How We Think About Risk: Part II

Margin of Safety

In seeking to protect our investors against permanent impairment of capital, we rely on five operational principles: (1) **margin of safety**, don't overpay for assets, (2) **diversification**, let positive and negative surprises average out, (3) **low leverage**, avoid potentially catastrophic losses associated with high leverage, (4) **balance**, build a portfolio that is not overly exposed to any single macroeconomic risk and (5) **protection against extreme outcomes**, consider assets, like gold, that may do well if the world falls apart. For each of these principles, First Eagle Funds has processes in place that seek to limit the risks involved in investing.

> *We believe that the value of a business depends ultimately on the cash flow — present and future — that it produces for its owners.*

FIRST EAGLE
FUNDS

This edition of First Eagle News describes how we estimate a margin of safety, the difference between what we pay for an investment and what we estimate its underlying intrinsic value to be. Since we have fairly accurate knowledge of the price we are willing to pay for each security, any error in calculating a margin of safety arises from our misestimating an investment's intrinsic value. Therefore, we are especially careful to build our estimates of intrinsic value from thorough and detailed knowledge of the particular businesses in which we are investing.

Since we generally avoid businesses with significant debt (i.e., high leverage), the value of each of our equity investments is usually very close to the value of the underlying business that the equity ownership represents.

We seek to identify the intrinsic values of underlying businesses before any financial engineering.

Earnings Potential

We believe that the value of a business depends ultimately on the cash flow — present and future — that it produces for its owners. In a perfect world, this distributable cash flow should coincide with a business's accounting earnings. Therefore, our starting point for estimating the intrinsic value of a business is to estimate its earnings potential.

We do this in several steps. First, we look beyond currently reported earnings and analysts' estimates of near-term future earnings and calculate an estimate of sustainable average earnings without making any provision for future growth potential. By treating growth separately, we isolate our earnings estimates from the uncertainties associated with future growth rates. We attempt to put our investors' capital to work by concentrating on the component of intrinsic value, which we feel can be known with reasonable accuracy.

Earnings in any particular year may be unusually high or low because of business cycle conditions, temporary industry over- or undersupply, a transient change in the prices of key inputs or other unusual competitive conditions. In most businesses, these factors affect profit margins far more than they affect sales. Thus, we estimate average profit margins over the full range of a business cycle, five to ten years, and account for other conditions and then compare these margins to the margins during perceived "normal" years and in similar national markets around the world. Usually, we feel this will yield a fairly clear picture of "average" profits.

We seek to identify the intrinsic values of underlying businesses before any financial engineering. The resulting estimate of earnings, typically referred to as "operating earnings," is then adjusted to correct for accounting distortions. The results of these adjustments provide a good estimate of the true "average" earnings potential of any particular business in its current state.

Sustainable Earnings

The next question we ask is whether our calculation of the business's historical "average" earnings level is likely to be sustainable in the future. Here the critical insight is that, in a market economy, sustainable earnings must be protected from competitive erosion either by the cost of the assets necessary to produce those earnings or by economic conditions that produce barriers to entry, or, as Warren Buffett calls them, "moats," against potential competitors. In the case of Internet stocks, neither asset requirements nor barriers to entry existed. Even companies like AOL, which produced significant earnings, were unlikely to be able to sustain those earnings because their "average" earnings-based values were illusory. Therefore, after calculating "average" earnings, our second focus is on identifying either asset protection of those earnings or, in the absence of asset protection, identifiable and reliable barriers to entry.

Earnings are protected by asset requirements when the value of those earnings is less than the cost of the asset investments necessary to produce them. But, in some instances, when there is less than full asset protection, we still ascribe value to earnings that appear well-protected by "moats," assuming, of course, that margins are not steadily eroding. We always look for adequate asset protection. But if margins are stable or rising over time and there has been little or no effective entry into the markets by a competitor (e.g., Gillette razors), then we are prepared to entertain the possibility that earnings are sustainable without the necessary level of asset protection. In the language of value investing, these are "Buffett-type" stocks; they are worth looking at, but call for great care.

Management Rationality

Lastly, a third factor we look at carefully, beyond the level and sustainability of earnings, is how well management redeploys earnings. There are instances when management reinvests earnings at returns below those that investors require. They often do this in pursuit of their own goals, such as prestige, growth for its own sake or survival. Some part of the value of earnings is then destroyed and intrinsic values are correspondingly impaired. We seek prudent — not aggressive — management teams, who make decisions that will benefit the business over the long term.

> *We want to commit our investors' capital to well-identified, stable, sustainable intrinsic values.*

When we look for a margin of safety, we want to commit our investors' capital to well-identified, stable, sustainable intrinsic values, not to the dream of future prospects; because however alluring, they may never materialize.

Average Annual Returns as of 06/30/2011

	YTD	1 Year	5 Years	10 Years	Expense Ratio
First Eagle Global Fund – Class A (without sales charge) (SGENX)	5.20%	25.48%	7.80%	12.84%	1.16%
First Eagle Global Fund – Class A (with sales charge) (SGENX)	-0.06	19.21	6.70	12.26	
First Eagle Overseas Fund – Class A (without sales charge) (SGOVX)	4.19	24.04	7.07	13.52	1.17%
First Eagle Overseas Fund – Class A (with sales charge) (SGOVX)	-1.01	17.82	5.98	12.94	
	YTD	1 Year	5 Years	Since Inception 09/04/01	Expense Ratio
First Eagle U.S. Value Fund – Class A (without sales charge) (FEVAX)	6.49%	22.30%	6.13%	9.62%	1.24%
First Eagle U.S. Value Fund – Class A (with sales charge) (FEVAX)	1.17	16.19	5.04	9.05	

The performance data quoted herein represents past performance and does not guarantee future results. Market volatility can dramatically impact the fund's short-term performance. Current performance may be lower or higher than figures shown. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Past performance data through the most recent month end is available at firsteaglefunds.com or by calling 800.334.2143. The average annual returns for Class A Shares "with sales charge" of First Eagle Global, Overseas and U.S. Value Funds reflect the maximum sales charge of 5.00%.

There are risks associated with investing in funds that invest in securities of foreign countries, such as erratic market conditions, economic and political instability and fluctuations in currency exchange rates. Investment in gold and gold related investments present certain risks, and returns on gold related investments have traditionally been more volatile than investments in broader equity or debt markets. The holdings mentioned herein represent the following percentage of the total net assets of the First Eagle Global Fund as of June 30, 2011: AOL Inc. 0.00%, Procter & Gamble Co. 0.00%. The portfolio is actively managed and holdings can change at any time. Current and future portfolio holdings are subject to risk.

The commentary represents the opinion of the Global Value Team as of January 2010 and is subject to change based on market and other conditions. The opinions expressed are not necessarily those of the firm. First Eagle Investment Management, LLC (FEIM) became investment adviser to the Funds commencing January 1, 2000. **These materials are provided for informational purposes only.** These opinions are not intended to be a forecast of future events, a guarantee of future results or investment advice. Any statistics contained herein have been obtained from sources believed to be reliable, but the accuracy of this information cannot be guaranteed. **The views expressed herein may change at any time subsequent to the date of issue hereof.** The information provided is not to be construed as a recommendation or an offer to buy or sell or the solicitation of an offer to buy or sell any fund or security.

The First Eagle Funds are offered by FEF Distributors, LLC, 1345 Avenue of the Americas, New York, New York 10105. **This collateral is not authorized for distribution unless accompanied or preceded by a prospectus. Investors should consider investment objectives, risks, charges and expenses carefully, which are detailed in our prospectus and summary prospectus and may be obtained by asking your financial adviser, visiting our website at firsteaglefunds.com or calling us at 800.334.2143. Please read our prospectus carefully before investing. For further information about the First Eagle Funds please call 800.334.2143. Investments are not FDIC insured or bank guaranteed, and may lose value.**

First Eagle Funds
1345 Avenue of the Americas | New York, NY | 10105-4300
800.334.2143 | firsteaglefunds.com