GREY OWL
CAPITAL MANAGEMENT

August 1, 2012

"If something cannot go on forever, it will stop."
- Herbert Stein

Dear Client,

Performance across all of Grey Owl's investment strategies was reasonable in the second quarter. Our bent toward higher-quality businesses, exposure to income-producing securities, and large cash holding enabled our equity portfolios to better protect capital as broad market indices turned down. Fixed income portfolios showed positive gains but lagged the Lehman Aggregate Index given its greater than 70% exposure to US government and government-backed mortgage debt (which, for now, still behave as "risk free" investments during times of economic stress). Our partnership vehicle[1], which utilizes a similar investment process to Grey Owl Opportunity Strategy but with broader flexibility, showed a modest gain for the quarter.

Here is the standard performance table for Grey Owl Opportunity Strategy as of June, 2012[2]:

	Q2	YTD	TTM	Cumulative Since 10/06
Grey Owl Opportunity Strategy (net fees)	**-1.93%**	**6.00%**	**0.37%**	**29.60%**
Spider Trust S&P 500 (SPY)	-2.75%	9.49%	5.45%	11.74%
iShares MSCI World (ACWI and MXWD)	-5.74%	5.51%	-6.79%	2.02%

[1] Grey Owl Partners, LP is only available to accredited investors. Positive returns from short positions and a higher percentage of fixed income investments outweighed equity and option losses in the quarter accounting for the majority of the difference between Grey Owl Partners, LP and Grey Owl Opportunity Strategy.
[2] For more information regarding performance, please refer to the performance disclosure at the end of this letter.

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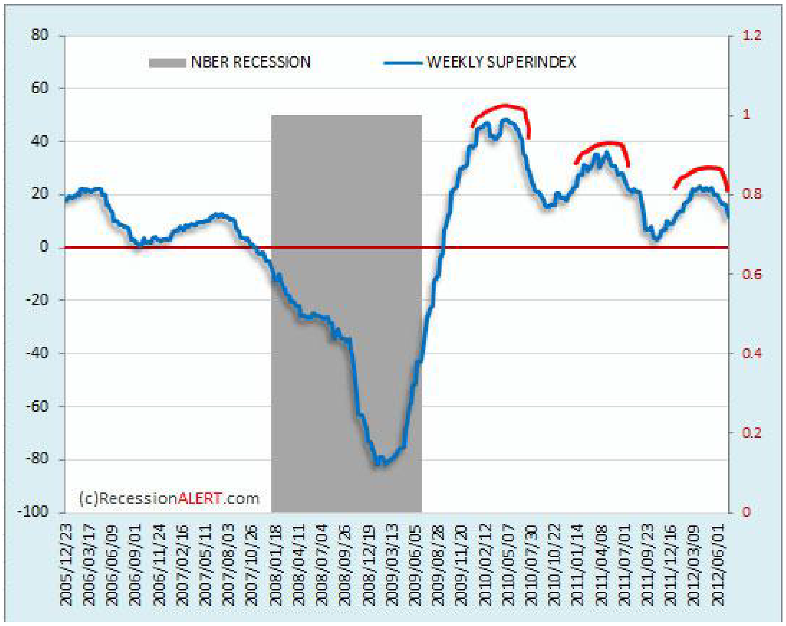
Over the past few years, we have made a conscious decision to minimize risk-taking across all of our investment platforms. The rationale is quite simple. We believe the economic “recovery” rests on shaky ground: unsustainable government fiscal deficits and unsustainable central bank money printing. As such, we will spend the bulk of this letter reviewing the current climate instead of delving into specific positions.

While the stock market meets every hint of further monetary accommodation from either the US Federal Reserve Bank or the European Central Bank like a breath of fresh air, absent real reform, we are forced to quickly hold our breath as the wheel plunges us back into the water. Business fundamentals continue to decelerate and the stock market is prone to rapid sell-offs. Today, investors’ broad choices include a stock market (i.e. the S&P 500) trading within 10% of its 10 year high and 10-year US Treasury bonds offering a nominal return under 1.5%. A few weeks ago, 10-year Treasury yields were lower than during the Great Depression. One market prices in growth, the other stagnation. The incongruities don’t stop there. At the last TIPS (Treasury Inflation Protected Securities) auction on July 19th, investors were willing to PAY Uncle Sam 0.64% per year to hold their principal and protect them from inflation above 2% annually for the next 10 years. These are interesting times.

Not only are the fiscal deficits and money printing unsustainable, they have become progressively less effective. Each new round of money printing has had a weaker impact on broad equity markets as depicted in the graph below.[3]

[3] The line is the price level of the S&P 500 broad market index. The shaded boxes represent each distinct round of major central bank balance sheet expansion. Notice that the trough to peak change in the S&P 500 decreases with each subsequent round.

Additionally, each round of central bank intervention has had a lesser impact on a broad index of economic fundamentals.[4]



In fact, US labor markets only appear to have improved at all (i.e. the "unemployment rate" has gone down) because fewer citizens are seeking employment. The drop in the labor participation rate has not once broken the decline begun in late 2006.[5]

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[4] The SuperIndex is a compilation of eight leading and coincident indices, some of them compilations in their own right. The graph depicts the fact that each subsequent round of central bank intervention has caused a short-lived improvement in underlying economic fundamentals but to a lower high. This graph is from a freely available blog post at www.seekingalpha.com We subscribe to RecessionAlert: http://recessionalert.com/ which is the source of the data.

[5] Since 2006 the percentage of the population of working age that is employed has decreased from the mid 66s to the high 63s.

Thus, growth in real (i.e. inflation-adjusted) personal income has been (only barely) supported by transfer payments (e.g. social security disability, extended unemployment insurance).

With personal income growing at a tepid 1.1% annualized rate, the US economy is quickly decelerating. It is true that broad US equity indices derive a significant percentage of their sales outside of the US. Unfortunately, that is no salve: Europe and China are slowing as well and Europe's Purchasing Managers Index (PMI) is well below the 50 value that divides growth and contraction while China's PMI has decelerated to the 50 level.[6]

[6] Purchasing Managers Indices are diffusion indices based on polling results of business purchasing managers. The managers are asked to indicate whether conditions across several metrics are better or worse than the prior month. Below 50 indicates an average response that is worse and thus signals a slowing economy.

All of this warrants caution. Thus, we are positioned as follows:

- **Equity accounts.** Our largest positions are excellent businesses with sustainable competitive advantages (i.e. business "moats") and low leverage. We also hold short-dated income-producing securities, gold as a hedge against further monetary intervention, and a significant cash position.

- **Fixed income accounts.** We continue to limit exposure to rising interest rates by keeping maturities relatively short. While slower growth and a "flight to safety" during tumultuous events can keep the 10-year US Treasury below 1.5% in the short-term, we do not believe the yield adequately compensates investors for the possibility of inflation and/or a credit rescoring (see Spain and Italy for examples of the speed at which credit markets can re-price risk). At this point, we choose to take modest credit and foreign currency risk as a means to increase prospective returns.

- **Grey Owl Partners, LP.** Like our equity accounts, our partnership is concentrated in excellent businesses. Given its more flexible nature, we have also been able to acquire a much broader array of shorter-dated corporate credits as "cash alternatives." In addition, our ability to short has helped to mute volatility and enhance returns. For example, we have benefited from short exposure to both high-cost producers of basic materials that have suffered as China has slowed and US-based casino operators with exposure to the most saturated gaming regions.

As a final note, we would like to wish Valori (Infanger) Perry good luck as she moves to England where her husband is pursuing an advanced degree. We don't always get our timing right, but in this case we got pretty close. Val's departure lined up perfectly with the closing of a long-tenured local investment firm, Growth Stock Outlook. With 29 years of experience in operations, compliance, and research, Janet Rakoczy is sure to be an outstanding addition to our team.

Val headed out on June 30th and Janet joined us on August 1st, making July a long month. Needless to say, we are really excited to have Janet on board and we look forward to you meeting her.

As always, if you have any thoughts regarding the above ideas or your specific portfolio that you would like to discuss, please feel free to call us at 1-888-GREY-OWL.

Sincerely,
Grey Owl Capital Management
Grey Owl Capital Management, LLC

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The securities discussed above were holdings during the year ended December 31, 2011. The stocks we elect to highlight each quarter will not always be the highest performing stocks in the portfolio, but rather will have had some reported news or event of significance or are either new purchases or significant holdings (relative to position size) for which we choose to discuss our investment tactics. They do not necessarily represent all of the securities purchased, sold or recommended by the adviser, and the reader should not assume that investments in the securities identified and discussed were or will be profitable. A complete list of recommendations by Grey Owl Capital Management, LLC may be obtained by contacting the adviser at 1-888-473-9695.

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For additional information about Grey Owl, including fees and services, send for our disclosure statement as set forth on Form ADV using the contact information herein. Please read the disclosure statement carefully before you invest or send money.

The performance information for the Grey Owl Opportunity Strategy presented in the table above is reflective of one account invested in our model and is not representative of all clients. While clients were invested in the same securities, this chart does not reflect a composite return. The returns presented are net of all adviser fees and include the reinvestment of dividends and income. Clients may also incur other transactions costs such as brokerage commissions, custodial costs, and other expenses. The net compounded impact of the deduction of such fees over time will be affected by the amount of the fees, the time period, and the investment performance. Grey Owl Capital Management registered as an investment adviser in May 2009. The performance results shown prior to May 2009 represent performance results of the account as managed by current Grey Owl investment adviser representatives during their employment with a prior firm. THE DATA SHOWN REPRESENTS PAST PERFORMANCE AND IS NO GUARANTEE OF FUTURE RESULTS. NO CURRENT OR PROSPECTIVE CLIENT SHOULD ASSUME THAT FUTURE PERFORMANCE RESULTS WILL BE PROFITABLE OR EQUAL THE PERFORMANCE PRESENTED HEREIN. Different types of investments involve varying degrees of risk, and there can be no assurance that any specific investment will be profitable. For additional performance data, please visit our website at www.greyowlcapital.com.

The indices used are for comparing performance of the Grey Owl Opportunity Strategy (“Strategy”) on a relative basis. Reference to the indices is provided for your information only. There are significant differences between the indices and the Strategy, which does not invest in all or necessarily any of the securities that comprise the indices. In addition, the Strategy may have different and higher levels of risk. Reference to the indices does not imply that the Strategy will achieve returns or other results similar to the indices. The performance shown for the iShares MSCI World Index Fund (“Fund”) includes performance of the MSCI World Index prior to March 26, 2008, inception date of the Fund.