January 20, 2009

Dear Partner:

Greenlight Capital, L.P., Greenlight Capital Qualified, L.P. and Greenlight Capital Offshore, Ltd. (collectively, the "Partnerships") returned (7.5)%, (6.6)% and (2.4)%, net of fees and expenses, respectively, in the fourth quarter of 2008, and (22.7)%, (20.8)% and (16.5)% for 2008.

2008 was the first year that we lost money since we opened our doors in May 1996. We are disappointed about our 2008 result, and we are sure you are as well. A tough market and a difficult economic environment expose the flaws in many businesses and many investment strategies. Although the past year was extremely challenging for Greenlight, we feel our investment program is different from some troubled investment strategies. We do not use leverage to try to turn small returns into medium sized returns. Our investment program is comprised primarily of listed equities and actively traded debt instruments, and we are able to mark almost our entire portfolio to readily observable market prices. We invest knowing that markets can become dislocated, and that even distressed marks are losses until and unless the markets reverse.

In 2008, we made too many mistakes and have identified areas for internal improvement. We believe the Partnerships are in good shape heading into 2009. For this, we are most grateful for your continuing support and confidence. While others are struggling with redemptions, we have successfully raised fresh capital to pursue the opportunities created by the current market dislocations.

In the fourth quarter, the financial crisis spread from the financial sector into the general economy. It seemed that when our leaders announced to the world that Wall Street had a big problem, a "we better give them $700 billion or else…" sized problem, the general population realized that it ought to be scared and sent the economy and the markets into a tailspin. When the dust settled, the S&P 500 fell another 22% in the fourth quarter, bringing the 2008 loss to 37%. Fourth quarter GDP and earnings are not yet known, but there is no doubt they will be awful.

The quarter witnessed a re-evaluation of all types of risk. Market participants considered the most dislocated markets and asked themselves: If government agency securities and municipal bonds yield this, then what should investment grade corporate bonds yield? Given that, what should leveraged bank loans yield? And if bank loans yield equity-like returns, why should anyone own an equity? The implicit answer to this question was that virtually all equities must be worthless and, by that logic, should be sold.

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To us, this appears to be flawed thinking. What if it turned out that the most dislocated asset market was dislocated for technical rather than fundamental reasons? If that were so, then all the decisions to re-price every other asset in response would prove to be an over-reaction. As the re-pricing logic became prevalent, we bought.

We bought a lot of things across the corporate capital structure. We bought bank debt. We bought high yield bonds. We bought convertible bonds. We bought unlevered equities and we even bought levered equities (where for the first time in memory the market appeared to over-penalize for leverage). We bought back (covered) some of our shorts. And, as discussed below, we bought gold and select foreign currencies. The number of securities in the portfolio grew dramatically during the quarter as we added many small positions in things we believed to be undervalued and good long term investments.

What we didn't do was try to be heroes and pick a bottom. We don't know where the bottom will be and don't want to bet the farm on guessing, so we did our buying with restraint. We want to be able to continue buying when the markets see extreme dislocations as they did in mid-October and mid-November. We began the fourth quarter 9% net long and by November 18 we were 43% net long.

During the quarter, pretty much everything fell in value. The partnership lost 22% on its longs and made 17% on its shorts (even accounting for our loss in Volkswagen, "VOW"). There were nine positions that contributed more than 1% (six shorts, gold, the Japanese Yen and a credit default swap we purchased on a foreign government as a very small rooting interest that exploded in value). There were eight investments that cost more than 1% (seven longs and VOW).

Ordinarily, we would discuss what happened in each investment that had a large impact on our results. In the fourth quarter, however, so much of the explanation is covered by macro and market developments, that we will limit the discussion to the two biggest losers in the quarter: Helix Energy Solutions Group (HLX) and VOW.

HLX was our largest loser in the quarter as the shares collapsed from $24.28 to $7.24. As the market corrected in the third quarter, we added aggressively to our position in HLX at exactly the wrong moment. Just as we were completing our order, hurricane Gustav hit the Gulf of Mexico and inflicted enormous damage on the company's current production. The temporary loss of production combined with the implosion of oil prices (which fell from $145 per barrel in July to $97 at the end of September, the worst quarterly loss ever, and then to $34 in late December) had a catastrophic impact on the stock.

On a fine Sunday afternoon in October, Porsche put out a press release announcing that it controlled substantially all the floating shares in VOW. It had done this through the acquisition of "cash-settled" options that it believed it did not have to disclose under a loophole in German securities laws. That Sunday, Porsche made its voluntary disclosure to give "short-sellers the opportunity to close their positions unhurriedly and without further risk." In response, VOW shares, which stood at €210 at the time of the announcement, exploded to over €1,000 by Tuesday morning. At this implied valuation, VOW – an automobile maker in the midst of a crash in auto sales – became the most valuable company in the world in terms of market capitalization.

While the German authorities are "investigating" whether any laws were broken in this "super short-squeeze," it isn't hard to see that something is wrong here. To know this, simply change the players and guess the response. Imagine the headline: "Hedge funds announce they cornered the stock of Volkswagen, Porsche loses billions." We doubt it would take long for the German authorities to find a crime in that.

As for us, the worst trade is the one you don't want to make, but the one you have to make. Our strategy generally looks for forced sellers who aren't considering the long-term values, and it considers taking the other side of their trades. Occasionally, we find ourselves on the wrong end of that dynamic. Periodically, we have covered short sales for portfolio management rather than fundamental reasons. We do this because we are simply unwilling to risk the entire portfolio on a single investment, particularly when that investment becomes detached from normal trading behavior. Though VOW was not a large position on Friday, it became one by Tuesday. We held our nose and covered a portion of our position at a significant loss.

During the quarter, the Partnerships added significant long positions in Allegheny Energy (AYE), Commscope (CTV), MEMC Electronic Materials (WFR), gold and an index of gold miners (GDX), and the Japanese Yen.

AYE is an electric utility that provides generation and transmission of power in western Pennsylvania and parts of Virginia and Maryland. As a regulated entity, AYE is currently selling power at below market prices within its service territory. The state of Pennsylvania has agreed to allow AYE to transition to market rates over the next three years. In addition, AYE is investing over $1 billion into the regulated transmission side of its business that will go towards balancing the power needs of the PJM service territory (Pennsylvania, New Jersey, and Maryland). AYE has been authorized to earn a 14% rate of return on this investment. As a result of charging market rates for power and higher earning projects coming on line, we expect AYE's earnings per share will improve from $2.30 in 2008 to almost $3.00 in 2009 and $4.00 in 2010. We bought AYE shares at an average cost of $28.26 per share, or less than 10x estimated 2009 EPS and about 7x estimated 2010 EPS. AYE ended the quarter at $33.86 per share.

CTV is a global provider of last-mile infrastructure to the communications industry (think antennas and cables for the wireless, cable, telephone and data industries). We had initially evaluated CTV earlier this year after its acquisition of Andrew Corporation. While we liked the long-term growth dynamics in the communications infrastructure business and believed that management was understating synergies from the Andrew deal, the stock didn't seem cheap enough. That changed in October and November as the stock fell sharply over concerns about the company's leverage and liquidity and its reduced outlook for the fourth quarter of 2008. We believe that the liquidity concerns are overblown. We established our position at an average cost of $16.96 per share, which represents 5x estimated 2008 earnings. CTV has a tenured management team with a proven ability to establish and maintain leading market positions in each of their business segments. While 2009 will undoubtedly be a tough year for CTV in the current business environment, we believe its prospects over the next few years are good as CTV should benefit from incremental revenue and costs synergies from the Andrew acquisition and new product introductions. CTV shares ended the quarter at $15.54 each.

WFR is a low cost manufacturer of bulk polysilicon and poly wafers for the semiconductor (half the business) and solar (the other half) industries. The semiconductor industry is expected to go through a large down cycle in 2009. Bulk polysilicon, which was sold at $400/kg just a few months ago, now sells for $100/kg and is likely to come down even further. WFR has contracted its solar-capable wafer capacity to four solar companies for ten years at very healthy gross margins. It is likely that these contracts will get renegotiated at a lower price. These headwinds will cause WFR's EPS to fall from a peak of $3.00 per share to $1.50 per share in 2009. WFR currently has $5.67 of net cash on its balance sheet. We established our position at an average cost of $13.68 per share or 6x cyclically depressed estimated 2009 earnings net of the cash. WFR shares ended the quarter at $14.28 each.

We never thought we would ever buy gold or gold stocks. David's grandfather Benjamin was a goldbug. From the time David was ten, Grandpa Ben took every opportunity to tell David about the problems with fiat currencies and the coming inflation and advised that the only sensible thing to do was to buy gold and gold stocks. And, for the last thirty years of his life, that is what Grandpa Ben did. And it was a lousy investment. Being a patient investor is one thing. Being "wrong" for three decades is quite another.

To everyone's dismay, we believe that some of Grandpa Ben's predictions are playing out. Our current chairman of the Federal Reserve, Ben Bernanke, is an "inflationist." When times were good, he supported an easy money policy. Even when the Fed raised rates, Bernanke took great pains to give the markets many warnings to insure that the higher rates wouldn't break up the credit party, *i.e. bubble formation*. Now that the cycle has turned, the Fed has promised to resort to "all means necessary" to head off the effects of the collapsed bubble. Rates have effectively been lowered to zero. The Fed is making loans collateralized by toxic waste and has now begun a policy called "quantitative easing" – a fancy term for "printing money." The size of the Fed's balance sheet is exploding and the currency is being debased. Combined with an aggressive fiscal policy, it is clear that the authorities are going "all-in" to try to mitigate the near-term effects of the economic collapse. Our guess is that if the chairman of the Fed is determined to debase the currency, he will succeed. Our instinct is that gold will do well either way: deflation will lead to further steps to debase the currency, while inflation speaks for itself. We have bought gold, calls on gold, an index of gold mining stocks (GDX) and calls on higher long-term U.S. interest rates. We have also moved some of our cash into foreign currencies, particularly the Japanese Yen.

The Partnerships closed the following select positions during the quarter:

Closed Security	L/S	Avg Entry Price	Avg Exit Price	IRR	Comments
Ameriprise Financial	L	$39.81	$42.69	6%	This spin-off from American Express performed decently for a while. However, it was over-exposed to equity markets, and management became complacent. We didn't sell at the top, but are glad we sold before it imploded.
American Reprographics	S	$32.16	$18.05	59%	A good short that we held for a good while that completely collapsed after we covered.
Aurelian Resources	S	CAD 7.56	CAD 6.56	18%	A company touting a "huge" gold find in Ecuador. We doubted the viability of the project, but Kinross Gold took them over.
Equinix Inc	S	$72.23	$56.79	37%	People thought this was a high value-add business with high barriers to entry. We thought otherwise. The market started to see it our way when a new company successfully raised money to do virtually the same thing.
Great Atlantic & Pacific Tea Company	S	$30.89	$16.52	36%	A multi-year short of one of the weakest supermarket chains around. It took a long time as acquisitions and divestitures made it hard to track. Ultimately, investors stopped buying the "story" and leverage compounded their problems.
Itron Inc	S	$64.90	$74.79	-15%	Another story clouded by acquisitions. However, its acquisitions were a bit more successful and its leverage was less. We took the stock market decline as an opportunity to exit this frustrating position.
Macquarie Airports	S	AUD 3.85	AUD 2.35	48%	A credit bubble stock….de-bubblized
McGraw-Hill Companies	S	$54.65	$24.88	50%	Short based mostly on rating agency exposure at Standard & Poor's. We covered when we felt the shares reflected no value for that unit.

Effective January 2009, we have opened an additional prime brokerage account with Merrill Lynch, now officially Bank of America. This account will complement our existing prime brokerage relationships with Goldman Sachs, Citigroup and BNP Paribas. We have also opened a custodial account with Bank of New York Mellon. Given the environment, we continue to monitor counterparty risk aggressively and work on a daily basis to minimize collateral requirements on our over-the-counter financial instruments.

In the fourth quarter Richard Owen joined us as our first research analyst on the ground in London. Previously he was with Blackstone's European M&A and Restructuring team. Richard has spent the past few months working with the investment team in New York, and he will transition to our London office in late January. Welcome Richard!

Two analysts departed Greenlight in December. Jeff LeBlanc decided to pursue an opportunity outside of the investment field. Vlad Artamonov left the firm to pursue an independent course. We wish Jeff and Vlad much success.

We completed the capital raise that we announced in the third quarter letter. We had significantly more interest than what we could accommodate, and took in additional capital for November 2008 and January 2009. We welcome our new partners who may be reading this letter for the first time, and we thank our existing partners for their continued interest and support.

At quarter end, the five largest long equity positions in the Partnerships were Allegheny Energy, Arkema, Criteria Caixa, Oesterreichische Post and URS Corp. The Partnerships had an average exposure to equities and fixed income (excluding credit derivatives, gold and foreign currencies) of 76% long and 37% short.

> "If they can get you asking the wrong questions,
> they don't have to worry about the answers."
> - Thomas Pynchon

Best Regards,

Greenlight Capital

Greenlight Capital, Inc.