

Dear Investors,

The Orange Capital Master Fund was down 10.8% for the third quarter 2011. As of November 4<sup>th</sup> the fund is down 9.8% for the year. Since inception in March 2008 the fund is up 73.3% net of fees and trading commissions, that is a cumulative average return of 17.1% per year net of fees and trading commissions.

As of November 4<sup>th</sup> the fund is 5% long, 25% short, the rest in cash.

We misjudged the impact of inflation. Inflation is bad and always leads to a slowdown because people react to prices. When incomes in the US and Europe are stagnant then inflation means less real income and that again means less consumption. We see similar issues in the emerging markets. There, inflation is so rampant that the only way to keep up with real cost increase is to expand credit. The risk in the credit growth in emerging markets is comparable with the subprime debacle in the US, where even more credit is thrown at consumption just to keep the ball rolling. We are concerned about the future development in emerging markets.

The most imminent event is Europe where we expect more carnage and trouble. Europe doesn't have experience in restructuring. On top of it the current situation is exposing past excesses and corruption. We expect Germany to stop financing the Eurozone debt particularly since the main beneficiary is France which over time will become politically unacceptable in Germany. Because the situation is complicated and potentially toxic for the financial markets we decided to stay away from Europe. There are two interesting trades we might consider, one is going long the French-German bond yield spread and the other is shorting short term rates in Europe. But both are rather complicated to implement and given the political sensitivity we cannot rule out massive interference from governments and central banks in the market. We therefore prefer to stay away for the time being.

However, the situation in Spain is relatively more straightforward. The country will have elections soon and the new government has a plan to fix the problems, which is to restructure the economy and pay back the debt. We met a few business leaders from Spain and as opposed to Italy there is much more willingness to tackle the problems and solve them. Within that context we see opportunities in Spanish equities given how far down they have been sold off.

The situation in emerging markets is a little bit more difficult since there are positives and negatives. On the positive side we do recognize the growth and the development of a middle class in many of these countries. But the cost of this growth is increasingly being financed with debt. We don't like that. The most dramatic credit growth is in China. While the country might have foreign exchange reserves China is also running a huge debt load. The key to understanding China is to understand the dynamics between state owned enterprises, state owned banks and the regional governments. It seems to us that most of the debt is being created there and nobody really knows how much debt there is. The interaction between regional governments, banks and developers can easily destroy the fiscal position of the country. Our conversations with Chinese developers are muddy but there are clear signs; first, there is a real estate problem in the first tier cities such as Shanghai or Beijing and second, the financing for new projects is tough to get.

As another strong signal of trouble corruption is rampant in China. Rich people are increasingly trying to park their money outside of the country. This is an indicator for rising instability. We expect real Chinese growth to slow down because of the above mentioned issues and also because of high inflation. This will have an impact on other emerging markets where inflation and credit growth have to

come down. We are short Latin American stocks because we believe China will slow down, the carry trade with the US Dollar will reverse and the credit driven growth in those countries is not sustainable at this point. The stocks trade at very high valuations which neither reflect the risk of a slowdown nor the risk associated with such rapid credit growth.

In the US we are much more positive. If there is a way out of this global financial mess then it is through value creation in the US. We are positive about this. We are therefore focusing on companies and sectors which can grow regardless of the global macro backdrop. There are two big themes which are working in the US.

First, shale oil & gas, energy transportation infrastructure, biofuels, energy efficiency and other technologies to produce or preserve energy are developing. We decided to focus on energy related technology companies which help the US either get more and cheaper energy or save energy consumption. We believe energy will be scarce no matter what happens to the macro environment. Examples are pipelines companies such as Transcanada or service companies such as Baker Hughes. We are still early in this so expect us to talk more about this in the future.

Second, there is income growth in urban centers driven by technology and service jobs. This theme is based on the observation that the growth in urban areas is primarily fueled by the rapid adoption of digital media. As usual with such developments it is hard to pick the winning technologies. It seems much more prudent to us to focus on obvious beneficiaries. Examples of companies that benefit from income growth in urban areas are Starbucks, Whole Foods and Abercrombie & Fitch. Starbucks is interesting because it also benefits from the trend of work away from the office. This is a strong demographic change which in our opinion will continue to fuel growth for Starbucks. The problem with these stocks is that they are already priced for high growth so the risk/reward is not interesting at this point.

In summary, we believe that the world is looking at a prolonged period of zero real returns with capital being wasted at bailing out the debt around the world. The interference of central banks around the world makes investing much more difficult. When the markets collapsed in 2008 there was also massive interference but nevertheless, the asset prices adjusted downwards. This led to the recovery in 2009. This time we are missing a correction in asset prices. The massive intervention by the Fed and other central banks is distorting asset prices and returns for investors. The interference in China is so massive that most corporates are not even making money anymore. You cannot have sustainable markets when failure is not corrected with bankruptcy.

We intend to make money with investments regardless of the global backdrop since the latter is currently impossible to gage.

As usual please feel free to contact us if want to discuss more.

Thanks,

Krim Delko

New York, November 2011