Dear Investors,

The Orange Capital Master Fund returned 14% net after fees in 2009. In the 4th quarter the fund returned 4.32%. Since inception in March 2008 the Orange Capital Master fund returned 38.3% net after fees.

The purpose of this letter is to give you an overview over what we did in 2009 and a basis to understand what we expect from the coming year. Our best guess for the future is the present so we will try to explain our current portfolio and why we chose to work on what we are doing right now. We also think it might be useful to shed some light on our investment process and how we decide to exit positions. Although we don't have a prefixed time horizon we tend to think in a three to six months time frame.

First, let's take a look back to the beginning of 2009.

In our 2008 annual letter we wrote about the bad state of the financial markets. We argued that too much leverage and too much inventories would further hurt asset prices in 2009. Our main positions were short oil and short Potash Corp. We decided to close our shorts by mid February. Closing shorts is much harder than closing long positions since the market usually only gives you a very narrow time frame to do that profitably. We were reasonably successful in doing so.

Our first long buy was the Chilean ETF (ECH) in early February which was driven by the strong fundamentals this country has to offer. We particularly liked the copper and timber exposure Chile offers since it is globally the low cost producer in these areas. We also bought the Russian ETF (RSX), which was much more risky but also more rewarding. Russia has a few great companies such as Norilsk Nickel which was trading at around 3 time projected 2009 Ebitda at the lows. The company is the global low cost producer of Nickel and Palladium with a large copper content. Similarly Gazprom is the largest gas company in the world and was trading at very low multiples.

Although we did well in timing the lows, we did not size our portfolio properly on time. We were only 40% invested when the rally started and it took us until the fall to be fully invested. Our caution cost us some performance. We preferred to wait to see real signs of a recovery before we put money back to work. We needed some time to build enough conviction to take large positions.

Here is a list of the largest contributors to the portfolio performance in 2009:

L'Oreal	+5%
RSX	+4%
ECH	+3%
Oil	+2%
Potash	-1%
Gold	-3%
S&P500 ETF	-3% (this was a short and used as a hedge, we exited this position in July)

We decided to be fully invested around October with exposure to cosmetics, steel, industrial gases, electricity and agriculture. The underlying theme in all these positions is growing demand, high market share and particularly good positioning in emerging markets. L'Oreal is a good example. The company has high margins, great market share in China and on top of that there is a chance that the founding family could sell and hence trigger a transaction with Nestle which already owns 30% of L'Oreal.

Our trip to China in June showed that there is real demand in other parts of the world. The country has interesting demographics and enough capital to fund the need for infrastructure, housing and consumption in that country. We were particularly impressed by how professional Chinese corporates are. Yes, they are driven by the government and make no mistake, this is a centrally planned economy where banks such as ICBC with balance sheets in the trillion dollar range are highly influenced by decisions from the top. But that alone is not a reason to deny China a leading position in the world economy. And even if you don't like the country, you can't go against the numbers.

The Chinese have around 300 million consumers, i.e. people with enough disposable income to buy cars, refrigerators, sneakers and many other consumer goods. The housing starts in China are estimated to be between 400k and 500k units per annum, which is about half of what the US has in a normal year. This number is not sustainable and has to grow. Further, there is a necessity to go vertical, i.e. build more high rises since large populations need space and land is scarce. Hence the myth of overcapacity in China in steel, aluminum and other basic materials is just that; a myth. We believe there is a huge need for more competitive capacity, capacity that can deliver the quality, quantity and reliability of modern infrastructure projects.

One interesting observation we made in China is the notion of sustainable capacity, that is capacity that can be be maintained even with more stringent environmental standards. For example, China has a lot of cement, coal powered electricity or shipbuilding capacity. But more than 50% of that capacity consumes too much energy, pollutes too much and is in no way competitive with state of the art facilities. Viewed from this angle China is in desperate need for capacity in pretty much every basic industry that underpins the country's industrial base. This is the main fundamental reason why we like low cost providers of basic materials such as steel, timber, copper or natural gas.

We mentioned already the housing starts in China which are way too low given the number of households in China. This will drive investments in housing and with that lots of other consumer oriented sectors will grow. The steel companies in China are almost at full capacity. But what is even more powerful is the fact that a lot of the Chinese capacity is obsolete, very inefficient and hence not competitive at current iron ore, coal and energy prices. This is good news for local steel companies with modern facilities such as Baosteel but also powerful for global players such as ArcelorMittal. Another example is cars. While the Chinese are buying about 12 Mio. Cars (including minivans) which is similar to the US, they don't have enough roads to drive on. They consume about one third of the oil consumption of the US and they have about 60 refineries while the US has 180. These numbers illustrate the potential for growth in infrastructure and housing which are fundamental pillars of economic growth.

The potential in the US might be less obvious but the numbers are also compelling. Housing starts are around 700k while family creation in the US is between 1.2 and 1.5 million per year. That spread might stay for a while because of the housing inventory but we are willing to take the bet that this spread won't last for long. Even more important, the capacity to build houses, supply them with furniture and infrastructure has been cut so deeply in the last two years that a pick up in demand will immediately translate into margin expansion and earnings power for the companies involved.

While the media are working hard to scare people off and create a sense of distress in the country the economy is starting to rebound. Retail sales are slightly up year over year and most businesses are planning for a 3% to 5% increase in volumes in 2010. We are seeing encouraging signs in China, where exports are picking up, orders for manufactured goods are up and shipping lines are actually having some capacity constraints because orders are coming in faster than capacity can be expanded. As a result of that air cargo has picked up in December 2009. Hong Kong Airport for example had a 25% surge in aircargo, similar to Frankfurt airport. In Dubai the cargo business at the local airport is at full capacity and our recent visit to the country confirmed that they are very bullish on an upturn in transshipment volumes from Asia to Europe. Also, Shenzhen Expressway, a listed highway operator in the southern Chinese province of Guangdong is seeing double digit traffic growth which is primarily driven by transportation demand for exports. Since many businesses have trimmed down their cost structure in the crisis the margin and earnings leverage is particularly big in the first phase of the recovery.

Given all this we changed some of our positions in the portfolio. We exited Energies Nouvelles and Areva and we concentrated on the remaining positions. We added three new positions, Palladium, Whole Foods and China Cosco.

First let's elaborate a bit more on the exits. Closing positions is almost as important as initiating them. One of the hardest tasks in investing is to keep questioning the portfolio. The key for us to successfully invest in public securities is to buy shares of companies with excellent economics and honest management. We also believe that the price matters. Thereafter all you need to do is make sure those factors remain in place. Our risk management is based on those premises.

Here is an example.

We bought Areva, a French builder of nuclear reactors, because we believed the company has an advantage in the market for nuclear reactors. We also expect more demand for nuclear reactors driven by the so called nuclear renaissance in many countries around the world. While the latter is still true, we had to give up on the former part of the thesis. Areva is actually not that well positioned since competitors from Korea won important contracts in the United Arab Emirates which we thought Areva should win. We also didn't get a satisfactory explanation from Areva for why they lost the contract and we hence concluded that the business is simply not as competitive as we thought. The economics of the business changed and we decided to get out.

Now let's talk about some of our new investments.

Palladium is a precious metal in the same group of metals like Platinum. Its main use is for catalytic converters. The interesting thing about Palladium is that it does almost the same job as Platinum but it's about 3 times cheaper. There is lots of talk in the industry that the metal might appreciate and close the gap with Platinum. We like the economics of Palladium particularly because a large part of demand growth is coming from China. The Chinese will have to use more precious metals to reduce emissions and Palladium is cheaper. Hence there is more potential for Palladium to pick up in price.

There is only one feature we don't like about Palladium and that is that it is partly driven by the Gold price. We don't like Gold and don't want to be long so we are short Gold in the same amount as we are long Palladium to hedge against the Gold price impact on Palladium. We bought Palladium at 389 and shorted Gold at 1100. Historically the relationship of Gold to Palladium was around 0.5. We believe we can at least get there if not higher.

We bought Whole Foods for one simple reason. It is the best food retailer in the US and possibly in the world. The company sells good food at reasonable prices. Their stores are more than just retail outlets, they are events and real estate prices usually go up wherever Whole Foods opens a store. We bought the stock at 24 when it was pricing a moderate growth with little margin expansion. We believe that gives us enough margin of safety and upside to justify a large position.

Our current positions are:

L'Oreal
Air Liquide
Monsanto
Whole Foods
EDF
Arcelor Mittal
Palladium
China Cosco
Africa Oil
Gold (this is a short position)

As of the end of 2009 we are fully invested and primarily long the market. Our only short position is Gold. Before we talk about what we are working on right now we'd like to give you the main themes that drive our investments.

First, the steep yield curve in the US is good for the market. The Fed is holding short term rates low to encourage banks to make money and start lending and investing. That is traditionally a very good indicator for rising asset prices. We expect the Fed to keep the rates low and the curve to steepen even further. This will help the rally continue.

Second, China is in good shape and has all the ingredients for economic growth. Demographics, access to capital and the need for investments will keep economic growth in China elevated.

Third, we are more optimistic about the US consumer. Even though it might take another two or three quarters until we see a real recovery in jobs and retail sales we believe the current assets prices are favorable. Hence there is a lot of upside once the US consumer turns.

Now let's talk a bit about what we are working on right now and our near term priorities. We just returned from a trip to the Middle East where we met with a number of corporates in Dubai, Abu Dhabi and Qatar. We like Qatar as a low cost producer of Liquid Natural Gas (LNG). The country reminds us of Chile, another low cost producer of raw materials (copper and timber). The key to the Qatar investment case is that they are the low cost producer of LNG. But more importantly we feel there is sustainable policy in place in Qatar which will avoid some of the excesses in other Gulf countries. We like their banking and real estate sector. Gas is off the charts for now since they are not willing to share the equity with international investors but we see opportunity in banks for example.

Here are some numbers to explain why we like LNG and Qatar specifically. Qatar will soon produce around 77 million tons of LNG per annum, that is about 40% of the world market. With the expected growth of LNG that share will shrink since Qatar will not expand for a number of years. But the key to the positive economics of Qatar is the fact that the capacity is built at much lower cost than any new capacity. We believe their cost per ton of capacity is between 500 and 750 Mio. USD per ton. That is way much lower than the current 1000-1250 per ton that new capacity will cost. Hence Qatar enjoys the low cost advantage. A few words on the demand side. The demand for natural gas is driven by two factors. First, the increasing demand for electricity is going to drive demand for gas as a fuel and second, the need to reduce CO_2 or simply not burn coal will bring additional demand to the table. Having seen the necessity for energy in China and even the Middle East we are strong believers in the increased demand for natural gas and we believe that buying into businesses in Qatar is a very good and profitable way to get exposure to that.

Some more operational points.

In 2009 we spent 22 bps on commissions. We spent another 34 bps on interest which comes primarily from our currency trades. For those who want a more detailed analysis of trading costs please give me a call and I will go over it.

We increased our concentration in the portfolio and we intend to keep it that way. It helps us manage the risk and understand our exposure much better.

We are in the process of registering with the New York State regulator. This registration will further enhance our transparency and make it easier for us to sign up new clients through the Interactive platform. The registration should be done by the end of the second quarter.

We are also looking to expand our platform to Switzerland. This should give us more flexibility and help us enhance our offering to clients.

As always, we appreciate any feedback and comments. Feel free to pick up the phone or meet with us.

Thanks,
Krim Delko

New York, January 2010