Motiwala Capital LLC
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Second Quarter 2013 Letter

Dear Investors,

The second quarter of 2013 ended with the S&P 500 up ~3% in the quarter. For the first half of 2012, S&P 500 was up 13%. On a consolidated basis, Motiwala Capital accounts returned ~15% even while cash levels remain high. Accounts that have been with us for a year or more are 70% invested whereas accounts opened in 2013 are anywhere from 50-60% invested. With a sharp rising market, we have been selling and paring down positions. The consolidated performance information is shown in the table below:

Year	S&P 500	Motiwala Capital
2011*	-1.7%	**4.9%**
2012	16.0%	**20.3%**
YTD 2013	12.6%	**14.9%**

See important notes at the end of the letter for more information

Portfolio Composition

Our portfolios are divided into two sections. The 'Generals' are equity investments that fit the value framework. The rest of the portfolio is currently in special situations (short term investments with a specific event that unlocks value) or cash which can vary at any time.

Portfolio Activity

Special Situations: Share and Closed End Fund (CEF) tenders

We participated in eight special situations in the quarter which included one CEF tender, one merger arb (described below) and six company tenders. Five out of the six closed positions yielded profits and one resulted in a narrow loss.

Special Situations: Merger Arbitrage

Indian car tire manufacturer Apollo Tyres (APTY:IN) announced a leveraged acquisition of US listed Cooper Tire & Rubber (CTB) worth $2.5 billion or $35/share in an all cash transaction. After the first day pop where CTB shares closed at $34.7, shares started trending down. We bought our initial position in CTB around $31.3. Shares of Apollo came under intense selling pressure with the stock tanking from Rs 100 to Rs 55. Taking significant debt to make acquisitions is always frowned upon in India, especially when the acquirer is much smaller than the target. So, maybe the market feared that the deal would not go through due to financing or some other reasons. Being a commodity business, I do not see any regulatory risks. Apollo has obtained committed debt financing for the transaction. The combined company would be 7^{th}

largest tire manufacturer. In a day or two, CTB shares reversed course and the spread which had ballooned to 15% is now under 5%. We continue to hold the position at the time of writing.

We had two merger arbitrage positions going into the quarter. We closed both positions for low single digit % losses. In the case of the first one, the merger went through but it was a stock swap transaction and unluckily both stocks moved down. We closed the position soon after the merger closed. The second position was the pending all cash acquisition of Arbitron (ARB) by Nielsen Holdings for $48/share. The merger has been delayed and the risk reward did not seem attractive to continue holding. In retrospect, the spread was much lower to begin with (~3%) and would have been only worth if the deal would have closed in a timely fashion.

<u>Generals: Portfolio exits</u>: We sold out of four positions in Q2.

GameStop (GME) was one of the first stocks we purchased in 2011 around $19. We held it for a little over two years. As you can see in the chart below, it was not an easy stock to own. While the management did an excellent job allocating capital over this difficult period for the entire video game industry, the stock was out of favor and one of the most heavily shorted stocks. GME generated heavy free cash flow ($450million in a $2billion market cap), paid off all debt, initiated and raised dividends, repurchased over a billion dollars of stock during this time. Finally, GME made a rapid and steep ascent and we sold our shares between $32-$34 range. The stock closed recently ~$43.

Aeropostale (ARO) – We purchased ARO for our first few accounts in early 2011 for $24. The outcome in ARO was totally opposite to that of GME, both business performance and stock performance wise. ARO continued to report one bad quarter after the other. The other reason to exit the stock is the management. I have not seen worse results in retail. On about the same sales base of $2.4 billion over the last three years, net income has gone from $230 million to $69 million to $35 million. Luckily, shares in most accounts were purchased $13 and ended in the black. We sold our shares after another horrible quarter report at $15.5.

Dolby Labs (DLB) – Dolby was a recent purchase. Sales have been stagnant in the face of declining licensing revenue from PCs, DVD and Blu-ray players. Revenue from mobile devices have not offset the overall decline in profits. We have exposure to PCs via MSFT and WDC already and it seemed prudent to reduce this overlap and book a quick short term gain.

Halfords (HLFDY) - Halfords is the third retailer to exit our portfolio. A new CEO had taken the helm at Halfords a few months back. In the year end call, he announced that the business needs investments and will be a 3 year turnaround. We did not sign up for that. Halfords seems fairly valued given the fundamentals - declining cash flows, profits and reduced dividend. We sold for small total return (~10%) after a year of ownership. The large dividend rescued the outcome.

Generals: New Positions:

We purchased four new positions. On one end, we purchased one of the largest companies in the world. And on the other end, we purchased three micro caps all under $100 million market cap.

Apple (AAPL): During the last two years, we watched Apple shares soar towards $700 and then decline even faster towards $400. Everyone knows about Apple – their iconic products, their late CEO Steve Jobs. Over the last few months, the mood of market participants went from one extreme to the other. Last summer, they could do no wrong and now they cannot get anything right. I believe the truth may lie somewhere in between. Anyways, let's just consider the numbers alone

- Market cap $375 billion (at purchase price ~$400/share)
- Balance sheet - $144 billion in cash and investments (majority of which is held overseas)
- Capital allocation – total $100 billion (yes billion) capital return program, $60 billion buyback, $12.2/share annual dividend yielding 3% dividend yield.
- Free Cash flow - $40 billion last year

We also get
1) market leading positions for their products and history of innovation
2) Low valuation given all of the above.

There are risks as well such as short product cycles, high competition, low barriers to entry and obsolescence risk faced by consumer facing technology products. However, we think there is value here especially in the balance sheet and capital allocation plan.

Amcon Distributing (DIT): Amcon is a wholesale distributor of consumer products such as cigarettes, candy, beverages, groceries, paper products, automotive and health and beauty products. It serves approximately 5,000 retail outlets such as convenience stores. In addition, the company operates fifteen retail health food stores in Florida and the Midwest.

This is a relatively simple but boring and low margin/high scale business. In 2012, on $1.17 billion in sales, the company generated gross profit of 'only' $79million and operating profit of $13 million. At our purchase price of $70, the market cap was $45 million. What attracted us to DIT? Low valuation, management and capital allocation. Since CEO Mr. Atayan took over in 2006, he has remarkably turned around a once floundering company. Book value has grown from $9.94/share at the end of 2006 to $67.54 in 2012. Debt declined from $63 million to $21 million. EPS has gone from $1.6 in 2006 to $9.4 in 2012. The company generates an average free cash flow of $8million annually and uses it to pay down debt. Value has transitioned from debt to equity and we estimate that entire debt could be paid off in three years. Despite this track record of value creation and capital allocation, DIT continues to trade at a low valuation due to reasons that may be applicable to many microcaps: small market cap, low float (only 630K shares outstanding and even less available for trading), extremely thin trading volume (avg daily volume of 1500 shares or $120k).

The other new positions may be discussed in future letters. We are still building positions in these companies.

<u>Generals: Reduced positions:</u>

Guru investors tell us to sell when things are rosy and cheerful which has certainly the case this year. We also sell when share prices appreciate close to our estimates of fair value and for portfolio management reasons (portfolio sizing, reduce overlap). In the quarter, we pared down positions in Western Digital (WDC), Big Lots (BIG), Microsoft (MSFT), Lear (LEA), Vodafone (VOD), and Kohls (KSS).

<u>Generals: Increased positions:</u>

We added to our positions in Tesco Plc. (TSCDY), MIND C.T.I (MNDO) and Big Lots (BIG). All of these came down in price after the companies announced earnings. In the case of Big Lots, we were trimming the position into earnings and we were able to buy back the shares after a 15% decline.

<u>One Baggers</u>: Peter Lynch coined the word ten-bagger to refer to a stock that was up ten fold. After two years, we had three stocks that doubled from our initial purchase. Two of them doubled with us (Western Digital and Conrad Industries), while we parted ways with GameStop before the double. As you can see in the chart for Western Digital below, it was also not an easy stock to hold. On three occasions, we had paper gains of ~30% which vanished. We did not sell as we believed in our valuation. The fourth time we had a 30% gain, we reduced the position. After a two year period, finally the market rewarded us for our patience. We have been reducing the position into strength.

Other news

For the second year running, I participated in the annual Ira Sohn stock pitch competition and my submission made it to the semi-finals. The free ticket offered to semi-finalists let me attend the excellent conference in NYC.

I also attended the superb 3 day conference-cum-vacation ValueX Vail organized by Vitaliy Katsenelson. It was a blast to meet so many smart investors in a private setting. I highly recommend this conference if for nothing then just to visit beautiful Vail, Colorado.

We wanted to thank all clients for their faith shown in us. We would welcome referrals to like-minded investors. If you have any questions or comments, please don't hesitate to contact me.

Sincerely,

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