SOUTHPAW CAPITAL

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Dear Partners,

For all the ups and downs over the last few months, the market indices finished about where they started with the total return on the S&P 500 coming in at -0.38% for the fourth quarter. The S&P 500 index finished the quarter with this negative performance despite a large amount of one-time special dividends and a sharp rally in the closing days of the year on the back of the "Fiscal Compromise" as the Fiscal Cliff and spending decisions were delayed. The Southpaw Value Fund fared slightly better on a gross (gross of fees, but net of expenses) and net (net of all fees and expenses) basis, ending at +3.07% and +2.34%, respectively. Fortunately for our existing and several new Partners, the expense ratio (audit, administration, etc.) will come down dramatically in 2013 due to a more than tripling of assets since the inception of The Fund. The short book was a large performance drag in Q4, as some high beta, heavily shorted names rallied hard into year end. We raised net exposure in the middle of the quarter, beginning at 61.5% net long exposure and finishing Q4 with 79.3% net long exposure (and 118.8% total Gross exposure), positioning us well for a strong December.

Southpaw Value Fund, LP

ESTIMATED MONTHLY PERFORMANCE | 2012

PERIOD	SVF (Net)	SVF (Gross)	HFRX (Gross)	S&P 500 TR
JANUARY	7.04%	8.88%	1.72%	4.48%
FEBRUARY	5.72%	7.11%	1.42%	4.32%
MARCH	3.90%	4.80%	-0.02%	3.29%
1st QUARTER	17.57%	22.23%	3.14%	12.59%
APRIL	-3.44%	-4.06%	0.12%	-0.63%
MAY	-1.13%	-1.29%	-1.69%	-6.01%
JUNE	-0.21%	-0.16%	-0.29%	4.12%
2nd QUARTER	-4.73%	-5.45%	-1.86%	-2.75%
JULY	2.26%	2.84%	0.54%	1.39%
AUGUST	3.04%	3.77%	0.51%	2.25%
SEPTEMBER	0.07%	0.16%	0.39%	2.58%
3rd QUARTER	5.45%	6.88%	1.45%	6.35%
OCTOBER	-1.49%	-1.71%	-0.52%	-1.85%
NOVEMBER	1.17%	1.50%	0.41%	0.58%
DECEMBER	2.68%	3.31%	0.92%	0.91%
4th QUARTER	2.34%	3.07%	0.80%	-0.38%
2012 Full Year	20.87%	27.31%	3.49%	16.00%

All performance figures are unaudited, estimated, and may be subject to subsequent adjustment. A limited partner's actual returns may vary from published fund returns based on the timing of capital and fee arrangements. This statement represents information based on the policies of the fund's managers and general partner. Please contact Travis Cocke, Managing Partner of Southpaw Capital, LLC, with any inquiries.

In *War and Peace*, Tolstoy asks: "Why does an apple fall when it is ripe?" Because of its gravitational attraction to earth, because its stem withers, because it is dried by the sun, because it grows heavier, because a boy standing under it wants to eat it? Unlike Tolstoy's multifaceted awareness, it seems most capital markets participants ignore the reality of the causal nexus in asset pricing in favor of partiality for single, niche causes, one right after another, rendering discussions of these as standalone reasons for price movements as fairly meaningless. The complexity and noise permeating any real causal nexus produces a frequent fog of uncertainty and the extent to which each news item contributes to short term outcomes in the market is not perfectly clear, often times even well after the fact. Investors that keep busy trying to figure out the causes of market movements using high frequency macro stats that have a million data points can miss the simple to understand situations and securities with immediate value creating corporate actions. This behavior reminds me of a comment that a Thracian handmaid made about the Greek philosopher Thales in the story *Theaetetus* by Plato when he fell into a well as he was looking up at the stars (or of my brother who rode his bike into a brick mailbox at age eight because he was staring up at a lunar eclipse). The maid observed that Thales was so eager to know what was going on in heaven that he could not see what lay before his feet. This is a jest which can be equally applied to some investors who are looking up at the stars and "fall into wells" because they don't see what's in front of them. The amount and variation of available global macro data is vast, and just like the heavens above it betrays our longing for finitude, making it easy to get caught up in perpetual star-gazing, searching for constellations (pattern seeking in the boundless universe of information). We aim to just focus on the ground in front of us and constantly turn over the small stones we come across, collecting bottom up analyses and macro-oriented puzzle pieces from company outlooks and management comments along the way.

We must then pick and distill these bottom-up investment ideas using value drivers that can be easily comprehended--value drivers that are neither reliant on a delicately linked chained logic nor on major binary-like predictions. We prefer something simpler like a liquidation of five properties, a divestiture of a non-core business segment and subsequent special dividend or a sturdy business model at a mid-single digit multiple of free cash flow.

Enter stage left: Noble Roman's.

Noble Roman's (NROM) is an under-followed micro-cap restaurant franchisor based in Indiana that was incorporated in 1972. The company is in the business of franchising its Noble Roman's pizza concept into four primary markets: grocery stores, traditional stores, non-traditional stores (such as convenience stores), and its new free-standing take-n-bake stores. Due to being 99% franchised, the company has 39% operating profit margins, which puts it in a truly rarefied air. The restaurant franchising business is a very unique business model that offers high margins, stable recurring revenues, and very attractive returns on incremental capital that is reinvested. The business model allows the company to grow sales and profits with practically no incremental capital expenditures.

Stockholders' equity is $11.7 million, of which $11mm is a deferred tax asset as a result of prior operating losses (write-offs of bad investments and legal expenses – events we view as in the past and not reoccurring). Adjusting stockholders' equity for the DTA, the company's adjusted theoretical book value is less than a million dollars. With adjusted annualized net income of approximately $2.5 million, the company already is generating unheard of returns on equity (21% if you want to use the $11.7mm figure). Businesses with such great characteristics deserve higher multiples as growth does not consume working capital, but instead each incremental revenue dollar is available for dividends (or other shareholder friendly measures). The company has 42 traditional units, 1,772 non-traditional franchisees (convenience stores, movie theaters, bowling alleys, etc.), 1,350 grocery store accounts, and two free-standing take-n-bake units. The grocery store take-n-bake initiative is where Noble Roman's supplies grocery stores the ingredients so that their deli department can customize and build un-cooked pizzas that their shoppers can purchase and take home to bake in their home. This initiative was launched in September 2009 and distribution has grown each year. The grocery store segment has gone from 6% of sales in 2010 to 19% today and sales from grocery store accounts is projected to grow to $2.2mm in 2013 from $1.4mm in 2011, a 50%+ growth rate. Meanwhile, on the non-traditional side Noble Roman's in the last 12 months has signed agreements with Huck's, a 110-unit convenience store chain, and The Pantry, another convenience store chain with 1,600 units.

The newest growth initiative is the aforementioned free-standing take-n-bake concept. The take-n-bake concept is one of the fastest growing segments within the pizza industry. This concept allows the consumer to customize a pizza and take home to bake in their oven when the family is ready to eat. This allows the pizza industry to tap into the growing population living off food stamps (eligible for purchase with food stamps since the pizza is cooked at home and thus considered a grocery), avoids sales taxes, no delivery charge, and offers a fresh, home cooked meal. The number of Americans living off food stamps has grown to 45 million, up from 31 million in 2008. The U.S. government has increased its budget on food stamps from $40 billion in 2008 to an estimated $89 billion in 2012 (up 11% from 2011). Papa Murphy's is the largest take-n-bake chain in the U.S. with over 1,200 units nationwide, demonstrating the viability of take-n-bake as a retail concept. The free-standing TNB units typically lease 800-1,200 square feet in a retail shopping center and cost approximately $100,000 after landlord allowances. The company generates ~$2,000 in revenue per grocery store, ~ $20,000 in revenue per non-traditional unit, and management estimates it might earn $48,000 - $72,000 in revenue per free-standing take-n-bake store. In the 4Q12 both of the free-standing TNB units were opened and according to management, preliminary results have been promising. The company has another 6 free-standing TNB units under contract and we believe in 2013 Noble Roman's will expand the pipeline of signed franchisee units for their free-standing TNB concept.

In May 2012 the company completed a refinancing of its debt, lowering the interest rate from 8%+ to 4.25%, providing substantial savings on interest expense. Based on our average purchase price of $0.65 per share, the market capitalization is $12.6 million. The company has $4.42 million in net debt and $800,000 in preferred stock outstanding yielding a $17.9 million Enterprise Value. The company's past Net Operating Losses (NOLs) will shield the next ~$25 million in net income, so the company will not pay cash taxes for the foreseeable future. The company has counter-sued some franchisees for a meritless suit and is attempting to get reimbursed for legal fees and other damages. This contingent asset is not included in our base case analysis, but management has estimated as much as $2 - 3 million in potential gains. In 2011 and 2010, the company generated between $3.1 - $3.25million in EBITDA. Unlevered free cash flow for these years was $2.3 million and $2.8 million. Our view is that we're buying a high quality business with some promising growth prospects for under 7x EV/trailing FCF (14.2% unlevered FCF yield) and 5.6x EV/EBITDA. Using levered free cash flow of $2.0 million, the levered FCF to Equity yield is 15.7% (6.3x Equity Value / FCF).

We always like to say that value investments should have a bias towards small and microcaps where there is a greater likelihood of inefficiencies. NROM is consistent with this mantra and is a quintessential example of an advantage we are able to exploit by venturing into the 'nooks-n-crannies' of the marketplace. With a well below market multiple, a fast growing FCF stream and a superior business model, we think our investment in NROM will provide market beating returns over the intermediate to long term.

There is a scene in Robert Pirsig's novel, *Zen and the Art of Motorcycle Maintenance*, where a main character of the story, Phaedrus, is teaching a creative writing/rhetoric class and helps his students overcome their writer's block. When choosing a topic for an assignment to write a 500 word essay, one of the most diligent (yet uncreative) pupils chooses the United States. She demonstrates real emotional distress when she is at a complete loss for words. Phaedrus suggests instead that she focus just on their home town of Bozeman, Montana. The student is still struggling and doesn't even know where to begin. The banal Montana town is so diminutive and meager, she complains, what could she possibly come up with to write about? Phaedrus changes her assignment once again to the main street of the town and finally tells her to write only about the façade of the opera house next to the school—and to start with the brick in the upper left corner. The student is immediately skeptical, but then a rush of creativity washes over her and she can't stop writing. The following day she shows up to class with over 20 pages of inspired prose. Investors casually observing the market and anchoring to broad news stories will certainly have the equivalent of the student's writer's block: the market may not look cheap as a whole, there is worry about overcoming the Fiscal Cliff ("Scaling the 'Cliff of Insanity'?! INCONCEIVABLE!" in the words of Vizzini of *The Princess Bride*), a Euro meltdown, unrest in the Middle East, riots in Greece, etc. They will be scared away by the volatility and not have many high conviction investment ideas. The epiphany that the student and Phaedrus have is that when thinking up content for the writing assignment the student was trying to remember and regurgitate things she had already heard about the town and therefore had no original thoughts or inspirations. When she was asked to write about something that she had never heard anyone speak about before (a single brick in the Opera House), she was forced to think independently, focus on the micro, and produce something truly original.

In our pursuit of solid risk-adjusted investment returns for our Partners, we seek to apply Phaedrus' approach: Independent thinking, first hand research, micro over macro, depth over breadth, a grassroots view versus a bird's eye view. Analyze the micro in order to understand what makes the macro tick. This sentiment towards finding high conviction ideas and drawing inspiration from the micro echoes an observation from Mother Theresa: "If I look at the masses, I will never act. If I look at the one, I will." When we focus on the less discussed micro- the individual bricks and building blocks that make up the market- we are forced to immerse ourselves in the fundamentals that matter and we are compelled to think for ourselves. Subsequently, we often become overwhelmed with high quality ideas to which we can allocate our attention. These include good businesses with attractive characteristics and bargain valuations, managed by owner-operators whose capital allocation decisions are primarily driven by maximizing long term shareholder value creation.

We continue to rigorously scrutinize our past decisions, both successes and failures, and maintain an earnest discourse on lessons learned and how to practically apply them going forward. We must strive to properly discount personal biases, political prejudices, and embellished or apocryphal anecdotes in favor of evenhanded empirical evidence in order to optimize our portfolio management efficacy. Thus far, five challenging quarters and a lifetime of competition have not even begun to cool our ardor to work hard to be among the world's best. On the contrary, the kindling burns brightly and we hope and sincerely believe that we are just warming up.

Thank you for your continued support and trust. As always, please let us know if we can be of assistance to you in any way.

Best Regards,

Southpaw Capital, LLC

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