



**Third Avenue Value Fund**

**Third Avenue Small-Cap Value Fund**

**Third Avenue Real Estate Value Fund**

**Third Avenue International Value Fund**

**LETTERS TO OUR SHAREHOLDERS**

First Quarter Commentary

January 31, 2008

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If you should have any questions, please call 1-800-443-1021, or visit our web site at: [www.thirdavenuefunds.com](http://www.thirdavenuefunds.com), for most recent month-end performance data or a copy of our prospectus. Current performance results may be lower or higher than performance numbers quoted in certain letters to shareholders.

M.J. Whitman LLC, Distributor. Date of first use March 3, 2008.



## Third Avenue Value Fund



**MARTIN J. WHITMAN**  
Co-CHIEF INVESTMENT OFFICER  
& PORTFOLIO MANAGER OF  
THIRD AVENUE VALUE FUND

Dear Fellow Shareholders:

At January 31, 2008, the unaudited net asset value attributed to the 182,418,451 shares outstanding of the Third Avenue Value Fund ("TAVF", "Third Avenue", or the "Fund") was \$57.04 per share. This compares with an audited net asset value of \$65.95 per share at October 31, 2007; and an unaudited net asset value of \$58.91 per share at January 31, 2007, both adjusted for a subsequent distribution to shareholders. At February 28, 2008, the unaudited net asset value was \$56.83 per share.

Quarterly performance for the most recent three month interim was one of the worst fiscal quarter return for the Fund since it started investing in late 1990. Security prices collapsed in Hong Kong and Japan. In the U.S., common stock prices also collapsed for companies involved in real estate, mortgage insurance, and bond insurance. I am confident that the common stocks owned by Third Avenue are issues of companies which are well financed, well managed, and are selling at prices that represent huge discounts from private business values or take-over prices. The Fund expanded its positions in these issues relatively aggressively during the quarter.

### QUARTERLY ACTIVITY

Principal activities during the quarter were as follows:

#### Principal Amount or Number of Shares

\$197,000,000

\$67,348,000

340,000 shares

14,030 shares

136,927 shares

137,157 shares

943,760 shares

1,999,959 shares

1,000,000 shares

1,669,227 shares

5,743,738 shares

1,000,000 shares

5,461,514 shares

1,000,000 shares

1,000,000 shares

#### New Positions Acquired

MBIA Insurance Corp. 14% Surplus Notes ("MBIA Surplus Notes")

Standard Pacific Senior Unsecured Bonds ("Standard Pacific Unsecureds")

Brookfield Infrastructure Partners, LP ("Brookfield Infrastructure Common")

#### Positions Increased

Colonial Bankshares Inc. Common Stock ("Colonial Common")

Fedfirst Financial Corp. Common Stock ("Fedfirst Financial Common")

Home Federal Bancorp Inc. Common Stock ("Home Federal Common")

Alliance Data Systems Common Stock ("Alliance Common")

Ambac Financial Corp. Common Stock ("Ambac Common")

CIT Group Common Stock ("CIT Common")

Forest City Enterprise Class A Common Stock ("Forest City Common")

Henderson Land Development Common Stock ("Henderson Common")

Legg Mason Common Stock ("Legg Mason Common")

MBIA Inc. Common Stock ("MBIA Common")

MGIC Investment Corp. Common Stock ("MGIC Common")

Mitsubishi Estate Common Stock ("Mitsubishi Common")

\* Portfolio holdings are subject to change without notice. The following is a list of Third Avenue Value Fund's 10 largest issuers, and the percentage of the total net assets each represented, as of January 31, 2008: Henderson Land Development Co., Ltd., 9.88%; Cheung Kong Holdings, 8.39%; Toyota Industries Corp., 6.52%; Posco (ADR), 4.36%; Forest City Enterprises, 3.32%; Brookfield Asset Management, 3.10%; Nabors Industries, Ltd., 2.64%; The St. Joe Company, 2.64%; Wheelock & Co., Ltd., 2.56%; and Wharf Holdings, Ltd., 2.50%.



Number of Shares	Positions Increased (continued)	Principal Amount or Number of Shares	Positions Eliminated
1,819,000 shares	Mitsui Fudosan Common Stock ("Mitsui Fudosan Common")	87,035 shares	ACE Ltd. Common Stock ("ACE Common")
660,200 shares	Power Corp. of Canada Common Stock ("Power Corp. Common")	726,718 shares	Ceridian Corp. Common Stock ("Ceridian Common")
290,200 shares	Radian Group Common Stock ("Radian Common")	15,675 warrants	ESG Re Ltd. Warrants ("ESG Warrants")
460,090 shares	St. Joe Common Stock ("St. Joe Common")	\$33,400,000	Hechinger Co. Bonds ("Hechinger Bonds")
3,000,250 shares	Tellabs, Inc. Common Stock ("Tellabs Common")	65,000 shares	Helicon Re Holding Ltd. Common Stock ("Helicon Common")
1,454,200 shares	Toyota Industries Common Stock ("Toyota Industries Common")	\$10,000,000	Mirant America's Generation Bonds ("Mirant American Bonds")
189,400 shares	USG Corp. Common Stock ("USG Common")	2,489,900 shares	Nuveen Investments Common Stock ("Nuveen Common")
5,402,822 shares	Wharf Holdings Common Stock ("Wharf Common")	598,000 shares	PAREXEL International Corp. Common Stock ("PAREXEL Common")
	<b>Positions Reduced</b>	2,000,000 shares	Pfizer Inc. Common Stock ("Pfizer Common")
110,000 shares	Aioi Insurance Common Stock ("Aioi Common")	206,627 shares	Sears Holding Corp. Common Stock ("Sears Common")
49,741 shares	Alico Common Stock ("Alico Common")	363,000 shares	St. Jude Medical Inc. Common Stock ("St. Jude Common")
197,000 shares	Chong Hing Bank Common Stock ("Chong Hing Common")	16,354 shares	Toronto-Dominion Bank Common Stock ("Toronto-Dominion Common")
11,263 shares	Consolidated-Tomoka Land Common Stock ("Consolidated – Tomoka Common")	None of the securities sold were issues which seemed to be grossly overpriced. Rather, the reasons for the sales were two-fold. First, given the very attractive pricing, it seemed prudent to expand the Fund's representation in core areas: U.S. real estate; Japanese real estate; Hong Kong real estate and private equity, where the businesses also have a major presence in Mainland China; and well-capitalized companies suffering through the U.S. housing melt-down. Second, in times of poor, relative performance, Third Avenue seems vulnerable to large scale redemptions. For example, in 1998 and 1999 when the Fund was not participating in the Dot-Com Bubble, the TAVF share count went from around 56 million shares outstanding to 38 million shares outstanding. Fund management is much easier when TAVF has a cash cushion. At January 31st, cash and cash equivalents account for about 9.4% of net assets. This does not account for the 1.8% of net assets that	
46,429 shares	Haynes International Common Stock ("Haynes Common")		
30,000 shares	Millea Holdings ADR ("Millea ADR")		
129,000 shares	Mitsui Sumitomo Insurance Common Stock ("Mitsui Sumitomo Common")		
240,022 shares	Phoenix Companies Common Stock ("Phoenix Common")		
110,000 shares	Sompo Japan Insurance Common Stock ("Sompo Japan Common")		
67,770 shares	Stewart Information Services Common Stock ("Stewart Common")		
12,847 shares	Tompkin Financial Corp. Common Stock ("Tompkin Common")		



were invested in MBIA Surplus Notes at a yield to call of slightly over 14% per annum. The MBIA Surplus Notes appear to carry very small, or non-existent, credit risk, and thus are considered by management to be a near-cash investment (albeit the MBIA Surplus Notes, unlike cash equivalents, are subject to market price fluctuations).

The Standard Pacific Unsecureds were acquired at around a 17.5% yield to maturity. The odds seem to favor rather strongly that the instruments remain performing loans. If not, Standard Pacific, a leading home builder, would have to reorganize in Chapter 11. In that event, the Fund believes it holds the fulcrum security and would probably become a significant stockholder of a well-capitalized home builder.

Brookfield Infrastructure Common is a Brookfield Asset Management spin-off.

Alliance remains in discussions with subsidiaries of the Blackstone Group about a cash out merger for Alliance Common. It is dicey as to whether, or not, there will be a transaction. At current prices, Alliance Common seems a reasonable value whether, or not, there is a transaction.

During the quarter, the Fund was able to expand materially its interests in companies holding high quality real estate at what appear to be very attractive prices. Most of the real estate consists of Class A office properties in Hong Kong, Japan and the USA, as well as large land banks in Mainland China. A small proportion of the real estate investments went into Florida land development. Issues acquired encompass Forest City Common, Henderson Common, Mitsubishi Common, Mitsui Fudosan Common, St. Joe Common and Wharf Common.

Third Avenue also increased its presence in investment management by expanding its positions in Legg Mason

Common and Power Corp. Common. Both issues seem to be selling at meaningful discounts from readily ascertainable Net Asset Values ("NAVs").

Third Avenue also acquired additional common shares of a mélange of strongly-capitalized companies in telecommunications equipment, auto supply and building products, i.e., Tellabs Common, Toyota Industries Common and USG Common.

The common stocks of all companies affected directly or indirectly with the current mortgage meltdown cratered in price during the quarter. One, CIT Common, became available at a modest discount from tangible book value;

while others, Ambac Common, MBIA Common, MGIC Common and Radian Common, have been selling at discounts of around 70% from tangible book value, or NAV. In Management's opinion, there is much profit to be made in these issues at these prices whether the companies continue as going concerns, or enter into a period when the companies run-off their books

of business in whole, or in part, as we wrote to you last quarter. Management classifies these investments as "distress investments", where the Fund tries to acquire meaningful positions in the most senior issue which will participate in a reorganization, i.e., the fulcrum security. In prior distress investing for the Fund, the fulcrum security had always been a debt instrument. In these cases, however, the fulcrum security is the common stock.

#### **MBIA REVISITED**

On February 11th, TAVF acquired from MBIA, 10,610,425 shares of MBIA Common at \$12.15 per share. This brought the Fund's holding to 23,148,845 shares of MBIA Common, or about 10% of the issue outstanding. Previously, Third Avenue also had acquired

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\$197,000,000 of 14% Surplus Notes issued by an MBIA insurance subsidiary. Since December 2007, MBIA has raised about \$2.6 billion of new capital, of which TAVF has supplied almost \$326,000,000.

MBIA is now strongly capitalized. It ought to qualify easily for an AAA rating with a \$17 billion claims paying ability. If so qualified, MBIA would be in a position to underwrite a large amount of profitable new business.

However, there seem to be three impediments tangential to capitalization that might prevent MBIA from receiving a credit rating of AAA-Stable.

- 1) The Credit Rating Agencies could be arbitrary and capricious, denying AAA ratings for highly subjective, qualitative reasons such as a supposed severe decline in “franchise value”.
- 2) MBIA is New York State domiciled with its principal insurance subsidiaries regulated by the State Insurance Department (“SID”) and is therefore subject to regulatory risk. The state leadership including the Governor of New York, Elliott Spitzer, appears not to fully appreciate the financial strength of issuers such as MBIA, and furthermore, MBIA’s utter lack of need for a “Bailout” or a “Rescue”.
- 3) As has been well reported by the financial media, MBIA is being victimized by an apparently well-organized bear raid headed by William Ackman (“Ackman”) of Pershing Square Capital Management. While the bear raiders have been helpful to Third Avenue, in making it easier to acquire MBIA Common at depressed prices, the bear raiders might have the ability to adversely affect the going concern attributes of MBIA, given the possible capriciousness of Rating Agencies and regulators.

Ackman recently laid out his views in two publications, “How to Save the Bond Insurers”, dated November 28, 2007, and “Bond Insurers Transparency: Open Source Research”, dated January 30, 2008. He also published “Is MBIA Triple A?”, in 2002.

While he is an articulate advocate, Ackman’s arguments are off base. This all can be laid out in three points.

- 1) **Ackman does not seem to understand the Property and Casualty (“P&C”) Insurance business and its sources of profitability.** Ackman believes that the Bond Insurer Model does not work because the insureds are able to buy an AAA credit rating so cheaply.

The facts are that Bond Insurance is one of the more profitable P&C businesses. Profitability for P&C’s are primarily a function of two factors: Underwriting Profit (or loss), as measured by the Combined Ratio; Underwriting expenses and loss expenses, as a percentage of Premiums Written and Premiums Earned. Historically, the MBIA combined ratio has ranged between 30%-40% (underwriting profit 60% to 70%). Looking past the current structured finance debacle, MBIA seems to have a pretty good shot at returning to old combined ratios, especially if some of the weaker bond insurers have to exit the industry and MBIA does not. The second element of P&C profitability is net investment income; i.e., essentially investing in performing loans. In part, net investment income is a function of how much time elapses between when an insurance premium is received and when a claim is paid to an insured. Insofar as the period is far distant, the liability is said to be “long-tail”. P&C companies with “long-tail” liabilities have the ability to generate large net investment income as cash balances are invested in performing loans. MBIA liabilities are quite long-tail. At present, MBIA enjoys an adjusted book value of around \$38 - \$40 per share. After the crisis passes, it seems reasonable to suppose that MBIA might be able to earn annually a return of, say, 10% to 12%, on adjusted book value.

- 2) **The use and limitation of Generally Accepted Accounting Principles (“GAAP”) in the analysis of investment portfolios or insurance books of business.** The publications argue that prices, as



determined by marks to market, or mark to model, always deserve 100% weight. This is arrant nonsense. Market prices do deserve dominant weight in an analysis where the portfolio consists wholly of common stocks and non-performing loans held in trading accounts. Market prices deserve little or no weight, when the portfolio consists of performing loans, and in force policies, to be held to maturity. FASB 133 requires marks to market and marks to model, in accounting for derivatives under GAAP, and changes in market are reflected in the reported income account. FASB 133 is pretty much irrelevant for MBIA – a buy-and-hold investor in performing instruments. Paul Samuelson, the Nobel Laureate economist, had it about right for most markets when he said, “the market has correctly predicted nine of the last five recessions.” MBIA’s losses will be determined not by market prices but, rather, by what percent of obligations default and how these defaults are worked out.

- 3) **The publications pay little attention to the rules of seniority and priority of payment in evaluating, or understanding, senior tranches of debt.** The argument that if an entity is in trouble, every liability on the balance sheet of that entity is also in trouble is strictly “amateur hour”. Frequently, senior issues sail through troubles unscathed. (Remember Third Avenue’s investments in Pacific Gas & Electric First Mortgages a few years back). A simple model of a Residential Mortgage Backed Security (“RMBS”) ought to suffice:

**RMBS – Original Balance Sheet**

**ASSETS**

Sub Prime Loans	\$1,000	Senior Tranches	\$ 600
		Junior Tranches	\$ 400
	<u>\$1,000</u>		<u>\$1,000</u>

Assume 30% of the Sub Prime Loans default. Recoveries on defaulted loans are 50%.

**RMBS – Reconstructed Balance Sheet**

Performing Sub Prime Loans	\$700	Senior Tranche	\$600
Present Value of			
Defaulted Loans	\$150	Junior Tranche	\$250
	<u>\$850</u>		<u>\$850</u>
Loss for Senior Tranche	0%		
Loss for Junior Tranche	37.5%		

With the exception of Home Equity Lines of Credit (“HELOCs”) and Closed-end Second Liens (“Closed-End Seconds”), virtually all of MBIA’s structured debt portfolio appears to be in senior tranches and super senior tranches. Losses are likely to be small, especially against the background that MBIA has \$17 billion of claims paying ability and that the gross cash flows from MBIA’s operations, even if the company writes little new business, should exceed \$1.3 billion per year through 2016 made up of net investment income, installment premiums, upfront premiums and investment management revenue.

Over the past several months, there have been a number of other charges that seem designed to influence a bear market raid. These other charges include: “MBIA parent might file for Chapter 11 relief by the second quarter of 2008”; “MBIA is writing certain policies illegally”; and “MBIA will not be able to clear a 1933 Registration Statement with the Securities and Exchange Commission”. C’mon!

In recent months, there have been draconian-type statements from the media about the need to arrange bailouts and rescues for the Bond Insurers, in general, and MBIA, in particular. This concern seems grossly misplaced. Neither MBIA nor Ambac seem to need bailouts, since in each instance the companies seem to have more than ample resources to meet any contractual requirements to policy holders. Rather, it is other financial institutions that hold insured obligations who need the bailout or rescue, if they are to avoid massive accounting charges against their income accounts and balance sheets, insofar as Bond Insurers are downgraded from AAA.





With a capital infusion of \$2.6 billion, there seems to be a good chance that 2008 will be a quite profitable year for MBIA from ongoing operations. This could occur if the Rating Agencies were to rate MBIA Corp. AAA-Stable while downgrading competition – Ambac, FGIC and Security Capital Assurance, who have not had capital infusions. There seems to be very good demand for AAA wraps at very good prices.

MBIA has made mistakes. The Company will take losses that seem easily met out of MBIA's approximately \$17 billion claims paying ability. Of particular concern are about \$10.5 billion principal amount of Closed-End Seconds and around \$11.0 billion of HELOCs. At this writing, MBIA has reserves for losses on its balance sheet of \$1.35 billion, of which \$813 million relate to the company's Closed-End Seconds and HELOC exposure (\$613 million in case reserves and \$200 million in unallocated reserves). MBIA management, and its auditors, think the reserves are sufficient to meet expected losses, but no one can know for sure. Reserve adequacy will be determined by future unpredictable events. The base case seems to be that losses will not be so great as to jeopardize MBIA's AAA rating. But even if MBIA is downgraded, the common stock, at current prices of around \$13 to \$14 per share, ought to fare reasonably well, even in a run off scenario. Adjusted book value currently is probably in a range of \$38 - \$40 per share.

Other than the Closed-End Seconds and HELOCs, the MBIA structured finance portfolio consists of \$131 billion of Collateralized Debt Obligations, \$43 billion of Mortgage Backed Residential and \$64 billion of Mortgage Backed Commercial Loans, Consumer Asset Backed Loans, and Corporate Asset Backed Loans. In all cases, MBIA was the equivalent of a senior lender. First losses on these structured finance vehicles ought to be absorbed by junior tranches or excess spread.

Governor Spitzer's apparent concern that municipalities will have to pay more to borrow if MBIA is downgraded is certainly misplaced. Municipalities, now seeking to borrow

or seeking to borrow in the future, will be able to acquire AAA wraps from many insurers, including new entrants.

Credit enhancement has been, and will remain, an important United States industry. Bond Insurers are likely to remain important credit enhancers. Others in the industry include private sector commercial banks which issue Letters of Credit; quasi-public enterprises, such as Fannie Mae and Freddie Mac, which insure qualified mortgages; and Federal, State and Local governments themselves.

One of the reasons for feeling comfortable with the MBIA investment is the relative "ease of exit" from the industry. If MBIA does not ultimately receive AAA-Stable Ratings, it will be hard to write profitable new business. At these prices, however, TAVF ought to fare reasonably well with its MBIA investment even if the insurance subsidiaries shrink as the business enters into a gradual run-off.

Obviously, I feel good about TAVF's investment in MBIA. The Fund ought to do well under almost any scenario. By any objective standard, the MBIA investments are attractive ones with the insurance subsidiaries deserving of an AAA-Stable rating. Yet, there exists a sense of discomfort due to the dangers of Rating Agency subjective considerations and capricious regulators.

I shall write you again when the semi-annual report for the period to end April 30, 2008 is published.

Sincerely yours,

Martin J. Whitman  
Chairman of the Board





## Third Avenue Small-Cap Value Fund



**CURTIS R. JENSEN**  
Co-CHIEF INVESTMENT OFFICER &  
PORTFOLIO MANAGER OF THIRD AVENUE  
SMALL-CAP VALUE FUND

Dear Fellow Shareholders:

At January 31, 2008, the end of the Fund's fiscal first quarter, the unaudited net asset value attributable to the 83,447,670 common shares outstanding of the Third Avenue Small-Cap Value Fund ("Small-Cap Value" or the "Fund") was \$22.67 per share, compared with the Fund's audited net asset value of \$24.94 per share at October 31, 2007, adjusted for a subsequent distribution, and an unaudited net asset value at January 31, 2007 of \$23.45 per share. At February 28, 2008, the unaudited net asset value was \$22.86 per share.

### QUARTERLY ACTIVITY

During the quarter, Small-Cap Value added five new securities to the portfolio, increased to 20 of its 72 existing positions, eliminated eight positions and reduced its holdings in 10 companies. At January 31, 2008, Small-Cap Value held positions in 71 common stocks, the top 10 positions of which accounted for approximately 29% of the Fund's net assets.

### Principal Amount or Number of Shares

71,478 shares

677,911 shares

900,965 shares

1,047,848 shares

\$18,500,000

196,497 shares

59,150 shares

16,900 shares

1,329,686 shares

327,630 shares

1,109,195 shares

2,407 shares

444,270 shares

768,947 shares

21,418 shares

558,000 shares

### New Positions Acquired

Brookfield Infrastructure Partners, L.P.  
("Infrastructure Partners Units")  
Genesee & Wyoming Inc. Common  
Stock ("Genesee Common")  
Imation Corp. Common Stock  
("Imation Common")  
Lanxess AG Common Stock  
("Lanxess Common")  
MBIA Insurance Corp. Surplus Notes  
("MBIA Notes")

### Positions Increased

Alexander & Baldwin, Inc. Common  
Stock ("Alex Common")  
Bel Fuse Inc. Class B Common Stock  
("Bel Fuse Common")  
Bronco Drilling Co. Inc. Common Stock  
("Bronco Common")  
Cross Country Healthcare Inc.  
Common Stock  
("Cross Country Common")  
Electronics for Imaging, Inc. Common  
Stock ("Imaging Common")  
Encore Wire Corp., Common Stock  
("Wire Common")  
Herley Industries, Inc. Common Stock  
("Herley Common")  
K-Swiss, Inc. Class A Common Stock  
("K-Swiss Common")  
Lexmark International, Inc. Common  
Stock ("Lexmark Common")  
National Western Life Insurance Co.  
Class A Common Stock  
("Western Common")  
Parco Company Ltd. Common Stock  
("Parco Common")

\* Portfolio holdings are subject to change without notice. The following is a list of Third Avenue Small-Cap Value Fund's 10 largest issuers, and the percentage of the total net assets each represented, as of January 31, 2008: Sapporo Holdings, Ltd., 4.31%; Brookfield Asset Management, 3.59%; Westlake Chemical Corp., 3.08%; Parco Co., Ltd., 3.05%; St. Mary Land and Exploration Co., 3.05%; Cimarex Energy Co., 2.64%; Fording Canadian Coal Trust, 2.50%; Lexmark International, Inc., 2.49%; Saskatchewan Wheat Pool, 2.34%; and Alexander & Baldwin Inc., 2.30%.



<b>Number of Shares</b>	<b>Positions Increased (continued)</b>	<b>Principal Amount or Number of Shares</b>	<b>Positions Eliminated</b>
538,433 shares	Pioneer Drilling Co. Common Stock ("Pioneer Common")	286,100 shares	Agrium, Inc. Common Stock ("Agrium Common")
16,643,370 shares	PYI Corp. Ltd. Common Stock ("PYI Corp. Common")	308,400 shares	Ceridian Corp. Common Stock ("Ceridian Common")
28,946 shares	Sybase, Inc. Common Stock ("Sybase Common")	535,800 shares	CNX Gas Corp. Common Stock ("CNX Common")
100,000 shares	Synopsys, Inc. Common Stock ("Synopsys Common")	1,661,873 shares	Comstock Resources, Inc. Common Stock ("Comstock Common")
2,974,227 shares	Tellabs, Inc. Common Stock ("Tellabs Common")	65,000 shares	Helicon Reinsurance Ltd., Common Stock ("Helicon Common")
400,100 shares	Tidewater, Inc. Common Stock ("Tidewater Common")	\$4,942,604	Insilco Technologies Bank Debt ("Insilco Debt")
50,000 shares	Trinity Industries, Inc. Common Stock ("Trinity Common")	283,843 shares	Nuveen Investments Common Stock ("Nuveen Common")
50,000 shares	Vail Resorts, Inc. Common Stock ("Vail Common")	1,541,017 shares	Pogo Producing Co. Common Stock ("Pogo Common")
1,312,637 shares	Westlake Chemical Corp. Common Stock ("Westlake Common")		
	<b>Positions Reduced</b>		
42,445 shares	Alamo Group, Inc. Common Stock ("Alamo Common")		
676,925 shares	ASV, Inc. Common Stock ("ASV Common")		
767,585 shares	Canfor Pulp Income Fund Units ("Pulp Units")		
855,446 shares	Cimarex Energy Co. Common Stock ("Cimarex Common")		
500 shares	FBL Financial Group, Inc. Common Stock ("FBL Common")		
8,324 shares	GSI Group, Inc. Common Stock ("GSI Common")		
773,900 shares	Ingram Micro Inc. Common Stock ("Ingram Common")		
59,550 shares	The St. Joe Company Common Stock ("Joe Common")		
166,000 shares	St. Mary Land and Exploration Co., Common Stock ("St. Mary Common")		
439,603 shares	Whiting Petroleum Co. Common Stock ("Whiting Common")		

#### **QUARTERLY ACTIVITY**

I have stated on many occasions that investors ought to view periodic market volatility more as a friend than as a measure of risk, as it allows those with a long-term focus, like Third Avenue, to buy when prices are cheap and to sell when they are dear. While we do not equate activity with progress, the most recent period came with its fair share of volatility, providing ample opportunities on both ends of the buy-sell spectrum. Of note this quarter, Fund management added significantly to the Fund's existing holdings, initiated a number of new positions and disposed of a few positions largely in connection with merger and acquisition activity.

Two of the Fund's newest holdings, Lanxess Common and Imation Common, share a common lineage in that both companies fall into the family of restructurings. The transformations have been accompanied by a fair degree of "noise" in the reported GAAP numbers in recent quarters – noise that has undoubtedly deterred many investors. As importantly, both firms are perceived – inappropriately in our minds – as "commodity" companies with little, or no, growth prospects. Such



factors attract us because most investors shun stocks like these that don't "screen" well, whose underlying businesses might be perceived as low growth, or whose prices are falling.

We became interested in Lanxess AG, a global chemicals group with headquarters in Germany, after hearing management speak at a conference in early 2007. Spun out of Bayer AG in early 2005, the company is a leading player in a majority of its markets, most of which are concentrated among a few suppliers. Lanxess operates in four primary segments, including: i) performance rubber, used in everything from truck tires to chewing gum; ii) engineering plastics with applications in autos, paper and packaging, electronics and medical technology; iii) chemical intermediates found in pharmaceuticals, agrochemicals, colorants, plastics and other fine chemicals; and iv) performance chemicals with uses in the leather, rubber, plastics and food and beverages industries, and in water treatment. Management has made steady progress toward improving the company's profitability through cost-cutting initiatives, more disciplined pricing strategies, and portfolio realignments (e.g., dispositions of underperforming assets). The improved profitability, which has more room for expansion, has resulted in a strong financial position, one that not only will protect the business during a downturn, but also easily lends itself to internal expansion, further acquisitions and share repurchases. Lanxess shares, which have declined 25% *in 2008*, were acquired at modest multiples of current cash flow and earnings and at a deep discount to a conservative break-up value of the company's highly separable and saleable assets.

Imation develops, manufactures and markets removable data storage media products with applications in both commercial enterprises, as well as for individual consumers. The company's products allow customers to store, edit, and manage data, photos, video, images and music. Imation boasts the leading market share in each of the magnetic tape and

recordable optical storage markets, mature business lines whose substantial cash flow is being used to transition the company to higher growth, consumer-oriented markets – no doubt you have seen some of the company's consumer products during a visit to the local Staples or Target. During 2006-2007, Imation acquired both the TDK and Memorex recording media businesses, with TDK Corporation taking an initial 17% ownership stake and a Board seat. Importantly, these acquisitions were completed on what appear to be sensible, economically attractive terms; add meaningful consolidation to the respective markets; and leave the company's balance sheet with more than \$100 million of cash, net of debt (versus a current market capitalization of \$1 billion). Operationally, Imation management, under new leadership, has embarked on a cost cutting drive with respect to both the company's manufacturing and R&D divisions. Having cut the share price in half during the past 12 months, Mr. Market seems to believe that Imation's transition toward a leaner, branded consumer products company is doomed to fail. TDK, like us, evidently disagrees, raising its stake to 20% at the end of 2007. Based on the Fund's cost basis, well below GAAP book value and at single digit multiples of pre-tax earnings, we believe that we have provided for a wide margin of safety and have stacked the odds favorably.

The Fund participated in the recent \$2.65 billion recapitalization of MBIA Inc., a financial guarantor whose expansion into structured credit products in recent years may have strained that company's financial resources. Importantly, the Small-Cap Value Fund's modest position represents a direct investment in "Surplus Notes" issued by MBIA's insurance subsidiary and not in the equity of the holding company, a security that holds the potential for considerably higher returns but also engenders a higher degree of investment risk. The company's travails have been well publicized in the sometimes hysterical financial press, but seem to be adequately accounted for by the 14% coupon payable on the Notes, a yield that puts this issue squarely in



“distressed” territory. The notes, which were issued under SEC Rule 144A<sup>1</sup>, are unsecured debt obligations of the insurance subsidiary, whose principal and interest payments are subject to the approval of the New York Superintendent of Insurance.

The Fund received Brookfield Infrastructure Partner Units in connection with a plan by Brookfield Asset Management (“BAM”) to make a special dividend to holders of its shares. The Units, which trade on the New York Stock Exchange, represent a 60% limited partnership interest in Brookfield Infrastructure L.P., a partnership established by BAM to own and operate infrastructure assets (e.g., generally defined as long-life physical assets with high barriers to entry and stable cash flows). The initial operations and assets include electricity transmission assets in Chile, Brazil and Canada and timberlands on Vancouver Island, and in Oregon and Washington.

As reported in last quarter’s shareholder letter, the Fund successfully exited its positions in Pogo Common, Ceridian Common and Nuveen Common following the cash acquisition of those companies in merger transactions. Fund management disposed of its holdings in the shares of oil and gas producer CNX following the announcement that it would be acquired in a share exchange offer by CONSOL Energy. We were sorry to see this one go, but the results in this case were highly satisfying, as the Fund doubled its investment in less than two and a half years.

## LOOKING FORWARD

As analysts, we don’t blindly assume that a company’s recent experience tells us much about the future of the business. In fact, as suggested in the description of our new holdings, it is often those securities where there exists a yawning gap between perception and reality that get our attention and capital. Similarly, many fund investors err in overweighting recent past performance when evaluating their investment managers, while underweighting a Fund’s prospective returns. In this vein, I would like to update you on some encouraging developments in the Fund and give you a sense of why the Fund’s holdings, generally speaking, present some

**“Although we try to avoid false precision, I believe that the *underlying business values* corresponding to the Fund’s holdings reside somewhere between 30% to 35% above today’s market values.”**

interesting opportunities and prospects. Although we try to avoid false precision, I believe that the *underlying business values* corresponding to the Fund’s holdings reside somewhere between 30% to 35% above today’s market values. Notably, in the vast majority of cases, the per share business values continue to grow at attractive rates. And almost without exception, the businesses in the Small-Cap

Value portfolio remain overcapitalized or extremely well financed, a position that ought to enable further expansion of business values. Recent “Resource Conversion”<sup>2</sup> activity among the Fund’s holdings evidences the currently wide discrepancy between market values and underlying business values. In addition to those completed Resource Conversion events mentioned

<sup>1</sup>SEC Rule 144A, as amended, restricts the purchase and sale of securities made pursuant to the provisions of this section to qualified institutional buyers.

<sup>2</sup>Resource Conversion activity as defined can include mergers and acquisitions, contests for control, leveraged buyouts, corporate restructurings, the acquisition in bulk of securities through cash tender offers, exchange offers and the use of the corporate proxy. Whitman, Martin J. *Value Investing – A Balanced Approach*. New York: John Wiley & Sons, Inc., 1999.



above, a few works in process, aggregating an additional 6% of Fund assets, illustrate my point:

**ASV, Inc.**, a maker of rubber track loaders used in construction, forestry and other arenas, announced on January 14th that it had agreed to be acquired by Terex at a 45% premium to the market (and a modest premium to the Fund's cost basis). The Fund has owned shares for a little over a year.

**Bronco Drilling**, a provider of contract drilling services to the oil and gas industry, announced on January 24th that it had entered into an agreement with Allis-Chalmers Energy to be acquired in a cash and stock deal at an 18% premium to market (approximating the Fund's current cost basis). This deal will be closely monitored by Fund management, as it appears to undervalue Bronco's attractive assets by at least 20%.

**Coherent, Inc.**, a leading supplier of laser-based photonic equipment used in semiconductor manufacturing, telecommunications equipment, packaging, testing and reprographics markets, announced on February 11th that it would use a portion of its existing cash to repurchase up to 24% of the company's shares at a premium to market in a Dutch Auction Tender Offer.

Calgary-based **Fording Canadian Coal**, one of the world's largest producers of seaborne, metallurgical coal used by steel mills, announced in early December that it had formed an independent Board committee to review "strategic alternatives," potentially foreshadowing a sale of all, or a portion of, the company's assets.

**Helicon Re**, a reinsurance holding company formed to write property and marine excess reinsurance through a quota share treaty with Folksamerica, was purchased on December 31, 2007 by White Mountains Insurance at Net Asset Value – a reasonable price in our view.

**Phoenix Companies**, a life insurance and asset management firm, has announced that it would spin off the asset management business to Phoenix shareholders in the form of a special dividend. Additionally, a dissident shareholder has proposed a slate of three directors for the company's board.

If these cases hold some positive implications for the Fund's other holdings – and at this stage I think they do – the Fund's *prospective* returns seem quite attractive.

I look forward to writing you again when we publish our Second Quarter report dated April 30, 2008. Thank you for your continued support.

Sincerely,

Curtis R. Jensen

Co-Chief Investment Officer and Portfolio Manager  
Third Avenue Small-Cap Value Fund



## Third Avenue Real Estate Value Fund



**MICHAEL H. WINER**  
PORTFOLIO MANAGER OF THIRD AVENUE  
REAL ESTATE VALUE FUND

Dear Fellow Shareholders:

At January 31, 2008, the end of the first fiscal quarter of 2008, the unaudited net asset value attributable to the 86,005,439 shares outstanding of the Third Avenue Real Estate Value Fund (the "Fund") was \$27.55 per share. This compares with an audited net asset value of \$31.72 per share at October 31, 2007, and an unaudited net asset value of \$31.86 per share at January 31, 2007, both adjusted for subsequent distributions to shareholders. At February 28, 2008, the unaudited net asset value was \$26.37 per share.

### QUARTERLY ACTIVITY

The following summarizes the Fund's investment activity during the quarter:

#### Number of Shares

240,456 shares

#### New Positions Acquired

Brookfield Infrastructure Partners,  
L.P. Common Units  
("Brookfield Infrastructure Units")

#### Number of Shares

1,878,851 shares

100 shares

630,263 shares

649,680 shares

86,286 shares

1,153,812 shares

1,900,000 shares

#### New Positions Acquired (continued)

Cousins Properties, Inc. Common Stock  
("Cousins Common")

#### Positions Increased

Daibiru Corp. Common Stock  
("Daibiru Common")

Derwent London plc Common Stock  
("Derwent Common")

Eastgroup Properties, Inc.  
Common Stock  
("Eastgroup Common")

First Potomac Realty Trust  
Common Stock  
("First Potomac Common")

Hammerson plc Common Stock  
("Hammerson Common")

Mitsui Fudosan Co. Ltd.  
Common Stock  
("Mitsui Common")

\* Portfolio holdings are subject to change without notice. The following is a list of Third Avenue Real Estate Value Fund's 10 largest issuers, and the percentage of the total net assets each represented, as of January 31, 2008: Forest City Enterprises, Inc., 11.33%; Brookfield Asset Management, 9.63%; The St. Joe Company, 6.73%; Vornado Realty Trust, 4.76%; ProLogis, 4.43%; Wheelock & Co., Ltd., 3.96%; Hang Lung Properties Ltd., 3.66%; British Land Company, 3.27%; Henderson Land Development Co., Ltd., 3.24%; and Derwent London PLC, 3.14%.





<b>Number of Shares</b>	<b>Positions Increased (continued)</b>
1,671,140 shares	Quintain Estates & Development plc Common Stock ("Quintain Common")
1,037,990 shares	The St. Joe Company Common Stock ("St. Joe Common")
	<b>Positions Reduced</b>
371,225 shares	Brookfield Asset Management, Inc. Common Stock ("Brookfield Common")
8,505,000 shares	Henderson Land Development Co. Ltd. Common Stock ("Henderson Common")
273,996 shares	One Liberty Properties, Inc. Common Stock ("One Liberty Common")
250,000 shares	ProLogis Common Stock ("ProLogis Common")
2,364,000 shares	Sapporo Holdings, Ltd. Common Stock ("Sapporo Common")
25,345,775 shares	Wharf Holdings, Ltd. Common Stock ("Wharf Common")
	<b>Positions Eliminated</b>
2,922,017 shares	American Financial Realty Trust Common Stock ("American Financial Common")
5,000 shares	Atlantic American Realty Capital Advisors, Inc. Common Stock ("Atlantic Common")
80,000 shares	First Capital Realty, Inc. Common Stock ("First Capital Common")

#### **DISCUSSION OF QUARTERLY ACTIVITY**

The Fund continued to experience net redemptions during the quarter (approximately \$213 million). The good news is the majority of redemptions took place in

November and December, and we may have turned the corner since the beginning of the New Year. During the quarter, the Fund established one new position in a U.S. REIT and it received partnership units in an infrastructure company that was spun-off from Brookfield Asset Management. The Fund decreased its holdings in several common stocks, to provide liquidity for redemptions and to take advantage of excellent buying opportunities in a new position as well as in existing holdings.

The Fund initiated a position in Cousins Common at a substantial discount to our conservative estimate of net asset value ("NAV"). Cousins is an Atlanta-based REIT that develops and owns commercial and residential properties, primarily in the Southeastern U.S. The company has a 45-year track record of creating wealth by developing, repositioning and gaining entitlements on all types of real estate. The company has a very strong financial position and owns a diversified portfolio of office, retail and industrial properties, as well as a large development pipeline of office, retail, industrial and residential properties. Fund management has been impressed with Cousins Properties for many years, but until recently, we were never able to acquire the stock at a substantial discount. Recent market volatility enabled the Fund to finally take a position in the stock.

#### **COMMERCIAL PROPERTY VALUES HAVE BEEN IMPACTED BY UNCERTAIN CREDIT MARKETS**

The global credit crunch that began to unfold in early 2007 as a result of the much-publicized, sub-prime mortgage melt-down in the United States, has now affected most financial sectors – even those that are only remotely related to U.S. sub-prime mortgages. Commercial property valuations – particularly in the United States and Europe – have declined as the result of uncertainties regarding availability of financing and how an economic slowdown may impact future rental growth.

Commercial property values are impacted by several factors, including economic fundamentals (e.g., supply



and demand), interest rates, availability of financing, location and quality of properties and, most acutely, valuations implied by recent comparable sale transactions. Property valuations are most often determined by applying a market-determined capitalization rate (cap rate) to net operating income. A cap rate converts income into value. Typically, a cap rate reflects the anticipated unleveraged yield for the succeeding year. The unleveraged yield is determined by dividing the net operating income (cash flow before debt service and capital expenditures) by the purchase price. A property expected to generate net operating income of \$900,000 would be valued at \$15 million using a 6% cap rate. Unfortunately, capitalizing first-year net operating income is not always an accurate measure of value. For example, a fully occupied office building leased to a single high-credit-quality tenant would seemingly warrant a lower cap rate than a similar building leased to multiple, lower-quality tenants. However, if the lease on the single-tenant building is set to expire in two years, and the contract rent exceeds current market rents in the area, then a higher cap rate (lower value) is warranted to compensate for the uncertainty of future cash flows. Similarly, if the contract rents on the multi-tenant building are substantially below current market rents, and there will be near-term opportunities to increase contract rents, then a lower cap rate (higher value) is warranted.

To determine an appropriate cap rate, several factors must be considered – including property specific and general market. Property specific factors include age, physical condition, location, credit quality of tenants, occupancy levels, in-place rents versus current market rents, lease expirations and local supply and demand. General market factors include interest rates, availability of long-term financing, unemployment rates, inflation and macro-economic conditions. Simply put, a cap rate (required yield) should indicate the “risk premium” over the “risk-free” return (e.g., U.S. government securities).

Each of the aforementioned factors must be taken into account when evaluating the risk premium.

Cap rates are heavily affected by interest rates and the availability of long-term financing. A primary source of long-term financing for commercial properties over the last fifteen years has been “conduit lenders” that underwrite and originate loans that ultimately get packaged into commercial mortgage-backed securities (“CMBS”). The recent global credit crunch has had minimal impact on interest rates, but a dramatic impact on availability of financing. Demand for CMBS has weakened globally since banks and institutional investors began suffering mark-to-market losses on investment-grade, subprime mortgage-backed securities. Despite strong credit fundamentals, especially high up in the CMBS capital structure, spreads on super senior CMBS have widened over 150 basis points (1.5%) since last summer. The decoupling of spreads and credit fundamentals is apparently due to uncertainty about potential economic fallout from the downturn in the U.S. housing and mortgage markets. U.S. 10-year Treasury yields have declined from about 5% last July to under 4% as of January 31st. Therefore, even though spreads have widened, actual yields on AAA-rated CMBS have not increased dramatically. (Note: the fact that the “risk-free” returns are lower, while required yields are higher, illustrates investors’ demand for higher “risk premium.”) The lack of liquidity and demand for CMBS has dramatically curtailed new loan originations by conduit lenders. This lack of financing has, in turn, resulted in a dramatic slowdown in commercial property transactions. Buyers and borrowers seeking refinancing have been forced to seek financing from “portfolio lenders” such as insurance companies and pension funds, that tend to have more conservative underwriting standards. These more conservative standards generally require more equity and more experienced and credit-worthy borrowers.



Like any other investment, real estate must generate fair, risk-adjusted returns on equity to be attractive. If an investor can obtain 75% leverage at 6% interest on an investment property that yields 7%, the investor's first-year return on equity is 10%. (The equity return is higher due to the positive spread between the 7% property yield and 6% cost of debt.) However, if the investor could only obtain 60% leverage at 6% interest, the first-year return on equity would be only 8.5%. In order to achieve a 10% first-year return on equity, the investment property would have to yield 7.6%. This example illustrates the effect tighter credit has on cap rates (required yields) and, thus, commercial property values. Simply reducing the amount of leverage from 75% to 60% can force cap rates to increase (in this example, from 7% to 7.6%, or an 8.6% decrease in property value). Tighter credit, coupled with economic uncertainty and wider spreads (increased risk premiums) has resulted in downward revaluations for all property types.

The market prices for common stocks of U.S. and U.K.-based real estate companies have also declined, but seemingly to a much more dramatic extent than the underlying properties. Notwithstanding the evidence that commercial properties values have declined, and may decline even farther, Fund management believes that the public market for common stocks of high-quality real estate companies has overreacted to the global credit crisis.

British Land Common is an example of a security held by the Fund that seems to have been oversold due to fear and uncertainty, despite very strong underlying property and corporate fundamentals. To wit:

- Properties are 99% leased.

- Average lease term is 14 years.
- Underlying rents increased 5% year-to-date for the nine months ended December 31, 2007.
- 100% of outstanding debt is fixed at 5.28% average rate.
- Average remaining term of outstanding debt is 12.6 years.
- Cash flow covers interest charges by 180%.
- Underlying profit before tax (excluding property revaluations) is up 12.5% for the nine months ended December 31, 2007.
- Development portfolio is substantially pre-let, sold or under offer.

**"Notwithstanding the evidence that commercial properties values have declined, and may decline even farther, Fund management believes that the public market for common stocks of high-quality real estate companies has overreacted to the global credit crisis."**

Despite British Land's strong fundamentals, NAV per share (based on independent appraisals) declined from £15.86 at December 31, 2006 to £14.37 at December 31, 2007, a decrease of 9.4%. Over the same 12-month period, the market price of British Land Common decreased from £17.31 to £9.45, a decrease of 45.4%.

As of December 31, 2007, British Land Common traded at a 34% discount to NAV. The NAV was calculated using an implied cap rate of 5.40%, representing a 74 basis point upward shift in yield from 4.66% nine months earlier.

British Land's reduced property valuations are clearly not the result of poor property fundamentals, ineffective management or poor quality properties or locations. Rather, it is entirely due to higher cap rates. British Land has the luxury of being able to effectively ignore what appears to be near-term market turmoil. The company has no near-term financing requirements; it does not need to sell properties; its properties are fully leased



pursuant to long-term non-cancelable leases; and sustainable and predictable property cash flows provide a strong cushion to service its debt, which is long-term and at fixed rates.

The Fund's investments are heavily concentrated in the common stocks of high-quality real estate companies that, like British Land, are fundamentally unaffected by the near-term market turmoil. On the contrary, these well-capitalized companies, in many cases, are able to use their strong financial positions to take advantage of opportunities to invest at distressed prices. For example, Forest City Enterprises recently acquired 2,500 residential lots in San Antonio, Texas for about 25% of what the seller had paid three years prior. The seller (a large, public homebuilder) needed to sell and Forest City had the liquidity to buy... apparently on their own terms.

Fund management has no idea whether property values in the United States and Europe will continue to decline and, if so, how far. In our view, the re-pricing of risk premiums for high-quality commercial properties is likely to be a short-term issue. In the event the downturn becomes extended, we take great comfort in knowing that the Fund is invested in the common stocks of extremely well-financed companies with high-quality portfolios. Regardless of near-term pricing issues, these investments should provide solid, long-term growth in value. Furthermore, we believe that the stock prices for the vast majority of the Fund's holdings represent significant discounts to any reasonable valuations. Real estate companies and owners that are not well-financed (highly leveraged, liquidity restrained or with significant near-term debt maturities) are likely to suffer serious and potentially devastating pain from the market turmoil. It is not unlike investors in the stock market that are forced to focus on near-term market results because they are invested on margin or their livelihood (paycheck) is based on short-term performance. As value investors, we focus our investments in companies with managements that think similarly – maintain a strong financial

position, develop and manage high-quality properties, take advantage of market volatility and create long-term value.

I look forward to writing you again when we publish our Semi-Annual Report for the period ending April 30, 2008.

Sincerely,

Michael H. Winer  
Portfolio Manager  
Third Avenue Real Estate Value Fund



## Third Avenue International Value Fund



**AMIT B. WADHWANEY**  
PORTFOLIO MANAGER OF THIRD  
AVENUE INTERNATIONAL VALUE FUND

Dear Fellow Shareholders:

At January 31, 2008, the unaudited net asset value attributable to the 101,161,737 shares outstanding of the Third Avenue International Value Fund (the "Fund") was \$18.21 per share, compared with the Fund's audited net asset value at October 31, 2007 of \$21.25 per share, and an unaudited net asset value of \$18.19 per share at January 31, 2007, both adjusted for a subsequent distribution to shareholders. At February 28, 2008, the unaudited net asset value was \$19.00 per share.

### QUARTERLY ACTIVITY:

In the most recent quarter of operations, the Fund established a new position in the common stock of one company, added to positions in the common stocks of six companies, eliminated holdings in six securities and reduced holdings in 26 securities.

**Number of Shares**  
56,450,000 shares

**New Position Acquired**  
United Microelectronics Corp.  
Common Stock  
("UMC Common")

### Number of Shares or Units

135,000 shares

8,176,515 shares

163,800 shares

106,000 units

877,500 shares

69,000 shares

606,050 shares

261,900 shares

9,660 shares

71,000 shares

3,065,000 shares

1,152,700 units

619,301 shares

278,620 shares

750,000 shares

500,700 shares

459,150 units

### Positions Increased

Asatsu-DK Inc. Common Stock  
("Asatsu Common")

CSR Ltd. Common Stock  
("CSR Common")

Daibiru Corporation Common Stock  
("Daibiru Common")

Fording Canadian Coal Trust Units  
("Fording Units")

Montpelier Re Holdings Ltd.  
Common Stock  
("Montpelier Common")

WBL Corp. Ltd. Common Stock  
("WBL Common")

### Positions Eliminated

Aiful Corporation Common Stock  
("Aiful Common")

Aker Kvaerner ASA Common Stock  
("Aker Common")

LG Corp. Preferred Stock  
("LG Preferred")

Pargesa Holding SA Common Stock  
("Pargesa Common")

UOB-Kay Hian Holdings Ltd.  
Common Stock ("UOB Common")

Westshore Terminals Income Fund Units  
("Westshore Units")

### Positions Reduced

ABB Grain Ltd. Common Stock  
("ABB Common")

Antarchile S.A. Common Stock  
("Antarchile Common")

BRIT Insurance Holdings  
plc Common Stock ("BRIT Common")

Canfor Corporation Common Stock  
("Canfor Common")

Canfor Pulp Income Fund Units  
("Canfor Pulp Units")

\* Portfolio holdings are subject to change without notice. The following is a list of Third Avenue International Value Fund's 10 largest issuers, and the percentage of the total net assets each represented, as of January 31, 2008: Saskatchewan Wheat Pool, 4.96%; ABB Grain, Ltd., 4.31%; Yuanta Financial Holding Co., Ltd., 3.79%; GuocoLeisure Ltd., 3.43%; Catalyst Paper Corp., 3.33%; Nippon Sheet Glass Co., Ltd., 3.29%; Guoco Group, Ltd., 3.16%; WBL Corp., Ltd., 3.09%; Antarchile S.A., 2.89%; and Compagnie Nationale a Portefeuille, 2.82%.



## Number of Shares

810,300 shares

5,000,000 shares

1,105,500 shares

666,450 shares

608,900 shares

7,500,000 shares

1,157,400 shares

135,000 shares

747,000 shares

1,590,000 shares

43,537,600 shares

2,220,000 shares

110,132 shares

729,300 shares

550,000 shares

3,806,000 shares

4,393,500 shares

986,000 shares

42,760 shares

11,334,000 shares

16,500,000 shares

## Positions Reduced (continued)

Capital Nomura Securities PCL  
Common Stock ("CNS Common")

Capital Securities Common Stock  
("Capital Common")

Chudenko Corp. Common Stock  
("Chudenko Common")

Farstad Shipping ASA Common Stock  
("Farstad Common")

Futaba Corp. Common Stock  
("Futaba Common")

Gigabyte Technology Co. Ltd.  
Common Stock ("Gigabyte Common")

Golar LNG Ltd. Common Stock  
("Golar Common")

Guoco Group Ltd. Common Stock  
("Guoco Common")

Guocoleisure Ltd. Common Stock  
("Guocoleisure Common")

Hutchison Whampoa Ltd. Common Stock  
("Hutchison Common")

KGI Securities Thailand PCL  
Common Stock ("KGI Common")

Liu Chong Hing Investment Ltd.  
Common Stock ("LCHI Common")

Compagnie Nationale a Portefeuille  
Common Stock ("CNP Common")

Nichicon Corp. Common Stock  
("Nichicon Common")

Nippon Sheet Glass Co. Ltd.  
Common Stock ("NSG Common")

President Securities Corp.  
Common Stock  
("President Common")

Saskatchewan Wheat Pool Inc.  
Common Stock ("Pool Common")

Tokyo Energy & Systems Inc.  
Common Stock ("TE&S Common")

United International Enterprises Ltd.  
Common Stock ("UIE Common")

Vitasoy International Holdings Ltd.  
Common Stock ("Vitasoy Common")

Yuanta Financial Holding Co. Ltd.  
Common Stock ("Yuanta Common")

billion, fewer and fewer companies can afford or justify spending on a new fab. The semiconductor industry is separating into companies that design and market chips and those that manufacture them. Starting in the late 1980s, dedicated manufacturing specialists, called foundries, began to take market share away from integrated design and manufacturing companies. United Microelectronics ("UMC"), a Taiwanese company, is the world's second largest semiconductor foundry and a direct beneficiary of the long-term move to foundries.

Economies of scale are crucial in the foundry business. UMC is one-third the size of the industry leader Taiwan Semiconductor Manufacturing Co. ("TSMC") and, therefore, suffers from smaller margins. It has, however, been consistently profitable and generated positive free cash flow over the long term, even after meeting the large capital spending requirements inherent in the semiconductor business. Apart from TSMC and UMC, no other semiconductor foundry in the world has managed to consistently generate cash. In fact, several of the second-tier companies consumed billions of dollars of capital, yet failed to reach profitability. Numerous entrants to the foundry business went bankrupt, or were forced to leave the industry.

Unlike its competitors, UMC used the cash flow from its core business to build a portfolio of investments anchored around a venture capital portfolio. UMC is one of the largest venture capital investors in Taiwan and it presents an attractive partner for semiconductor startups, as it offers technological expertise to its investees and access to UMC's manufacturing capacity. This investment portfolio has performed remarkably well over the long term. In the past five years, gains on the portfolio exceeded operating earnings from the semiconductor business by a multiple of three, despite the bursting of the technology bubble and widespread decline in valuations of technology firms. The company continues to invest in new ventures, both in Taiwan and in China. Taking into account the liquidation value of the UMC venture capital and investment portfolio, the Fund's investment was initiated at a valuation that attributed to three times (trailing) earnings derived from UMC's operations.

## REVIEW OF QUARTERLY ACTIVITY

As the cost of building semiconductor factories ("fabs") increases rapidly, and now exceeds an average of \$3





Post quarter-end, one of the Fund's holdings, Catalyst Paper Corp. ("Catalyst") announced the purchase of a newsprint mill in Snowflake, Arizona from a subsidiary of AbitibiBowater Inc. A significant portion of the cash purchase price of US \$161 million is intended to be funded via an equity rights issue of CDN \$125 million, of which the Fund has agreed to exercise rights to subscribe for up to CDN \$62.5 million, not otherwise subscribed under the rights offering, slated to take place during the next two months. Fund management is of the view that the purchase of this low cost, recycled fiber-based mill is an attractive one, modestly priced (less than three times 2006 operating earnings, before accounting for any synergies with Catalyst's existing operations), and provides the company with geographic, currency and fiber source diversification, in addition to proximity to one of North America's most rapidly growing markets.

Over the past several months, the Fund decreased its holdings in a number of stocks to maintain liquidity to meet shareholder redemptions and to take advantage of unfolding opportunities in attractively valued securities and, in particular, to subscribe to the above-noted rights issue of Catalyst.

#### COMMENTS ON THE CURRENT INVESTMENT ENVIRONMENT

Since the middle of 2007, a series of credit problems has unsettled the financial world and led to a general decline in the equity markets. This is certainly not the first time (and, dare we predict, not the last time) that problems at financial institutions reverberated through the markets and the wider economies. Within recent memory, we have witnessed several examples of market turmoil that bear some similarity with the current scenario. In 1990 and 1991, we saw the simultaneous collapse of the U.S. high-yield market and commercial real estate market which led to, among other

results, the savings & loan crisis and failures of several insurance companies. Throughout the 1990s and into the early 2000s, many Japanese financial institutions slowly descended into near, or actual, bankruptcy as the excesses of the 1980s Japanese financial boom came to haunt them. In 1997 and 1998, a foreign exchange crisis originating with Thai financial companies triggered a series of financial and economic seizures in East and Southeast Asia. More recently, in January 2002, the floating and subsequent collapse of the Argentinian peso destroyed that country's financial system.

Although these economic and financial crises spanned a variety of time periods and geographies and had varied recovery periods, each case presented tremendous investment opportunities which provided attractive rates of return in the following periods, as the financial markets returned to normalcy.

Today's financial problems may have been triggered by the subprime mortgage crisis in the

U.S. However, given the linkages both on the asset and liability sides with foreign institutions, it is inevitable that repercussions will be felt worldwide. We do not know whether, or not, there will be a recession; but, our investment style does not depend on our ability (or lack thereof) to predict the timing and severity of economic downturns. We restrict ourselves to investing in only the common stock of companies which we believe have long-term staying power and the ability to cope with economic or cyclical downturns, without the need to access capital markets to finance their operations.

The sell down in equity markets presents an expanding set of compelling investment opportunities worldwide that meet our "safe and cheap\*" investment criteria. Among our existing holdings, we have been adding to investments whose share prices seem to have suffered due to:

**"The sell down in equity markets presents an expanding set of compelling investment opportunities worldwide that meet our "safe and cheap\*" investment criteria."**

\* "Safe" means the companies have strong finances, competent management, and an understandable business. "Cheap" means that we can buy the security for significantly less than what a private buyer might pay for control.



- generalized fears of an economic slowdown, e.g., UMC in Taiwan, Daibiru and Asatsu-DK in Japan;
- the taint of belonging to the financial services sector, e.g., Montpelier Re;
- small, but manageable, exposure to poor-quality asset-backed instruments, e.g., Millea.

In each case, the risk of a permanent impairment of the value of the business seems minimal, given their fortress-like balance sheets, and current valuations look exceptionally cheap from a long-term perspective.

Companies that have available cash or the ability to raise fresh cash in the current credit environment have a tremendous advantage over their cash-starved competitors. Similar to the financial markets, the markets for corporate assets suffer from lack of buyers. Those few companies able and confident enough to purchase assets from forced sellers can find exceptional investment opportunities, as the aforementioned example of Catalyst Paper's bid for Snowflake paper mill illustrates.

Buying when everybody else is selling is not for the faint of heart – otherwise, it would be a more popular practice. In addition to capital, such contrarian investing demands exhaustive research, care in execution, patience, and unwavering conviction in our investment philosophy. Our past experiences of profiting from previous bouts of market turmoil have certainly helped train us to withstand short-term pain, but conviction and emotional fortitude are not enough. We would not be able to execute our long-term investment strategy without the support and trust of like-minded clients, who are willing to be patient and look towards long-term absolute returns, rather than short-term relative performance. Third Avenue enjoys the good fortune of having incredibly supportive fellow shareholders who share our long-term outlook and investment philosophy. In the end, it is our clients who make it possible for us to do what we do and we are grateful for your trust.

#### GEOGRAPHICAL DISTRIBUTION OF INVESTMENTS

*At the end of January 2008, the geographical distribution of equity securities held by the Fund was as follows:*

Canada	14.23%
Japan	13.12
Taiwan	9.21
Hong Kong	7.80
Singapore	7.66
Australia	6.20
Chile	2.89
Belgium	2.82
Norway	2.80
Poland	2.77
United States	2.52
Bermuda	2.35
United Kingdom	2.21
South Korea	2.14
Denmark	1.80
New Zealand	1.74
France	0.91
Thailand	0.76
Equities-total	83.93
Cash & Other	16.07
Total	100.00

*Portfolio holdings are subject to change without notice.*

Note that the table above should be viewed as an ex-post listing of where our investments reside, period. As we have noted in prior letters, there is no attempt to allocate the portfolio assets among countries (or sectors) based upon an overarching macroeconomic view or index-related considerations.

I look forward to writing to you again when we publish our next quarterly report for the period ending April 30, 2008.

Sincerely,

Amit Wadhwaney  
Portfolio Manager,  
Third Avenue International Value Fund



## **BOARD OF TRUSTEES**

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## **TRANSFER AGENT**

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**Providence, RI 02940**  
**610-239-4600**  
**800-443-1021 (toll-free)**

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**New York, NY 10017**

## **CUSTODIAN**

**Custodial Trust Company**  
**101 Carnegie Center**  
**Princeton, NJ 08540**



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