a leader in the investment and benefits consulting business. CEO Greg Case and his team have increased margins substantially and gained share over the last six years. Additionally, they have reinvested the growing cash coupon into Aon's discounted shares and several successful acquisitions. The stock sells below 70% of our appraisal because of both depressed earnings from low interest on premium float and a substantial difference in reported and cash earnings due to goodwill amortization from acquisitions. As long as the shares remain significantly undervalued, management expects to grow value-per-share by meaningful repurchase activity. Based on 2012 expected FCF, Aon yields 10.1%.

DIRECTV: Based in El Segundo, DIRECTV is the largest satellite broadcaster in the U.S. and has dominant market share in Latin America. Domestically the company offers unique technology and programming that attract high-end customers with little churn. In Latin America, most countries have no alternative because neither cable nor fiber have been or will be laid where there is minimal infrastructure. The market puts a low growth multiple on the entire earnings stream, not accounting for the more valuable emerging market growth. Additionally, SAC (subscriber acquisition cost) is counted against earnings rather than being treated as discretionary capex that provides a return via revenues over multiple years. The stock trades below 70% of our appraisal, and Mike White has done a tremendous job building value by using the substantial cash coupon to buy in shares aggressively at deeply discounted levels. The free cash flow yield based on 2012 expected FCF is 10.3%.

Partners Fund FCF Yield Summary	%
Average FCF Yield[(a)]	10.6
Average Adjusted FCF Yield[(a)]	13.9
S&P 500 Earnings Yield[(b)]	7.9

See footnote on page 6.

Small-Cap Fund

Five Largest Holdings	%
Texas Industries	7.6
tw telecom	7.1
Lamar Advertising	6.4
Service Corp	6.1
Madison Square Garden	5.5

Texas Industries: Based in Dallas, Texas Industries (TXI) owns valuable aggregate assets and cement plants in California and Texas, where TXI is the largest producer. These are two of the most populous states with Texas among the fastest growing, and they receive the largest share of federal highway spending. Since new cement plants are difficult to permit and build, TXI's facilities have a capacity and cost advantage in these top markets. The stock sells far below replacement value because depressed residential and commercial construction and lack of a transportation bill in Congress have created uncertainty as to when demand will increase utilization rates beyond 50% to levels that produce meaningful free cash flow. In the last year, others have paid per ton prices for U.S. cement plants that make TXI a steal. Our appraisal is based on future free cash flows and replacement values for the assets. Because of the low plant utilization, TXI may not generate FCF in 2012.

tw telecom: With headquarters in Littleton, CO, tw telecom (TWTC) is a leading national provider of managed telecommunications services for businesses. Because they own their local area fiber networks, the company provides superior facilities-based services versus most competitors who are re-sellers that must pay to use others' networks. Management has the best operating record among CLECs (competitive local exchange companies). The market puts an industry multiple on GAAP earnings, which are far below net free cash flow because of large depreciation from building out the network. TWTC's margins are much higher than those of industry re-sellers, warranting a higher multiple for TWTC. The FCF yield based on estimated 2012 free cash flow is 0.6%. Adjusted for the excess depreciation, the yield is 10.8%.

Lamar Advertising: Based in Baton Rouge, Lamar owns supply-constrained real estate via billboards, primarily in mid-tier markets. The company's boards have a competitive advantage due to strong local market share and regulations that make building new supply difficult. We have owner operators in the Reilly family who added to their stake near the lows of 2011. Their history includes smart acquisitions as well as prudent balance sheet management. The market has sold the stock down because of skepticism over the virtue of converting to digital boards and concerns about leverage given volatile local advertising since the recession. Debt is being paid down at a rapid pace, and the company's recent results have shown improved local advertising as well as incremental benefits from digital. Our appraisal is below comparable transactions, and the value should grow rapidly as the economy returns to more normal growth. Based on 2012 FCF estimates, the FCF yield is 10.9%.

Service Corp: Headquartered in Houston, Service Corp is the largest provider of death care products and services in the U.S. The company's vast real estate assets cannot be replicated because of the difficulty permitting cemeteries. Management not only has delivered strong operating results, but has a record of generating high returns through acquisitions and share repurchases. The market penalizes the stock because a decreased death rate is currently depressing

earnings. This challenge will fade with the wave of baby boomers moving into their later years. Estimated free cash flow for 2012 provides a 10.3% FCF yield.

Madison Square Garden: Based in New York, Madison Square Garden (MSG) owns one of the most valuable regional sports networks at a time when live sports content is increasingly important to traditional distributors. In addition, the company owns two of the best franchises in the NBA and NHL (Knicks and Rangers) and the iconic Madison Square Garden arena in which these teams play. The Dolan family controls the company, owns 20%, and has done a tremendous job building network value. The market is punishing the stock because the teams are generating no profits currently, and MSG's billion dollar arena renovation that will draw higher team revenues is depressing this year's earnings. The media network generates a valuable cash coupon, and comparable transactions imply a breakup value of the teams and arena over twice the stock's price. Additionally, programming contracts with huge revenues are being signed, causing the values of big-market NBA teams to explode. Because of the current renovation, 2012 FCF will be negative. Adjusted for the arena renovation, the FCF yield is 7.0%.

Small-Cap Fund FCF Yield Summary	%
Average FCF Yield[c]	4.3
Average Adjusted FCF Yield[c]	9.8
Russell 2000 Earnings Yield[b]	6.4

See footnote on page 6.

International Fund

Five Largest Holdings	%
Fairfax	8.4
ACS	7.0
Ferrovial	6.4
Philips	6.3
Carrefour	6.0

Fairfax: Based in Toronto, Fairfax is a holding company with an array of global insurance and reinsurance companies that constitute a significant emerging markets presence. The company has the underwriting capacity to significantly grow profits and float when insurance prices are attractive. The decentralized management culture has attracted high-caliber talent that has generated cheap float. Prem Watsa, the founder, a large owner, and a uniquely capable investor, has used these float assets to deliver stellar investment returns. The price is less than 70% of our conservative assessment of intrinsic value due to the market's dislike of the unpredictability of reported earnings (uncertain timing of insured events) and depressed insurance pricing over the last five years. Premiums have begun to increase, and Watsa is taking advantage of market volatility to produce large capital gains on investment assets. Using consensus 2012 EPS estimates, the free cash flow yield is 6.4%, but assuming a 15% ROE which the company historically has delivered, the yield is 13.7%.

ACS: Headquartered in Madrid, ACS is one of the world's largest global infrastructure engineering firms providing construction and management of utility networks, transportation systems, airports, waste facilities, and similar large projects. Through its own business and its stakes in Hochtief and Leighton, the company's unique capabilities and experience provide an advantage in pursuing large civil works projects. CEO Florentino Perez owns 13%, and other board members hold an additional 40%. The company sells for approximately half of our valuation because the market oversimplifies this as a Spanish business with optically high leverage. In addition, many question ACS' strategy around its 19% ownership of Iberdrola, Spain's #1 utility and the largest owner of renewable assets in the world. In fact, less than half of ACS' direct operating exposure is to Spain, and most is outside of Europe when looking through their 50% ownership of Hochtief. The debt, which financed the stakes in Iberdrola and Hochtief, is extended through 2015, and, importantly, is non-recourse to ACS. A recent court victory gives ACS increased rights at Iberdrola, making it easier to pursue a significant and profitable investment outcome. Over the next few years without any Spanish or European economic recovery, ACS should generate a stable earnings coupon from its long-dated concession contracts, build construction projects around the world, and monetize assets when buyers are willing to pay fair prices for high-yielding infrastructure as they did in 2011 with some of ACS' wind, solar, and toll road assets. Although strapped municipalities have made the market bearish on infrastructure spending, projects that physically must be done will have to be private-public partnerships, aided by today's low interest rates. ACS is a world leader in privatized infrastructure projects. The company's current free cash flow yield based on expected 2012 FCF is 16.8%, and if adjusted for sold assets and assets held for sale, is over 30%.

Ferrovial: Based in Madrid, Ferrovial owns two of the best infrastructure assets in the world: London's Heathrow Airport (through BAA) and the ETR-407 toll road in Toronto. These assets are superior because of the long-term concession agreements in place and their pricing power (tariffs in the U.K. are raised at RPI + 7%, and in Canada toll tariffs have risen an average of over 10% per year for the past eleven years). Rafael del Pino's family founded the company, owns 45%, and has been an opportunistic value builder. Within the last two years, they sold 10% of the 407 and 6% of BAA at substantial premiums to our value and the stock's market multiple. We bought Ferrovial at less than 60% of our

appraisal in 2011 as others focused on what looks like a levered Spanish construction company at first glance. The debt is 100% non-recourse held against the concession assets, and they have net cash at the holding company. Over 80% of assets are outside Spain and the Eurozone. Asset values should continue to grow with increasing transportation demand and the pricing allowances. Additionally, BAA will start paying dividends to Ferrovial in 2012. Management is likely to continue to crystallize value through the sale of stakes in these core infrastructure properties as long as the market under prices them. The 2012 estimated free cash flow yield is 8.7% and adjusted for the cash, is 9.9%.

Philips: Based in Amsterdam, Philips is one of the three leading medical diagnostic and treatment device companies in the world and the leader in lighting. The company's consumer health products such as Norelco dry shavers and Sonicare toothbrushes are also dominant brands. Nearly 40% of revenues come from burgeoning emerging markets. When the new CEO and CFO, Frans van Houten and Ron Wirahadiraksa, took over in the second quarter of 2011, they immediately began to address bloated costs, set achievable 2013 targets for each segment, and announced a share buyback of €2bn, equal to 15% of the company. They also disposed of the challenged television division. The stock trades at 60% of our appraisal. Philips' profit misses under previous management have made analysts skeptical that the improvements implemented by our current partners will deliver results by 2013. These dominant worldwide businesses are growing, and the substantial repurchases at discounted prices are augmenting value-per-share accretion. The current free cash flow yield is 8.6% based on expected 2012 FCF which includes a number of one-time charges. Adjusting for those, the yield is 10.1%.

Carrefour: Headquartered in Paris, Carrefour is the number two retailer in the world with top food share in France, Spain, and Brazil. Over one third of cash flow comes from rapidly growing emerging markets including China. Blue Capital, a joint venture between Colony Capital and Europe's richest man, Bernard Arnault, holds three board seats and more than 20% of votes. Over the last fourteen months they successfully pursued selling both non-core geographies such as Thailand and owned real estate such as French supermarkets for multiples well above those implicit in the stock's price. In addition, the company successfully spun off Dia, its hard goods discount retailer. Dia is now listed on the Spanish stock exchange and a member of the IBEX 35. Carrefour's 60% price-to-value ratio reflects the market's assumption that margins and sales in France will stay at trough levels and ignores both the faster growing emerging market business and the significant worth of the company's real estate. Blue Capital is committed to capturing value recognition for Carrefour's dominant market share positions and valuable real estate. We believe they are likely to pursue additional high-return asset sales and to force adjustments needed to move French operating margins from current trough levels. Unlike most of our holdings which have positive momentum, the challenges for Carrefour in the very short term will get harder before they get easier. Premised on conservative 2012 free cash flow projections, the company's current FCF yield is 11.4%.

International Fund FCF Yield Summary	%
Average FCF Yield[(a)]	10.4
Average Adjusted FCF Yield[(a)]	15.5
EAFE Earnings Yield[(b)]	9.3

See footnote on page 6.

The Great Dichotomy

Never in our investing careers has the prospective return on corporate ownership so surpassed the return on long-term lending. Never has the risk of permanent capital loss from long-term lending been so great. Oft-discussed macro fears and the accompanying market volatility have driven investors from equities into the supposed security of U.S. government bonds and other highly rated sovereign and corporate debt. The January 5, 2012 *USA Today* headline, "Bonds Outperform Stocks over 30 Years," highlighted this flight and was reminiscent of the 1979 *Business Week* "Death of Equities" headline that preceded the high stock returns of the 1980s. Unlike the double-digit yields that 10-year Treasurys offered in the early eighties, today's below 2.0% government yields are meager competition for the S&P 500's earnings yield of 7.9%, the Russell 2000's 6.4%, and the EAFE's 9.3%. Moreover, and surprising to some, equities are even more attractive vis-à-vis bonds today than at the end of 2008, the worst economic downturn and bear market in our lifetime. Because of the large and unprecedented spreads between "safe" lending and business ownership yields shown above, we believe it is almost certain investors will begin swapping low or no return debt instruments for the much higher returns that high quality equities offer. According to the *Wall Street Journal* story on January 13th titled "China Reserve Changes Weighed," China has begun to reconsider its approach to investing its $3.2 trillion in foreign-exchange reserves. The chairman of China's largest state-owned bank indicated that "China may invest more of its...reserves in stocks, enterprises, and other assets as it looks for ways to boost returns."

The Opportunity

As indicated in each Fund's summary table, our largest holdings' adjusted FCF yield, which represents how true business owners would calculate their current FCF yield ranges between 9.8% and 15.5%, and is growing and after-tax. Not only are the adjusted yields much more attractive than the earnings yields of the indices, but the quality of our businesses far surpasses that of a random collection of hundreds of companies. We own a select group of industry leaders with sustainable competitive advantages and vested CEO and board partners who are building shareholder value. The Funds are selling at or below a 60% P/V. We expect to deliver outsized, risk-adjusted returns as our business franchises continue to produce, grow, retain, and intelligently reinvest their FCF coupons, and the markets arbitrage our FCF yields and values to those offered by inferior companies and low-yielding debt securities.

When our analysts communicate in writing, in the absence of being able to raise our voices and pound the table to convey our convictions, we WRITE IN ALL CAPS. As we enter 2012, we want to express to you our belief that WE OWN SUPERIOR BUILDING BLOCKS THAT SHOULD GENERATE OUTSTANDING FUTURE INVESTMENT RETURNS.

Sincerely,

O. Mason Hawkins, CFA
Chairman & Chief Executive Officer
Southeastern Asset Management, Inc.

G. Staley Cates, CFA
President & Chief Investment Officer
Southeastern Asset Management, Inc.

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(a) *Unweighted average from five largest holdings.*

(b) *FactSet 2012 P/E estimates inverted to calculate yield.*

(c) *Unweighted average from five largest holdings, excluding TXI where replacement value is more relevant than 2012 FCF.*