HALF YEARLY INVESTOR REPORT

31 DECEMBER 2007

Magellan Global Fund

MAGELLAN ASSET MANAGEMENT LIMITED

Investment Managers Report

DEAR INVESTOR

I am delighted to write to you as an investor in the Magellan Global Fund for the six months ended 31 December 2007.

For the 6 months to 31 December 2007 the net Fund return was -4.0% after fees, compared with the market benchmark (MSCI World Index Net $A) of -3.15%. In our view, short-term performance statistics are largely irrelevant for an investor with any sensible investment horizon. For example, as at 31 January 2008, the performance of the Fund since inception was -5.67%, whereas the recent decline in world share markets has resulted in a decline in the market benchmark of -12.49% over the same period. We are neither disappointed with the performance statistics as at 31 December, nor are we excited by the relative outperformance one month later. We remain focused on assembling a portfolio of what we regard to be outstanding companies, and during times of market volatility, we are often provided with opportunities to buy these outstanding companies at lower valuations. We aim to purchase securities when we believe that the investment will deliver very satisfactory returns for our investors over a 3 to 5 year timeframe. We are far more interested where a company's share price is likely to be in 5 years time than where it may be in 6 or 12 months time.

As at 31 December 2007 the portfolio consisted of 20 investments and we maintained a high cash weighting of approximately 41%. The high cash weighting reflects our relatively measured approach in establishing the portfolio and our concerns regarding the likely implications of the global liquidity crisis which began to emerge last August. We only sold one position during the quarter, being an investment in Google Inc as it appreciated by approximately 25% from cost and passed our assessed valuation of the company.

PORTFOLIO SUMMARY

Magellan Global Fund - Top 10 Investments as at 31 December 2007	
American Express Company	6.8%
eBay Inc	6.2%
Yum Brands Inc	5.7%
Nestle	5.3%
Wal-Mart Stores Inc	4.9%
Tesco Plc	3.8%
Lowe's Co Inc	3.0%
Wells Fargo & Co	2.8%
Abercrombie & Fitch Co	2.6%
Harley Davidson Inc	2.6%

Our investments in the Financial Services Sector: American Express and Wells Fargo; and our investments which are most susceptible to US discretionary expenditure, Lowe's and Harley Davidson produced negative share price returns over the period. The remaining Top 10 investments produced positive returns over the period.

In hindsight it would be a fair question for you to ask: "Wasn't it obvious that financials and US discretionary stocks would underperform with the unfolding credit crisis and slow down in the US economy?" Unfortunately we do not possess a perfectly clear "crystal ball" and we purchased each of these investments prior to the real emergence of the mortgage crisis in the US. Since August we have been more cautious on the short term outlook for US discretionary spending and the financial services sector in general. Notwithstanding the short term negative share price movements, there has been no material change to our assessment of the underlying intrinsic values of these companies and we believe each of these investments will deliver very satisfactory returns over a 3 to 5 year period.

In the short term the stock market predominately reacts to the most recent information, both positive and negative, which can lead to large fluctuations in share prices often unrelated to the underlying value of a business. In the long term the share price should broadly track the underlying intrinsic value of a business. This is what Benjamin Graham was referring to when he famously said "In the short term the market is a voting machine and in the long term it is a weighing machine".

We think in a similar method to Mr Graham, thus it is crucial in our view to focus on the underlying intrinsic value of a company in assessing the likely returns from an investment over a 3 to 5 year investment horizon. We also believe that it is easier to estimate with reasonable accuracy the underlying intrinsic value of an outstanding business than a lower quality or more speculative investment. This does not mean that we ignore short term issues in making purchase decisions, as evidenced by our decision to maintain a high cash weighting at the present time.

A number of people have commented that the Fund's investment portfolio is too concentrated in the United States. It is important to appreciate that we are not seeking to create a balanced portfolio with investments in all major markets around the world. Contrary to many, we do not view the sector and country composition of the Benchmark as an appropriate starting point when constructing the portfolio. The Benchmark can, at times, be a very risky place to be - (for example, leading up to the technology crash of 2000, the index portfolio had over 30% in technology and telecommunication stocks). Our investment philosophy is to hold a concentrated portfolio (25 to 50 securities) of outstanding companies and to purchase investments when we believe they will deliver very satisfactory returns over a 3 to 5 year period. More importantly, we do have regard to "factor diversification" and closely monitor how much of the portfolio is exposed to correlated economic factors, such as a recession in the United States. The fact is the vast majority of the world's most outstanding companies are domiciled in OECD countries and many of these are domiciled in the United States. It is therefore very unlikely that the Fund will hold a meaningful part of the portfolio in companies domiciled in non-OECD countries or emerging markets. Until very recently, our analysis indicated there were more compelling opportunities to invest in outstanding companies domiciled in the United States than outstanding companies domiciled outside the United States. Since 31 December the Fund has made additional investments in European domiciled companies, as share prices became more attractive.

MARKET COMMENTARY

There has been much market commentary on the US sub-prime mortgage crisis, the global credit crisis and the possibility that the United States will fall into recession in 2008. Whilst we don't focus specifically on macro global influences to drive our portfolio management activity, we do believe that the global credit crisis is probably the most serious issue that has arisen in financial markets in the past 20 years. The global credit crisis virtually froze the short term inter bank funding market and the asset backed securitisation markets. Whilst there has been some stabilisation in the inter bank funding market, primarily driven by massive injections of liquidity by central banks around the world, the asset backed securitisation markets have not yet stabilised. The credit crisis is likely to result in a re-pricing of risks (i.e. an increase in spreads) for the near future. In our view liquidity will remain materially tighter then it has been over the past few years as it is unlikely that investors will quickly return to certain funding markets (such as off balance sheet bank funding vehicles (conduits and SIVs), collateralized debt obligations (CDOs) and highly structured securitised debt). We do have confidence that investor appetite will more quickly return for more traditional asset backed securities (e.g. for prime mortgages, credit cards, auto loans and student loans) and to the short term commercial paper market for investment grade corporate and well capitalised financial institutions. There are still some unresolved issues (such as the recapitalisation of the monoline bond insurers to retain their AAA credit ratings) and unknown issues (such as major unreported losses by hedge funds and other non-bank financial institutions) which could cause major disruptions to financial markets in the short term. We therefore retain a cautious view in the short term. Whilst we remain cautious, the market volatility is presenting some opportunities to purchase outstanding companies at very attractive prices compared with our view of the underlying values of the business. Whilst it is unlikely that these values will be reflected in share prices in the short term, we believe that investors that are willing to take a 3 to 5 year view will be rewarded.

KEY STOCK IN FOCUS

AMERICAN EXPRESS

As the largest investment in the portfolio we believe it is appropriate to briefly outline our investment case for American Express. It is even more pertinent given that as at 31 December 2007, market value (in US dollars) of our holding in American Express was approximately 11% below our average cost.

American Express is one of only three major global credit payments networks (together with Mastercard and Visa). It operates the only global closed loop credit card network where it issues cards (both charge and credit cards), processes transactions across the network and acts as the acquiring bank for merchants around the world. This enables American Express to capture the entire value chain.

In our view there are three fundamental drivers of American Express' business:

- Growth in cards on issue – American Express has approximately 86 million cards on issue which have been growing at approximately 10% per annum. We believe that recent developments (such as winning the court case against Visa and Mastercard which has enabled partner banks in the United States to issue co-branded American Express cards for the first time) and the secular trend around the world from cash and cheques to other payment methods are very positive for American Express. Most pertinently, cheques are still used for 41% of payments in the United States, significantly above other developed countires. This is expected to decline significantly over the next five years in favour of cards and electronic transactions, with American Express a major beneficiary. With these factors in mind, we believe American Express will continue to be able to grow its cards on issue at high single digit rates for the foreseeable future.

- Growth in spending per customer – due to its business model (which American Express describes as "spend centric") it has the highest spending customers with an average annual spend per proprietary card of approximately US$12,100 which has grown at around 10% per annum over the past five years. By way of comparison the average annual spending on a Mastercard (excluding debit cards) is approximately US$2,400 per card. We believe that American Express will continue to be able to grow its spending per card, due to its very attractive rewards programme and its increasing penetration with merchants around the world.

- Average discount rate – the discount rate is the fees it charges to merchants for transactions processed by American Express. The discount rate is currently running at around 2.55% of each dollar transacted. We believe that the discount rate will fall very modestly over time as American Express increases its penetration into large volume retailers which are able to extract better terms with American Express than smaller volume retailers. The reduction in the discount rate over time will be as a result of a change in business mix rather than any reduction in American Express' pricing power. We believe that the moderation to the discount rate will be more than offset by the growth in spending per customer and merchant penetration.

The most often cited criticism of American Express is that its credit card lending business is an inherently risky business. While the credit card lending business does increase short term earnings volatility, due to the need to provide for credit losses which vary through the economic cycle, we believe that American Express' credit card lending business is a very attractive business from an economic perspective as it generates returns on capital materially above the cost of capital through the full economic cycle. American Express' credit lending business is one of the more attractive lending businesses you would want to invest in. In the short term, the stock market usually reacts negatively to any increase in credit provisions, notwithstanding that an increase in periodic credit provisions usually does not have any impact on the long term intrinsic value of the company. As a long term investor it is important that you factor in long term average loss rates when valuing American Express and not be overly influenced by prevailing high or low credit loss levels. The recent increase in credit loss provisions by American Express were (at least) factored in by us in valuing American Express and have had no impact on our view of the underlying value of the Company.

American Express has established long term performance targets to grow revenues at 8% pa, EPS at 12% to 15% pa and to generate return on equity in the range of 33% to 36%. We believe that there are very few major companies in the world that could realistically set such lofty long term financial targets. In the case of American Express we firmly believe that these long term targets are achievable.

Yours sincerely,

Hamish M Douglass
Portfolio Manager
Magellan Global Fund
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