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First Quarter 2012 Letter

Dear Friends,

Global equity markets remained extremely bullish since October 2011. Most US indices were up 10%+ in the first quarter of 2012. Motiwala Capital completed its first year of operations. At the end of the quarter, assets under management (AUM) were about $1 million. All accounts are of friends and family and we appreciate the trust placed in my firm. I have invested a six figure amount which is 90% of my liquid net worth in the same investments as my clients. As a reminder, we manage separate accounts and not a single commingled fund.

Portfolio activity - Summary

We had another busy quarter. Our portfolio is broken up into two parts. The bulk of the portfolio is invested in long equity positions we refer to as "*Generals*". These investments are made with a longer time horizon. We initiated four new positions and closed two. One portfolio company (GME) initiated quarterly dividends and is now fully debt free. We also added to four existing positions and reduced two positions. We ended the quarter with 15 positions.

We initiated eleven new special situations in the quarter and subsequently closed seven of these for modest gains. We received cash payment for three special situation positions from the previous quarter.

Portfolio activity - Detailed

Generals: 2 closed, 2 reduced, 4 new positions, 4 increased. Ended with 15 positions.

Portfolio exits: We closed our positions in Bolt (BOLT) and Gravity (GRVY).

We initiated our position at $1.2 per share in the last quarter. In our Q4 report we wrote "*While investors have been disappointed, at the price we took the position we feel there is limited downside.* ***Shares trade significantly below cash and securities held on the balance sheet***". As the company launched private and public beta testing for its next generation game, the price appreciated strongly. We exited as the share price moved from trading significantly below cash to near cash levels. We booked a 40% gain in the stock. We sold early and the stock rose 50% since our sale. While one can be upset at selling too early, we would gladly take 40% gains in such a short period of time. This business is often one of disappointments – you don't buy enough or you buy too much too early or you sell too early or you sell too late or you sell too much too soon…you get the point!

BOLT appreciated strongly on the special dividend announcement. We took smaller gains in this medium size position as we were not very sure about the acquisition Bolt did a few quarters back. We exited around $13.2. Our total return (capital appreciation + dividend) was ~15%. Bolt went on to announce a regular dividend as well and shares have held up pretty well with oil prices continuing strong north of $100/barrel.

New positions: We added four new positions to the portfolio in the quarter.

We often hear commentators talking about valuations of entire markets and comment that the markets are undervalued or overvalued. At Motiwala Capital, we invest in one company at a time. We look to buy good quality businesses (strong balance sheets, consistent free cash flow generation, high ROIC) at attractive valuations.

For two of our new positions, we went across to Europe (through US ADRs). We purchased positions in primarily UK retailers Tesco and Halfords. The other two positions were companies headquartered in the US. Shares of Iconix Group came under pressure after the company announced Q4 and 2011 earnings and issued guidance for 2012. While Lear shares were not purchased at the lows seen in last fall, we feel the shares trade at a significant discount to their fair value and also to the industry despite having one of the best balance sheets in the industry.

Lear Corporation (LEA) is a leading global supplier of automotive seating and electrical power management systems. Lear came out of bankruptcy in late 2009 with a solid balance sheet and closed down under performing operations. With 100 million shares outstanding and a share price of $46, Lear has a market cap of $4600 million. Lear has $1 billion in excess cash on the balance sheet and will generate FCF of $400 million. Lear returned excess cash to shareholders in 2011 via buybacks and dividends and plans to do more of the same. We think Lear should continue to do well as the demand for cars/trucks should be robust as world economies improve and the average age of cars in US is about 11 years.

Tesco Plc (TSCDY) is one of the world's largest retailers with operations in 14 countries including UK, South Korea, Thailand, China, Japan and the US. In FY 2011, Tesco had sales of £61 billion and generated profit before tax of £3.5 billion. Tesco had a market cap of £26 billion with a P/E of 10x and a dividend yield of 4.5% (that has grown for many years). Tesco owns about 75% of the land beneath its stores and this acts as a large margin of safety for our investment. Tesco has stumbled recently in the UK market but it has a leading market share of about 30%. Tesco is also growing rapidly and profitably in Asia and is number one in Thailand and South Korea.

Iconix Brand Group (ICON) is a brand management company that has a portfolio of 27 different brands. Their brands do roughly $12 billion in sales at the retail level. Iconix receives royalty payments from its partners for these sales. It has a superb business model with no inventory, no manufacturing, no capex -- an extremely asset light model producing strong free cash flow and high operating margins. In FY2011, ICON had revenues of $370 million and generated $180 million in FCF. ICON has more debt than we usually like in our investments. However, with the stable FCF, interest is well covered and Icon could chose to pay off the debt in 2-3 years if it wants to. We purchased ICON at P/FCF of 7x and think there is lot of room for growth as it increases partnerships globally.

Halfords Group Plc (HLYDY) is the UK's leading retailer of automotive and leisure products and leading independent operator in garage servicing and auto repair. Halfords has 467 retail stores in the UK and 250 car repair centers. Last year, Halfords had sales of £870m and generated operating profit of £130 million. Halfords has excellent share holder friendly management and pays out 50% of profits in the form of dividends. Last year, Halfords began to buy back shares aggressively and spent £59m by the end of December 2011. Halfords has a market cap of £600 million and enterprise value of £740 million. Despite some headwinds over the next one or two years, we feel the business is resilient and should continue to reward long term shareholders over time. Halfords has a P/E of 8x and dividend yield of 7%.

Reduced positions:

We reduced our positions in Big Lots (BIG) and Western Digital (WDC) as the stocks appreciated strongly and closed in on our initial target prices. See Appendix for a discussion on Big Lots which is one of our biggest winners so far.

Increased positions:

We added to four existing positions as either a falling share price made valuation attractive in the case of GME and UFPT (before the recent run-up) or despite higher prices, our confidence in the company increased after owning them for a period of time in the case of CSGS and CNRD.

Special Situations: 11 new positions (4 open, 7 closed), 3 positions from Q4 closed

Some of you may be wondering how come we take so many positions in these so called "Special Situations" and what are they. Special situation is a term used for any investment that has an ongoing corporation action of some kind that can unlock value. These could range from bankruptcies, spin offs, mergers, split offs, tender offers. So far, we have ventured in mergers and tender offers. Spin offs are in vogue off late but we have not yet participated in any of them --- there is only so much time in a day! However, we do own Abbott Labs (ABT) which has announced its own spin off, so we are participating before most others and already have a decent gain ☺

Share tenders – 3 positions closed from Q4 2011

You may recall that in Q4 2011, we participated in four cash tender offers. We had already received cash payment for CRFN for a 5.5% gain. In January, we received cash for tendering our MCCK shares for a 13.6% gain. The two other tenders in progress at the end of last year were Nathan's Famous (NATH) and Seaspan (SSW). We received cash payment for these shares for a 5% and 15% return respectively. SSW shares are up sharply since the tender closed and we were intrigued to know that a Canadian Value Investor we follow was not going to tender his shares. However, we bought the shares as a special situation and kept our discipline and pocketed our gains.

Merger arbitrage – 2 positions, both closed.

Inhibitex (INHX) was being acquired by Bristol Myers (BMY) in an all cash transaction. There was no financing risk and we did not feel there would any anti-trust issues. The only concern was if something were to go wrong during the period of the tender offer. Having seen the Gilead Sciences acquisition close, we felt the probability of this one going through would be very high. To be clear, we acquired our shares after the deal was announced. The tender closed on time and we earned a 6% return for our shares of INHX.

Baldwin Technology (BLD) was being acquired in an all cash deal. We initiated the position as the spread reached double digits. However, as we realized that the payment per share (if the deal went through) was uncertain (unlike the INHX merger), we exited the position for a small 2% gain. The merger eventually closed at the high end of range (another 8% upside) but we do not harbor any regrets.

Closed end fund tenders – 1 position, closed.

We purchased shares of Korea Equity Fund (KEF) with the intention to participate in the tender offer. However, as the spread narrowed prior to the close of the tender and with better opportunities in other tenders, we exited the position for a small gain.

Share tenders – 8 positions, 4 closed, 4 active

Share tenders are similar to the closed end fund tenders above. However, in this case the underlying investments were equity positions v/s closed end funds. It seems it was raining tenders in this quarter! We participated in eight cash tenders. We initiated and subsequently closed our positions in Mastech Holdings (MHH), Hackett Group (HCKT), Weight Watchers (WTW) and FBL Financial (FFG) for an average 4% gain. Four tenders are in progress and we will disclose their outcomes in our next quarterly report.

The main attraction of this Special situation portion of the portfolio is the ability to cycle through many positions in a short definite period of time – albeit for smaller % gains and hence contribute in a meaningful way as a group to the performance of the portfolio. Also, these investments are not correlated with the rest of the market. As long as we can find good opportunities, we intend to continue investing in this area.

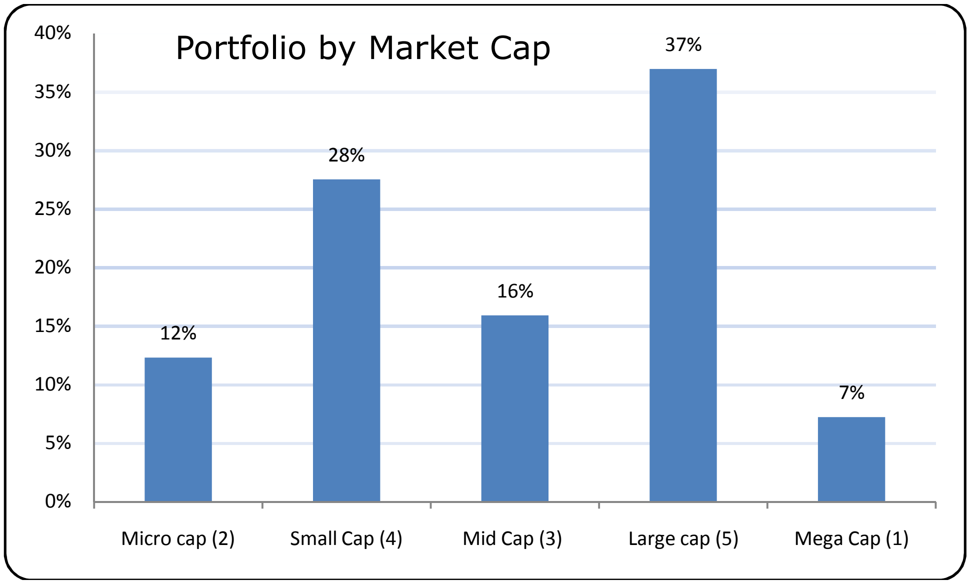
Discussion on Portfolio composition

If you have followed us from the beginning, you would have noticed we have been building our portfolio slowly over the last twelve months. We currently have 15 regular positions (Generals) in our portfolio. This makes up about 70% of the portfolio. The rest of the portfolio is currently in special situations or cash which can vary at any time. The top 10 positions add up to 52% of the portfolio.

<u>Portfolio Characteristics</u>
Weighted average P/E = 13.1 (Average P/E is 12.4) P/E are based on 12-month trailing earnings
Generals dividend yield = 2% (1.4% on the entire portfolio)
Weighted average Market Cap = $43 billion (Avg market cap is $39 billion)

<u>Current Portfolio</u> (some clients will not have all the positions and in the same weights)

Company name (Ticker)	% of portfolio
Aeropostale (ARO)	8.5%
Vodafone (VOD)	5.7%
Conrad Industries(CNRD)	5.5%
Western Digital (WDC)	5%
Abbott Labs (ABT)	5%
Tesco (TSCDY)	5%
Microsoft (MSFT)	5%
Gamestop (GME)	4.5%
Becton Dickinson (BDX)	4.5%
Iconix Group (ICON)	4%
UFP Technologies (UFPT)	3.5%
CSG International (CSGS)	3.5%
Halfords (HLFDY)	3%
Big Lots (BIG)	3%
Lear Corp.(LEA)	3%

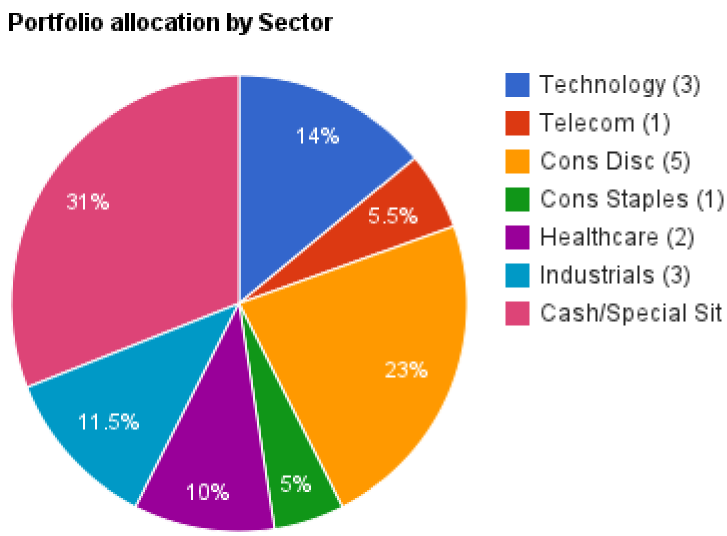


This is our portfolio split into different market cap buckets. The numbers in brackets are the number of positions in that bucket. For our purposes, we defined

Microcap – less than $250m
Small cap - $250m to $2billion
Mid cap - $2billion to $10billion
Large Cap - $10 billion to $200 billion
Mega Cap - $200 billion +

As you can see, we have invested across the market cap spectrum. We are market cap agnostic. Our smallest company (Conrad Industries) has a market cap of $100 million and the largest is Microsoft with a market cap of $273 billion. While there is no conscious attempt to diversify across market caps, we certainly like having a good mix. The large caps add stability to the portfolio in times of distress and have solid competitive positions. However, the large caps like any other investment still have to meet our criteria of quality and cheapness to be considered for the portfolio.

If you like pie charts and sector allocations, the next chart is for you.



We do not go out seeking specific investments by sector. We make our investments one stock at a time. However, as part of risk management, we do want to make sure all of our investments are not in just one or two sectors. Currently we do not have any investments in 4 sectors – Materials, Energy, Financials and Utilities.

We would like to thank our clients for placing your trust in us. We are looking to grow our client base and we welcome referrals. If you have an interest in us managing a part of your investment capital, please feel to call me to have a discussion.

Sincerely

Adib Motiwala
Portfolio Manager
Motiwala Capital

Appendix: **Big Lots (BIG)**

We purchased shares in Big Lots in Q2 2011 at an average purchase price of $32. The company had a market cap of $2400 million with 75 million shares outstanding. Big Lots had an excellent balance sheet with $284 million in net cash (12% of market cap). With trailing EPS of $2.85, BIG sported a P/E of 11 (ignoring excess cash) and EV/EBIT of 6x. Pre-tax return on Invested Capital (ROIC) averaged 30-32% for the last three years. Free Cash Flow (FCF) in the previous year was $208 million.

Clearly, Big was cheap on valuation, a good business as seen by ROIC and free cash flow and had an excellent balance sheet. The management team led by Steve Fishman had done a tremendous job since 2006. It checked all the boxes we look for in an investment. There was no identifiable catalyst in sight. As they say in India, it was just "*Sasta" – or cheap.*

In FY 2011, BIG spent $359 million on the repurchase of a whopping 11 million shares or 15% of the shares outstanding at an average price of $32.8 per share. This gave a nice boost to EPS which came in at $2.98 per diluted share. Big Lots made an acquisition in Canada to make it first international expansion. While the acquisition was and will be a drag on results in the short term, BIG paid only 13 million CAD for 92 stores of Liquidation World at a valuation of 0.1x sales. The EPS increase (which would have been even more without the aforementioned drag) combined with the re-rating of the stock from 11x P/E to 15x P/E meant we had a nice 40% return on the stock ($32 to $45). We trimmed our position at $41 and still hold a 3% position. We feel the company can reward share holders with a double digit return going forward from here.

Here are summary financials for Big.

Fiscal Year	Sales	Op Income	Net Income	Diluted EPS	OCF	Capex	FCF	Shares
2006	4,430	30	(10)	0.14	213	(67)	146	113.7
2007	4,743	185	124	1.01	381	(32)	350	111.9
2008	4,656	236	158	1.47	308	(60)	248	102.5
2009	4,645	255	152	1.89	211	(90)	121	82.1
2010	4,727	316	200	2.44	392	(78)	314	82.7
2011	4,952	357	223	2.83	315	(107)	208	78.6
2012	5,200	358	207	2.99	320	(120)	200	65

Note: All figures in millions except for EPS.