ETOLIAN CAPITAL

Monthly Letter: October 2005

Etolian Capital Group, LP is a private investment management company, which focuses on US credit fixed income opportunities. Its objective is to generate above average, stable returns which are uncorrelated with major market indices by going long and short in cash and derivative fixed income obligations issued by primarily US investment grade rated corporations. What differentiates Etolian Capital from other similar efforts is its credit selection process which is based on an options-based quantitative methodology and relies, among other things, on information from the equity and equity option markets to assess credit. This methodology is used to identify undervalued and overvalued situations and accordingly create long and short positions in them. Interest rate risk is hedged and moderate leverage (up to 5 times) is deployed to achieve objectives. The long/short approach, combined with the use of leverage, as well as other risk management techniques, reduces the probability of a major capital loss.

Currently, Etolian Capital offers two funds; the **Etolian Capital Credit Fund, LP** (a US domestic partnership), and the **Etolian Capital Offshore Credit Fund, Ltd** (a Cayman exempted company).

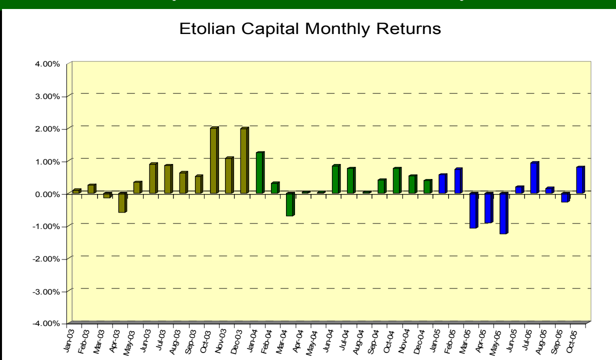
	Etolian Capital*		S&P 500 Index**	CSFB Indices***	
	Credit Fund (Onshore)	Offshore Credit Fund	S&P	LUCI	CDSI
October Return	0.80%	0.80%	(1.77%)	(1.44%)	0.14%
October Volatility	0.38%	0.38%	0.63%	1.11%	0.20%
October Sharpe Ratio	1.51	1.51	(3.20)	(1.50)	(0.43)
YTD Return	(0.13%)	(0.10%)	(0.41%)	0.28%	2.30%
YTD Volatility	2.82%	2.82%	21.66%	4.15%	0.78%
YTD Sharpe Ratio	(0.68)	(0.68)	(0.10)	(0.37)	0.63

(*) Returns are **net** of fees (1.5% management fee and 20% incentive allocation of profits). October and YTD gross returns were 1.167% and 1.075% respectively.

(**) The S&P 500 and CSFB Index returns are **gross** returns

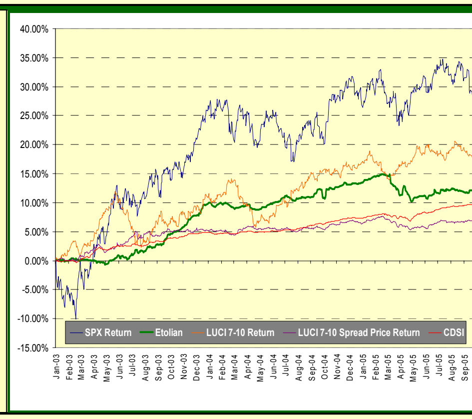
(***) The 7-10 year LUCI Corporate Bond Index is compiled by CSFB (CDSI=Credit Default Swap Index)

Monthly Gross Returns – As of July 2005



Portfolio Performance

	2003	2004	2005
January	0.10%	1.26%	0.56%
February	0.25%	0.31%	0.75%
March	(0.14%)	(0.69%)	(1.08%)
April	(0.59%)	0.04%	(0.92%)
May	0.34%	0.03%	(1.26%)
June	0.90%	0.85%	0.25%
July	0.87%	0.77%	0.95%
August	0.64%	0.03%	0.15%
September	0.53%	0.41%	(0.27%)
October	2.01%	0.77%	0.80%
November	1.08%	0.54%	
December	2.00%	0.39%	
Year to Date	8.25%	4.79%	(0.10%)
Since Inception:		13.32%	



October Monthly

October kept up with its tradition for being a volatile month, bringing a lot of volatility and associated pain and consternation to market participants, almost across the whole market spectrum. Participants struggled to assess the current state and future outlook of the economy and, in the process, caused wide market gyrations. For starters, the equity markets, spooked by stagflation fears and a potentially aggressive Fed, were the most volatile finishing the month with a 1.77% loss, after registering intra-month losses as high as 5%. Equity volatility, as captured by VIX, mirrored the equity markets sentiment, spiking at 17 (from September's close at 12), before finishing the month as around 15. But it was the interest rate markets that bore the brunt of these fears by registering a hefty rise in rates which reached as much as 40 basis points in the 10-year Treasury note. What does this leave us regarding the outlook for the economy which, after all, is the main driver of all of the above? As we have said before, the Fed is far from done, indicating the potential strength of the economy. Yet, we will continue to keep a close eye on the housing market which, through its effects on consumer spending, has been the main economic driver. It seems to us, though, that the risk does not seem to be from a slowing economy.

Unsurprisingly, the credit market moved largely in sympathy with the other markets causing credit spreads to move out. Again, Autos and Auto-parts were the main culprits behind the spread widening. Delphi's bankruptcy filing was the catalyst to start the widening process which saw some of the Auto and Auto-parts credits widen by as much as 300 basis points. Once again, one of the most telegraphed events caught a lot of market participants by surprise, making us wonder about the whole concept of market efficiency. However, unlike the Spring turmoil, the impact on the rest of the credit market was relatively muted, leading only to modest spread widening in other sectors of the credit market. Overall robust earnings announcements and GM's mid-month announcement about the GMAC spin-off, also helped restore – at least temporarily – market sentiment. As a result, the remainder of the month was spent in a relatively lackluster and illiquid trading environment. Apart from the Auto-related credits, other movements worth noting were the weakness consumer related credits and telecoms, and the strength in financials – despite the increase in rates. As a result, the CDX HVOL4 index finished the month at around 122 (from last months' close at 115), after having traded as high as 141. As we look to the remainder of the year, and with the earnings behind us, the market expectation is of a year-end rally in credit spreads. We doubt it! We continue to be of the view that we have entered the asymmetric stage of the credit cycle where the upside from being long credit spreads is fairly limited, while the downside could be significant. This coupled with the steady rise in idiosyncratic risk that we have been observing daily in the form of LBOs and share buybacks (Starwood, Computer Science, Cadence, TXU, Albertsons, etc.) makes life in the corporate credit market a dangerous place to be!

At Etolian Capital, October was a gratifying month as a number of the themes that we have been positioning for, within our market neutral context, played out delivering a positive result of 80 basis points for the month. In short, our shorts and the market hedges that we had against our longs significantly outperformed our long positions. In addition, by consciously reducing the number of long positions, we minimized the chance that we may get hit by one the LBO landmines (as we have in the past). The only regret, perhaps, was with letting some of the shorts go a bit to early, depriving ourselves for the possibility of an outsized gain (i.e., Kodak, Unisys). As we look to the remainder of the year, and given our outlook above, our stance remains unchanged. That is, within our market neutral way, we will continue to look for opportunities to source shorts and balancing them through credit indices, being wary of the increased idiosyncratic risk. As we enter November our portfolio has been further reduced and is fairly balanced between short and long positions with about 78% long and 82% short.

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