OTSI KETA QUARTERLY

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OTSI KETA CAPITAL

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Otsi Keta Quarterly is designed to share insight on both current performance and future potential.

IN THIS ISSUE...

QUESTIONS...

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WHY THE MIDWEST?

First of four articles in a series for 2012

Many visions come to mind when thinking about businesses in the Midwestern United States. If you focus on the history of the Detroit area, your first thought probably would be the auto industry. If your mind wandered to Cleveland, visions of an old steel industry might come to pass. Chicago has been considered a financial center, Milwaukee was known as a hub for beer brewers, Pittsburgh had steel and banking, Minneapolis was a hub for farming and consumer packaged goods.

What you would find today is a completely retooled section of the United States, and one that motivated us to form the Fund. Of course, there are remnants, as well as viable businesses, in the above-mentioned examples in each of those cities. You would even find that some of those industries are better known in other parts of the Midwest than the original locations.

The point is that the Midwest continues to evolve and keeps us very interested as investors. What we will touch on for the rest of this article is the agricultural sector in the Midwest.

Agriculture-focused companies have always been an interest for the Fund. It is hard to ignore the global trends of a developing population while your country has some of the most productive land in the world. We are always on the hunt for a well-run company that fits into this space. We wanted to share our thoughts on the coming year.

The first factor everyone should focus on is the price of agricultural commodities right now. Commodities affect everyday life for everyone in the United States, from the gas pumps to the supermarket. But sometimes current prices for commodities do not reflect the future. Unfortunately, for 2012, we think they do. We think farmers will be aggressive in locking in prices for their crops early this year, with prices that continue to stay near record highs. This will translate into sustained profits for the farmer and high prices for the consumer. There also is a continued trend with livestock that sees the herds continuing to be thinned because of the cost of feed. While the price of proteins might continue to be held for the beginning of 2012, look for those prices to increase, as there could be fewer head to market in the latter half of the year.

We believe the government will continue to look at the farm subsidies as a potential for reducing the deficit. Ethanol legislation is already in play, and other subsidies could find their way out as the country continues to struggle with high debt. The fact that the farmer has enjoyed record returns over the last couple of years plays into this thinking as well.

Continued on page 3...

MUCH ADO ABOUT SINGLE-FAMILY HOMES

In AD 79, Gaius Plinius historically said, "Home is where the heart is." His home was in Como, Italy, and history is a little vague on whether he bought it from a distressed seller or in a short sale from the local thrift. Regardless of how Plinius got his home, his words indicate he thought it was pretty special. Recent data indicates many of today's homeowners don't share his sentiments.

With affordability at multi-decade lows and available inventory at all time highs, the pundits claim now is the time to buy. We recently asked ourselves, "If houses are such a good deal, why is there so little appetite from buyers?" We will save our readers the rote answers like tighter lending standards, high unemployment and inability to sell your current castle. The above factors explain much of the decline in housing, but as they have improved, housing hasn't. We think there are two additional factors curbing buyer's appetite.

Rate Risk

In 2011, the Federal Reserve purchased 61% of the total net treasury issuance, and these purchases have been keeping treasury yields artificially low. Mortgage rates are based in part on 10-year Treasury yields and are also near record lows. The Fed can't buy the majority of our debt forever. While many people may not understand how interest rates are set, they know intuitively that when lending money for 30 years to a stranger, 4% seems a little light. People are worried if they buy today and rates rise, future buyers won't be able to afford to pay what they paid. The table below shows how sensitive home affordability is to interest rate changes.

Mortgage Size based on $1,000 Monthly Payment at different interest rate levels

Fixed Interest Rate	Loan Term	Maximum Mortgage Size	Decline in Value Based on Rate Rising	Reduced affordability based on rate increases
4% - Today	30 years	$210,159	--	--
5%	30 years	$187,057	($23,102)	-11%
6%	30 years	$167,625	($42,534)	-20.2%

What the chart above makes clear is that there is a lot of affordability risk if rates rise in the future. A 200-basis-point increase in mortgage rates, all things being equal, would reduce the value of a home to the average 20% downpayment buyer by more than 20%. Mortgage rates moving from 4% to 6% seems a real possibility.

Illiquidity Recognition

Houses are inherently illiquid and that was an easy fact to forget during the late 1990s and early 2000s. The hallmark of an illiquid market is things can't quickly be sold without a significant loss in value. Buyers today are demanding big discounts to compensate for the increased selling risk. Young buyers who drive the demand for housing put a significant premium on flexibility. Our instincts tell us that members of this demographic cohort have been leaving the market regardless of lower prices, low interest rates and higher affordability.

At Otsi Keta, we have had success investing against conventional wisdom, but never investing against the consumer. For now we just don't think the consumer has much of an appetite for single-family homes, and that means home price appreciation could be a ways off.

OUR PORTFOLIO

During the first quarter of 2012, the fund took advantage of a recovering equity market to make a number of changes to the portfolio. We reduced or exited six holdings and added seven holdings. The changes affected 25% of the portfolio's AUM (assets under management), generating the most turnover we have had in any quarter since the fund's inception. The net result of the moves was a small capital gain for the fund. We believe the fund's annual long-term turnover should average 30%.

Three things drove turnover within the fund in Q1:

1. Opportunity seeking asset redeployment
2. Changes in our perception of a company's business risk
3. Violations of our investment thesis

When we take a position in a company, we believe it is our best use of capital and will generate acceptable risk-adjusted returns. With the exception of companies in our portfolio being taken over or sold due to valuation, sales frequently hinge on items two and three above. The table below summarizes the drivers of our recent turnover.

Portfolio Turnover

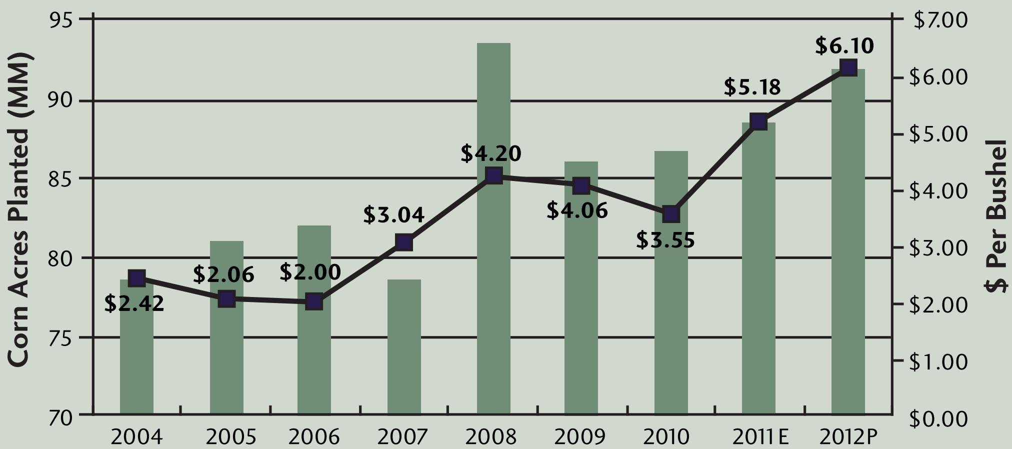
Business	Driver	Comments
Outside the Body Diagnostic Testing	Valuation	Stock price and fundamentals became stretched
Single-Use Cath Lab Tools	Violated investment thesis	Adopted excessively dilutive executive compensation plan
Analog Video Converters	Increased business risk	Failed to retain large customer
Electronic Couplers and Sensors	Increased business risk	Enjoined patent litigation with major competitor
Disposable Fluid Delivery	Increased business risk	Ineffective inventory management
Weight Management	Violated investment thesis	Poorly executed new product rollout

Keeping with our tradition, we don't talk about new positions in the fund. However, it goes without saying that we are very pleased with the new additions and, as always, will remain focused on the individual businesses and leave the broader market commentary to the pundits.

...Why the Midwest? continued from page 1

What does this mean for the Midwestern farmer? We see increases in spending for equipment to improve marginally productive land and become more efficient. Let's take a look at our backyard in Michigan. Michigan farmers exported $1.75 billion worth of food—mostly to Canada—in 2010. Forecasts have that number growing to beyond $2 billion for 2012. The state's goal is to double Michigan's agricultural exports over the next five years. The trend seems to be heading that way in a hurry.

The farming community tends to shun debt and only spends when coming off of productive years. Well, they are here. We continue to position the Fund to take advantage of these trends for 2012 with direct agriculture company exposure and second derivative companies in the agricultural sector.



OUR PERFORMANCE

For the first quarter ended March 31, 2012, the Otsi Keta Focus Fund was up 12.68%, or 63 basis points more than the Russell 2000 index (see below). Over the last year, the Fund was up 5.2%, outperforming the same index by 727 basis points. Since inception, the Fund has outperformed the Russell 2000 index by 449 basis points. All of the Otsi Keta Focus Fund numbers mentioned are net of all fees and expenses. Please see the table below to review how Otsi Keta Focus Fund Limited Partnership has performed this year.

Fund Name	Morningstar Rating	ROR 1st Quarter 2012	One Year	ROR From Inception (May 7th 2010)
Otsi Keta Focus Fund Limited Partnership*	**N/A**	**12.68%**	**5.2%**	**27.99%**
Russell 2000 Index	N/A	12.06%	-2.07%	23.5%
Russell 2000 Value	N/A	9.71%	-3.67%	14.7%

Source: Morningstar, Otsi Keta Capital, Russell Investment
*Note all OKFF performance data is shown net of all fees and expenses

Our annual meeting, audit and window

Otsi Keta Capital's second annual meeting will be held in downtown Detroit on Friday, May 18, at the Detroit Athletic Club. We are looking forward to reviewing the year with our investing partners, including a comprehensive look at some of the holdings within the portfolio. We are anticipating most, if not all, of the investing partners to be in attendance. We would love to extend an invitation to our readers—the only thing you have to do is pick up the phone and find out how to become a partner.

As this letter goes to press, we are wrapping up our second annual audit. As a refresher, we chose Baker, Tilly, Virchow, Krause LLP out of Minneapolis, Minnesota, because of their reputation and Midwest presence. The audit will be sent to partners during the first two weeks of April. If you are a potential investor and would like a copy of the fund's annual audit, please give us a call or drop us an e-mail, and we would be happy to provide one.

Finally, just a reminder to everyone who is looking forward to the "Window" opening for 2012. The Window Indicator will be featured in the second quarter 2012 investor's letter. The Soo Locks opened on March 26th and we anticipate a robust shipping season. We look forward to keeping you up on what is going by the "Window" this year.

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