OTSI KETA QUARTERLY

OTSI KETA CAPITAL

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

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QUESTIONS...

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WHY THE MIDWEST?

Third of four articles in a series for 2012

Manufacturing, available commercial real estate, low cost of living…

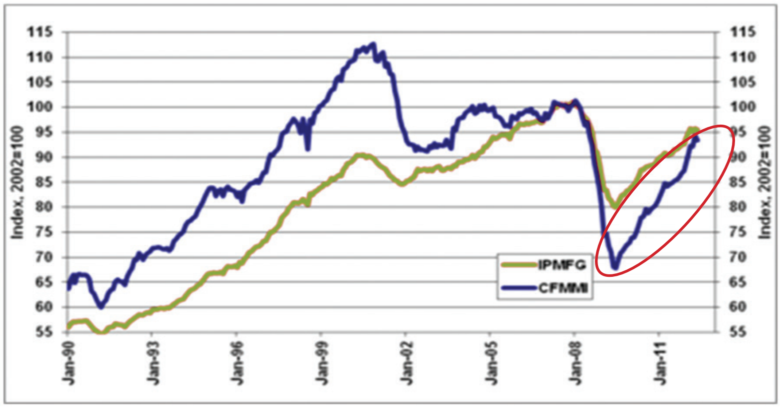
Some say that the Midwest remains a coiled spring. Years of creating industrial infrastructure, building housing stock and developing multiple transportation arteries have left this region ready for a resurgence. We would argue that the Midwest never went away, but that might be a different article.

A number of macroeconomic factors are contributing to the current resurgence in Midwest employment:

- Perhaps the most important factor fueling the turnaround is the weak United States dollar, which makes United States-produced products more cost-competitive in world markets. We see Midwest manufacturing as a drect beneficiary of this trend (see graph below). Also, foreign manufacturers that set up or expand manufacturing operations in the Midwest can reap additional benefits from the weak dollar, since it stretches the buying power of their currency.
- Another factor is the ample amount of idle industrial properties available in the Midwest for new or expanded manufacturing ventures. The Midwest is full of abandoned manufacturing facilities and towns that would welcome new opportunities with open arms (a few dozen come to mind right away).
- Third, the relatively low cost of living, including relatively low-cost electricity, is a contributing factor. While not the least expensive region in the United States (we can't get around four seasons of weather) in which to do business, the Midwest is cost competitive and provides a friendly regulatory and cost environment for manufacturers to operate in.

Continued on page 2...

Chicago Fed Midwest Manufacturing Index (CFMMI) vs. U.S. Manufacturing Production Index (IPMFG)



Source: Federal Reserve Bank of Chicago

THE TWO PERCENTERS

During the third quarter, investors continued to pour money into the corporate bond market. Fixed income has become the new must-have of the boomer generation, driven by global uncertainty and the manic desire for something with yield. Pundits debate whether the rush to fixed income is a form of hysterical blindness or sound stewardship; we think equity investors should be thanking these new two percenters.

10-year Treasury Yields	1.7%
AAA Corporate 10-year Bond Yields	2.06%
CPI Index	1.7%

So what are two percenters? Basically, they are regular folks and fund managers who work, pay taxes and then invest money in corporate bonds with two percent yields while inflation runs at roughly two percent. We know. We know. It doesn't sound like a great investment, but with treasuries yielding less than two percent, there are not many good options.

In truth, you can usually tell a two percenter by the grimace on their face when discussing their portfolio's yield. This contrasts sharply with the large smiles affixed to the faces of treasurers borrowing for corporations large and small. August set a record, $120 billion dollars, for corporate bond issuance according to dialogic, the highest since records have been kept. It seems to us a rather one-sided deal and begs the question: "If corporations are flush with cash, what is the purpose of borrowing more?"

The new issuance should, over time, be a great thing for stock investors. Equity holders will benefit from higher forward earnings due to companies refinancing their current obligations at lower rates and additional funds directed to stock repurchase plans. We currently have 10 companies in the portfolio that have active repurchase programs running, and the economics are compelling. Companies in the portfolio are paying roughly seven times operating cash flow to repurchase shares. Said another way, expressed as yield, they are investing low-cost, borrowed funds from the two pecenters in exchange for a 14.3 percent operating cash flow yield. That should make long-term stock investors smile.

	10 Portfolio Companies with Active Repurchase Programs
Aggregate Market Capitalization	$4.93B
TTM Operating Cash Flow	$721MM
Market Cap/TTM OCF	7X
TTM/OCF/ Market Cap	14.3%

...Why the Midwest? continued from page 1

- Lastly, consider the average age of vehicles on the road (steel and manufacturing), the slowly recovering housing market (labor and manufacturing), or the infrastructure spending that continues to be discussed and lightly executed. These factors are all wildly positive for the Midwestern United States.

DID YOU KNOW?

Almost all of the jobs created in the United States are in firms less than five years old, according to the Kauffman Foundation. Between 1995 and 2005, immigrants started 25 percent of businesses in the high-tech industry, adding about 500,000 new jobs for Americans. Four of the top 10 states hosting international students are in the Midwest: Illinois, Indiana, Michigan and Ohio. Moreover, these states reported the highest growth rates for the number of hosted international students.

What if the United States can award more temporary visas to these would-be entrepenuers?

ON THE ROAD

"Somebody once said that in looking for people to hire, you should look for three qualities: integrity, intelligence and energy. And, if they don't have the first, the other two will kill you."

– Warren Buffet

Otsi Keta Capital took to the road in September to visit with management teams of companies in the portfolio. In keeping with our curious nature, we looked for businesses to enhance the portfolio, too. Our travels took us to Chicago, Columbus and Cincinnati.

Businesses we hold

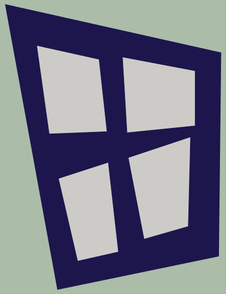
We had nothing but solid meetings with management teams of companies that we currently hold, meeting with no less than the CFO at every stop. This certainly reinforced our opinions on those companies, and also allowed us to comfortably add to some positions. We found all management teams very open to our questions and extremely proud of their businesses. The three management qualities referenced in the quote above shone through in each of our meetings.

Here are some takeaways from the meetings:

- Small, Midwestern companies are not waiting to retool operations or personnel. They all seemed to have a proactive strategy that they were implementing or were about to roll out for 2013.
- Companies are looking to work with the teams that were in place through the downturn. While the businesses we toured had a union component, management and labor appeared to be on a different footing from a few years back. We feel this "refreshed" thinking will benefit the investor (us) and the company.
- To a business, the awareness and familiarity with upper management was apparent as we walked the shop floor with either the CFO or a member of the front office. This kind of relationship, vertically, was good to see at each one of the portfolio's companies.
- We saw a number of new product initiatives that we considered drivers for 2013. We were encouraged with the businesses we saw.

We continue to review ideas throughout the Midwest and find it very valuable to be "on the road." And, just to recap, we do not add positions on a whim or a quick presentation. What we can say is that we have a couple of interesting companies that we have started to accumulate. We currently have a five-to-six company tour in the works for the end of 2012. We'll keep you posted!

The Window Indicator



The 2012 shipping season continues to track as mentioned in the second quarter newsletter. No fewer boats seem to be passing by the window as the summer winds down and we welcome fall. Typically this time of year, the Great Lakes would start to see boats being laid up early for the winter. There has been no indication of that phenomenon.

There are a couple of drivers that help the boats to stay on the water:

1. The water levels continue to stay at 30-year lows. This causes the ships to be lighter when loaded due to water depths in channels and harbors. Essentially, more travel for the same tonnage.
2. The Midwest was blessed with a hot and rather still summer. This allowed for some ideal weather conditions on the Great Lakes. Good weather equals great opportunities to safely transport goods.

We also believe that some commodity pricing has influenced shipping to the positive. It has surprised us that the iron ore trade has remained as robust as it has. Could it be that steel mills are stock piling cheaper commodities in preparation for more robust demand in 2013? We don't know, but it makes us curious to keep looking out the window this year.

OUR PERFORMANCE

For the third quarter ended September 30, 2012, the Otsi Keta Focus Fund was up 3.73%, or 115 basis points less than the Russell 2000 index (see below). Year to date the Fund is up 11.40%, underperforming the same index by 163 basis points. Since inception, the Fund has outperformed the Russell 2000 index by 194 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 the performance of Otsi Keta Focus Fund Limited Partnership.

Fund Name	Morningstar Rating	ROR 2nd Quarter 2012	ROR YTD June 30, 2012	ROR From Inception (May 7, 2010)
Otsi Keta Focus Fund Limited Partnership*	**N/A**	**3.73%**	**11.40%**	**26.52%**
INVESCO Van Kampen Small Cap (VSMIX)	4 star	5.71%	16.05%	25.26%
Royce Special Equity (RYSEX)	4 star	5.65%	11.98%	26.64%
Russell 2000 Index	N/A	4.88%	13.03%	24.58%
Russell 2000 Value	N/A	5.11%	12.59%	16.31%

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

Portfolio Statistics

	OKFF Portfolio	Russell 2000
Price/Perspection Earnings	9.94	15.92
Price/Book Ratio	2.38	1.59
Return on Assets (%)	14.98	3.25
Return on Equity (%)	24.08	8.79
Projected EPS Growth (5-yr %)	13.59	12.91
Dividend Yield (%)	1.34	1.58
Average Market Cap ($mil)	433.12	988.31

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