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Theta Deep Value Fund

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Quarterly Investor Letter – Q2 2007

Theta Capital Management

July 2007

Dear investor,

The Theta Deep Value Fund (the Fund) continues to perform well, generating a return of **5.2%** in the second quarter of 2007. This brings the performance of the Fund over the first 12 months since inception on July 1, 2006 to **23.3%**, comfortably above our indicated 15-20% range. Star performers during the first year were the Paulson Credit Opportunities funds as a result of a dramatic repricing of US subprime mortgage backed securities. Although we will see considerable (monthly) volatility from this fund, we expect further significant gains going forward as actual losses in the underlying mortgage pools materialize. So far, our holding in the Paulson Credit Opportunities Funds more than doubled in value since we began investing in this fund as of October 1, 2006.

Although not as spectacular, the performance of the other funds has been more than satisfactory over those first 12 months. Strong performers are CIM Special Situations, Greater Europe Deep Value and the Montpelier Fund. Disappointing performers over the first 12 months have been the Red Kite Metals Fund and the Eidesis Special Opportunities Fund/Special Situations Fund. Nonetheless, we have high expectations for these going forward.

We have added four funds as of July 1 (Focus Capital, Autonomy Capital C Class, Marwyn Neptune fund and Pershing Square) and have redeemed one fund (Jolly Rogers Activist Fund, Pirate Capital). Following the July 1 closing, the Theta Deep Value fund has approximately EUR 150 million under management.

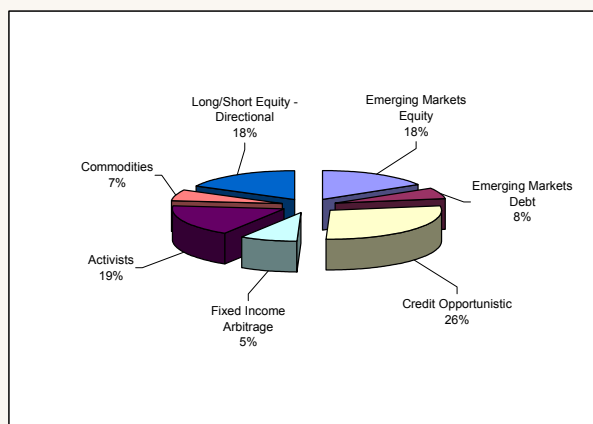
In April the Fund returned 1.36%. The biggest contributors during that month were The Montpelier Fund and the Red Kite Prospect Fund. The Montpelier Fund particularly benefited from their positions in China. The fund very carefully avoids the hyped, financials dominated A-shares, but instead focuses on attractive opportunities within Hong Kong listings. In May, the Fund generated 0.99%. The biggest contributor in that month was again the Montpelier Fund. In June, the Fund returned around 2.80%, driven by another (following February) spectacular month for Paulson Credit opportunities. As readers of our previous reports know well by now, this fund is fully positioned to take advantage of the structural weaknesses in the US Subprime Mortgage market. The Bear Stearns hedge funds meltdown led to a reappraisal of risk in the subprime market. Paulson returned around 40% for the month as a result of their short positions. Other positive contributors during the month were our investments in CIM Special Situations and Greater Europe Deep Value. The main detractor was Eidesis who was hit by a sharp dislocation in the market as index investors heavily bought credit protection through the indices in June, but tranche investors on the same names remained remarkably sanguine about the risk of the most risky part (the equity tranches) of the index. We have full faith that this strategy will pay off nicely over the medium future, but monthly volatility like this can be expected.

Theta Deep Value Fund - Performance (July series)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2006
Net Performance							-1.68%	1.19%	-0.75%	3.17%	2.90%	3.83%	8.83%
Cumulative Performance							-1.68%	-0.51%	-1.26%	1.87%	4.82%	8.83%	
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2007
Net Performance	-0.08%	6.60%	1.12%	1.36%	0.99%	2.80%							13.34%
Cumulative Performance	8.74%	15.91%	17.21%	18.81%	19.99%	23.34%							

Note: As the fund's independent administrator provides an official NAV on a quarterly basis, monthly numbers are estimates provided by the manager.

Strategy Allocation	Jul-07
Emerging Markets Equity	18%
The Montpellier Fund Greater Europe Deep Value Fund	
Emerging Markets Debt	8%
Autonomy Capital C Class	
Credit Opportunistic	26%
CQS Directional Opportunities Fund Camulos Paulson Credit ZAIS	
Fixed Income Arbitrage	5%
Eidesis Special Opportunities Eidesis Structured Credit	
Activists	19%
Pershing Square Focus Capital Marwyn	
Commodities	7%
Red Kite Metals Fund Red Kite Prospect Fund	
Long/Short Equity - Directional	18%
CIM Special Situations Sector Speculare III Ecofin Special Situations	
Total	100%



Second Quarter 2007 Performance Review

The **Absolute Activist Value Fund** (Activist Investing) had a decent quarter with a **3.2%** return, bringing the year to date return to almost **9%**. During the 2nd quarter the fund has doubled its assets to USD180 million. As mentioned in our previous quarterly, Comet has been a significant holding in the fund since the end of last year. The discussions about the strategy with the Comet management lead to certain corporate governance changes in April, which set the scene for an acquisition at the end of May. The manager sees some further upside for Comet the rest of the year.

The manager is very confident about the opportunities in Europe the coming years, because of the M&A activity and the development of the private equity sector in Europe over the last years. In the US there is 1 activist versus every 10 situations whereas in Europe the ratio that is only 1 activist for 100 situations.

Due to the relatively low volatility of the Absolute Activist fund (partly a result of the diversified nature of the portfolio) we decided to move the fund into our medium volatility portfolios and use the space in Deep value to invest in more concentrated activist funds.

Camulos Partners Offshore Fund (Distressed Debt) had a solid quarter with a return of **5.9%** generated in leveraged loans and distressed securities. As we noted in our previous quarterly, we have switched out of the master fund into the more volatile/higher return Special Situations Fund they launched recently. Although it is early days yet for the fund with just one investment so far, the pipeline looks extremely promising and we expect attractive, non-correlated returns from this fund in the medium term.

The **CIM Special Situations Fund** (Event-driven) generated **7.5%** in Q2. The fund's mix of technology, natural resources and distressed situations continues to pay off nicely with the fund posting positive returns every single month so far this year returning around **14.6%** year-to-date. The fund remains well diversified in terms of companies and geographies with investments ranging from Australian Uranium mining companies to Russian helicopter manufacturers to UK mobile software developers. The common strain amongst all of them is that the fund manager believes there is a high likelihood of the investment at least doubling over the coming two years. Some of their recent profitable investments have been Global Testing (the Taiwanese chip tester which was up nearly 40% in June), Lonrho Africa which was up 40% in June as new management took charge and Zambezi Resources which was up nicely during the month due to anticipation of an Australian listing. The investment team of CIM spends a considerable amount of time on

the road in order to find new investments and they seem to cover most of Asia and Africa in order to find interesting opportunities.

CQS Directional Opportunities Fund (Convertibles) generated a **2.9%** return in the second quarter, bringing the year to date performance for the fund to **7.7%**. CQS is a very impressive organization, lead by Michael Hintze, who has established a premier league investment company.

The main driver of the returns so far is the long structured credit position. In the portfolio they focus on short duration bonds. CQS holds credits with a 0 to 3 year maturity and is short credits with a longer duration. After the widening at the end of February and the beginning of March they took a long position in sub-prime mortgages in the UK. The running yield of the portfolio is currently about 14 to 15%. Although the current short term credit environment is not ideal for this fund, its opportunistic nature and wide mandate gives us comfort about outsized return in the longer term.

Greater Europe Deep Value fund (Emerging Markets Equity) generated around **3%** in the second quarter (and is up around **20%** for the year following a very strong first quarter). The investment climate in Russia has deteriorated over the last couple of months as witnessed by a couple of high profile diplomatic spats between Russia and various Western countries. Although the tone of Russian diplomacy once again calmed down in June, the Litvinenko affair and its effect on UK-Russia relations has once again increased risk premia for Russia. Overall, despite the political risks, valuations look very attractive in Russia, the underlying economic picture remains positive and demand for commodities and oil in particular remains buoyant. The fund is close to exiting their second (private equity) deal in a row, with an average annual yield of around 70% per annum.

Ecofin Special Situations Utilities Hedge Fund (Event-driven) returned **7.5%** during the second quarter, bringing the year to date performance to **12.5%**. Especially April and May were good months for Ecofin. The main event in April was the new valuation of Airtricity from EUR 19.20 to EUR 24.50 per share. The strategy of the company is to build, own and operating wind farms in Europe and North America and they are developing capacity in the UK, Ireland and Portugal. Ecofin owns 16% of Airtricity. The sale by Goldman Sachs of Horizon Energy demonstrated a strong investor interest for wind development platforms. The strong performance in May was the result of a number of announced IPO's in the Solar space, with LDK Solar, PV Crystalox and Solaria all announcing plans to come to the market. In addition, the fuel cell company Idatech announced that it was raising approximately Gbp 30 million to expand R&D and its marketing operation. Further, Boreal Energy, a wind farm operator and developer was also seeking to come to the market. Ecofin's portfolio benefited from the positive sentiment in the energy market. Currently the fund has USD 880 million under management.

Eidesis Special Opportunities Fund and the **Structured Credit Fund** (Distressed Collateralised Debt Obligations). These funds had a difficult quarter with a blended return of **-11%** bringing the year-to-date loss to around **-8.5%**. Over 85% of the fund is invested in liquid, transparently priced CDX positions and in cash. The long exposures are in standard 3- and 5 year CDX high yield series. The shorts are in CDX equity and mezzanine tranches, matched to protect the cash flows under the conservative default scenarios of 6 to 8% per year. In June, extreme volatility in the mark-to-market of the CDX index was not offset by a commensurate sell off in the equity and mezzanine tranches. This resulted in a 9% loss for the 2 funds we hold in the portfolio. According to the manager the expected base case unlevered IRR's on the capital allocated to the 3 year CDX high yield positions is over 40% over 3 years. Although we are disappointed with the result of the manager so far we are confident that the results will improve going forward and that the fund will provide a hedge when default expectations rise.

We exited our **Jolly Rogers Activist Fund/Pirate Capital** (Activist Investing) investment as we saw better opportunities elsewhere (in particular with Pershing Square where the stability of both the team and returns compares favourably). During the second quarter performance was again volatile: down 4.5% in June, up in May and down in April. Year-to-date, the fund, with considerable volatility, is flat.

The **Montpelier Fund** (Emerging Markets Equity) returned close to **18%** in the second quarter, resulting in a **32%** year-to-date return. Over the quarter, the fund's portfolio performed nicely with the investments in China performing very well in April and May before returning some of their gains in June. However, in June their Egyptian, Russian and Middle-Eastern holdings performed very well thus compensating for the correction in China.

As mentioned in our previous reports the Montpelier fund is closed and remains one of our high conviction names. The biggest part of the Montpelier fund, about 28%, is invested in State Owned Enterprises in China. To top up our position we decided to invest in the **Montpelier China fund**. This fund, which was launched at the end of June 2007, will be managed by Montpelier in conjunction with Nankai Capital in Shanghai. This fund will focus on investing in State Owned Enterprises (SOEs) listed in Hong Kong. The theme behind the investments is that these SOEs are not followed by the investor community and that the performance so far has been pedestrian. However, it is the intention of the Chinese government to inject more assets in those SOE's which should make analysts more aware of their attractions.

Paulson Credit Opportunities Fund I & II (Credit) generated a blended return of over **30%** during the second quarter. The year to date performance for the credit opportunities I fund is 129% and the blended return is around **106%**. In June, the pricing of the sub prime securities partially caught up with fundamentals and took a major leg down. The trigger for the correction was the collapse of the Bear Stearns high grade structured credit enhanced leverage fund, which invested in supposedly high-grade tranches of CDO's, backed by mezzanine tranches of sub prime securitizations. Paulson has significant short positions in these securities.

The sub prime market decline in June caused rating actions by S&P at the beginning of July. On July 10, both S&P and Moody's put 562 credit names on watch and downgraded 399 tranches of sub prime securitizations.

The manager believes this is only the beginning of a down rating cycle and they expect that the fundamentals will continue to deteriorate for both the housing market and the sub prime market because of declining home sales, a rising inventory and a rise of delinquencies and defaults.

Red Kite Metals Fund/Prospect Fund (Commodities)

Red Kite had a decent second quarter with especially the Prospect fund doing well (which is the largest of our two investments in Red Kite), returning **9%** for the quarter. The Metals fund disappointed with the fund's return around **0%** for the quarter. Our blended year-to-date return across the two funds is **-4%**. As we already stated following the disappointing start to our investment in January, we still have full confidence in the manager who has a good long-term track record and has managed to benefit from sharp up- as well as downturns in various commodity markets (albeit with a focus on the copper market). The Prospect fund is a more long-term fund than the Metals fund which tends to focus on trading the nearby contracts. The performance of these further-out contracts, in combination with the current strong backwardation of the curve explains the difference in performance between the Prospect and Metals fund. The presence of Red Kite in the physical trading market, especially in China, gives it considerable advantage when assessing short

term demand in the copper market. China remains the key swing factor with regards to setting prices in the market and they see continued evidence for solid demand of copper going forward.

Sector Speculare III has made the second capital call and is now very busy investing those proceeds in numerous transactions they have in the pipeline. Sector has made a modest contribution so far since inception (March 2007) of around **2%**. This was due to some of their listed investment and/or OTC investments which saw modest markups during the quarter. After the ramp-up, Sector Speculare III will have 12 to 13 investments. All these should have a clearly defined exit within 3 years of investment. The biggest investment is in a very experienced ex-BP team who have set out to build up an attractive E&P business which should be a highly attractive takeover candidate for one of the oil majors once it is fully operational. Although it is still too early to say anything too specific about the transactions within Sector Speculare III, the quality of the team at Sector and the returns achieved with the Speculare I and II funds (the first two funds returned most of their capital within the first 12 to 18 months and had/have considerable upside going still going forward) give us great confidence about returns going forward.

The **Zais Matrix V Fund** (Structured Credit / Distressed CDO's) called some additional capital in the second quarter resulting in about 15% of the capital being called. ZAIS focuses on opportunities that return a substantial amount of the investment through upfront interest cash flow rather than a return at some future date, as they feel these are too speculative. Currently they take a conservative stance and will enter the market only when they see attractive opportunities. Currently they own one CLO equity piece which was priced too cheaply. Other investments are in the ABS and in the ABS CDO space. Additional capital calls will follow in the third quarter.

New Allocations

Autonomy Capital C class (Emerging Markets) will be added per August 1. The fund is managed by Robert Gibbins whom we have known for a long time and with whom we are invested with some of our other funds. Robert has a strong pedigree in Emerging Market Debt and local currency. After being an early participant in the emerging debt market he now sees a lot of opportunities in the local economies. The emerging middle classes, who are going to use financial instruments like mortgages, are the main driver behind these opportunities. Currently mortgages are only 5% of GDP in Brazil which he expects to grow to 30% in 5 years time. In this fund he will invest in Asset Backed Lending, real estate opportunities and in agriculture. In the beginning the main focus will be on Brazil, but other countries will be added to the portfolio at a later stage. As a result of the opportunities, the low correlation with other funds and the expertise of Robert Gibbins and the Autonomy organization we view this as a valuable addition to the Theta Deep Value portfolio.

Focus Capital (Activist Investing) is a NY/Zurich based fund which actively engages in friendly activism (don't expect their name in the newspapers). They run a concentrated portfolio of companies which have world class products or services, but where some operational or financial restructuring is necessary to unlock that value. The geographical focus so far has been on Switzerland given the background of the principals and the opportunities they have identified there. However, they will also look at other German speaking countries and/or the Benelux. Their track record is impressive, generating 112% in 2006 and 45% year-to-date. Although their portfolio is concentrated, it is not simply buy and hold but they will actively trade around positions to capture some additional alpha. Furthermore, they actively hedge their portfolio to reduce their market exposure.

Pershing Square, run by William Ackman, is a US based activist manager with a concentrated portfolio focused on the US market. The top-10 investments typically represent around 80% of the portfolio and these positions tend to be research-intensive, complex situations which hide simple underlying businesses or assets. The team has an excellent track record in identifying opportunities and unlocking value from these franchises. Investments where Pershing Square has been active include Plains Resources, Sears, Wendys and McDonalds. Furthermore, the fund is an active shorter. Bill and his team seek to generate absolute returns from these shorts by focusing on companies with accounting issues and/or low earnings quality. They also focus on companies where there is considerable liquidity and bankruptcy risk. The combination of aggressively looking for undervalued opportunities where value can be unlocked and overvalued franchises where the market does not understand the risk is compelling.

The **Marwyn Neptune Fund** strategy is basically to find top quality management and then use these management teams to run either a private or listed company in a private equity manner. They focus on companies in a regulatory environment, such as gaming, food and water because these are areas where an experienced management team has an edge. A key part of the approach is that they are consolidators and are interested in growing the business. Their expertise lies in identifying bolt-on acquisitions, integrating these and selling the more attractive bigger company at a significant premium to what they bought it for. This growth strategy makes it easier for them to speak to management/owners as Marwyn wants to be seen as a partner who can help a company to take the next step in its growth phase. We took only half a position because of the market sensitive nature of the strategy.

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