

FIRM BROCHURE

(PART 2A OF FORM ADV)

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This brochure provides information about the qualifications and business practices of Cape Ann Capital, Inc. If you have any questions about the contents of this brochure, please contact us at: (978) 526-7541, or by email at: DaveU@CapeAnnCapital.com. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission ("SEC") or by any state securities authority. Registration with the SEC or a state securities authority does not imply a certain level of skill or training.

Additional information about Cape Ann Capital, Inc., also is available on the SEC's website at www.adviserinfo.sec.gov

ITEM 2: MATERIAL CHANGES

Material Changes since the Last Annual Update

This summary only includes the material changes made since last year's brochure and not a list of all of the changes we have made. We last updated our brochure on March 31, 2010.

- David Umstead now owns 85% of Cape Ann Capital and James Jasinski owns 15%. As of our last annual update, David Umstead owned 100% of Cape Ann Capital.
 - Our revenue is 100% from investment advisory services. As of our last annual update, 99% of our revenue was from investment advisory services and 1% was from consulting services.
 - Last year we offered investment advisory services either as a percentage of assets under management or at an hourly rate. At this time, we are only offering our services as a percentage of assets under management.
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ITEM 4: ADVISORY BUSINESS

Firm Description

Cape Ann Capital was founded in April of 1999 to provide investment advisory services to individuals and institutions. The firm manages 108 client portfolios with an aggregate market value of \$77 million.

Principal Owners

David Umstead owns 85% of the firm and James Jasinski owns 15%.

Types of Advisory Services

Cape Ann Capital manages portfolios of actively managed mutual funds and exchange traded index funds for individuals, corporations, trusts and charities. Each client portfolio is individually tailored to a long-term asset allocation target determined by the client. Cape Ann Capital assists in finding an asset allocation target that will meet each client's long-term return objectives without exceeding his or her tolerance for risk. Most clients are targeting exposures to all of the following asset classes: U.S. cash, U.S. bonds, U.S. equities, European equities, Asian equities, emerging markets equities and commodities. Allocations across these seven categories vary considerably from client to client.

Tailored Relationships

Because each client portfolio is individually managed, we are able to tailor portfolios to the particular needs of each client. Once each client commits to a long-term asset allocation target, they can be as involved or uninvolved as they wish in the investment process. For example, we are willing to discuss transactions before they are made, hold "unmanaged" positions and work closely with each client's CPA to help minimize taxable income.

Wrap Fee Programs

Cape Ann Capital does not participate in any wrap fee programs.

Assets Under Discretionary and Non-Discretionary Management

As of December 31, 2010, Cape Ann Capital had assets under discretionary management of \$77 million.

ITEM 5: FEES AND COMPENSATION

Description

Cape Ann Capital is a fee-only advisor. Fees are based on the market value of the assets being managed and are calculated according to the following fee schedule.

Fee Schedule

<u>Assets</u>	<u>Annual Fee Rate</u>
First \$1 million	0.65% of assets
Next \$1 million	0.35% of assets
Over \$2 million	0.20% of assets

Fees are negotiable.

Fee Billing

Fees are collected monthly (at one-twelfth the annual rate) in arrears based on month-end valuations. Cape Ann Capital submits fee invoices to TD Ameritrade. TD Ameritrade debits our monthly fee directly from client accounts.

Other Fees or Expenses

Cape Ann Capital uses TD Ameritrade for custody and discount brokerage. Clients will incur brokerage and other transaction costs. Further information on brokerage is provided at Item 12 in this brochure.

TD Ameritrade currently charges our clients a \$24 commission whenever we buy or sell most mutual funds. All but one of the exchange traded index funds we use is commission-free. One carries a \$9.99 commission.

All mutual funds and exchanged traded index funds have internal operating expenses, which are debited from the fund and therefore paid by the client. Any fees charged by any mutual fund are the client's responsibility and are in addition to the fees charged by Cape Ann Capital.

Participation or Interest in Client Transaction

Cape Ann Capital receives no compensation for the sale of securities or other investment products and therefore has no incentive to select one investment over another.

ITEM 6: PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT

Cape Ann Capital does not accept performance-based fees, flat fees or hourly fees.

ITEM 7: TYPES OF CLIENTS

Cape Ann Capital provides investment advisory services to:

- individuals,
- profit sharing plans
- trusts,
- corporations, and
- charities.

Generally, Cape Ann Capital does not require a minimum account size.

ITEM 8: METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS

Methods of Analysis and Investment Strategies

In most cases, Cape Ann Capital invests exclusively in actively managed mutual funds and exchange traded index funds.

Cape Ann Capital regularly evaluates every mutual fund in the country to identify those that have outperformed their benchmarks over the long term with a consistency that is very unlikely to have been achieved by chance. Cape Ann Capital employs various research tools to conduct ongoing analyses of these funds. Cape Ann Capital typically draws on its proprietary research to select a diversified mixture of actively managed mutual funds and then adds exchange traded index funds if necessary to provide exposure to sectors not covered by the actively managed funds. The active and indexed proportions within the portfolio depend on Cape Ann Capital's ability to identify actively managed funds with convincing evidence of skill in delivering returns above what can be achieved with index funds.

Cape Ann Capital uses a multi-factor risk model to measure the effective asset allocation history of each mutual fund and to calculate a unique reference benchmark that is appropriate for each manager. This allows measuring a value manager against a value index, a bond manager against a bond index, a small cap manager against a small cap index, etc. Cape Ann Capital then calculates each manager's average excess return, the consistency of the excess return and a t-statistic that reflects the probability the result could have occurred by chance.

Cape Ann Capital looks at additional factors such as investment process, corporate culture, management tenure, expense ratios, portfolio turnover and load structure to arrive at a final Buy List. Cape Ann Capital reviews its Buy List at least once a year to ensure that it always reflects the most skillful managers available.

Constructing Portfolios: Cape Ann Capital constructs a unique portfolio for each client. Every Cape Ann Capital client commits to a long-term asset allocation target. Cape Ann Capital seeks to create a portfolio from the Buy List that meets this target. Cape Ann Capital uses an optimizer and a multi-factor risk model to solve for the target weights that minimize risk relative to each client's benchmark. The optimizer tells us which mutual funds to select from the Buy List and what the target weight for each fund should be.

Cape Ann Capital's software identifies the target weights that come closest to aligning the asset allocation of the client's portfolio with the asset allocation of the client's benchmark. The analysis takes account of the risk of each asset and the correlations among the assets. Cape Ann Capital sets lower and upper bounds on the calculation.

If the optimal portfolio is not within tolerance, Cape Ann Capital adds exchange traded index funds to bring the portfolio in line. We use a statistic called tracking error to monitor each portfolio's risk relative to its benchmark. Cape Ann Capital strives to keep tracking error under 2%. A portfolio with a tracking error of 2% has a high likelihood of performing within plus or minus 2 percentage points of its benchmark on an annual basis.

Why Mutual Funds: There are many investment vehicles available to investors. Cape Ann Capital prefers mutual funds for the following reasons:

Transparency: Mutual funds provide a transparent investment vehicle with a publically available track record. Net asset value is reported daily. The SEC carries out regular audits of mutual fund operations, independent directors oversee fund activities, independent auditors scrutinize fund financial statements and fund assets are held by independent custodians. These characteristics allow us to evaluate all mutual fund managers on a consistent basis. In our view it is very difficult to compare hedge funds or separately managed accounts as these vehicles are less regulated, performance is often not readily available and not all are registered with the SEC.

Professional Management: If a skillful management team can achieve a higher return, net-of-expenses than the return of the asset classes in which they invest, this benefit accrues to the shareholders of the fund. Investors do not have to pay more for the services of a skilled manager vs. an unskilled manager. Investors would certainly be willing to pay a premium for skilled management, but because mutual funds exchange shares at net asset value the services of a skilled manager costs no more than the services of an unskilled manager. Cape Ann Capital seeks to identify mutual fund managers with more than enough skill to overcome the expenses of their fund and the expenses of Cape Ann Capital.

Diversification: A single share of a mutual fund provides an investment in many individual securities.

Lower Trading Commissions: Because mutual funds trade in large volume, they can negotiate much lower commissions when buying and selling securities.

Liquidity: Mutual fund shares are redeemable on a daily basis.

Load vs. No Load: Mutual funds come in two types; load funds and no-load funds. A load is a commission that goes to the salesperson who markets the fund. Cape Ann Capital's fund selection is driven by our fiduciary responsibility as a registered investment adviser. In that regard, we never buy load funds. Since no-load mutual funds do not have a sales force marketing their shares, they must rely primarily on performance to compete. Since expenses detract from performance, no-load funds tend to have lower expense ratios than load funds.

Risk of Loss

An investment in a mutual fund or an exchange traded fund involves a risk of loss which a client should be prepared to bear.

Client portfolios are generally invested in ten to twenty mutual funds depending on the asset allocation being targeted. For most clients we are able to achieve our target tracking error without using any exchange traded index funds. For very small portfolios and some unusual asset allocation targets we are forced to use exchange traded index funds. No single actively-managed mutual fund can be more than 30% of a client's portfolio. There is no limit on the percentage of a client's portfolio that can be invested in a single exchange traded index fund.

The mutual funds invest in stocks and bonds as well as various derivative contracts such as foreign currency contracts, futures contracts, options contracts and swap agreements.

Investing in securities markets is risky because securities markets fluctuate in value. These fluctuations may be due to political, economic or general market circumstances. Other factors may affect a single company or industry, but not the broader market. Because the values of securities fluctuate, portfolios managed by Cape Ann Capital may decline in value.

Investments in derivative instruments carry exposure to various risks such as, but not limited to, interest rate and foreign currency risk. Interest rate risk is the risk that a fixed income security will decline in value because of changes in interest rates. Foreign currency risk is the risk that a foreign currency or a security that is denominated in a foreign currency will decline in value. Derivative contracts also carry counter party risk; i.e. the risk that the entity on the other side of the contract will default.

All of these risks are mitigated by the fact that Cape Ann Capital portfolios hold numerous mutual funds and each mutual fund holds hundreds or even thousands of securities. Through all of this diversification Cape Ann Capital believes it is able to eliminate most of the idiosyncratic risk in client portfolios. Systematic risk can be controlled, but not eliminated. Each client commits to a long-term asset allocation target and commits to the systematic risks associated with that target. One of the largest risks born by Cape Ann Capital clients is the risk that they will capitulate on an aggressive asset allocation after suffering an extended period of market value declines and thereby convert an unrealized loss to a realized loss.

ITEM 9: DISCIPLINARY INFORMATION

Cape Ann Capital has never been involved in any kind of disciplinary proceeding in any court or with the SEC or with any other federal, state or foreign regulatory authority.

ITEM 10: OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS

Broker-Dealer Registration

We do not have a registration or an application pending to register as a broker-dealer or a registered representative of a broker-dealer.

Futures, Commodity Pool Operator, Commodity Trading Advisor

We do not have a registration or an application pending to register as a futures commission merchant, commodity pool operator, a commodity trading advisor, or an associated person of the foregoing entities.

Related Person Arrangements

Neither we nor any of our management persons have any relationship or arrangement that is material to our advisory business or to our clients that we have not otherwise disclosed.

Arrangements With Other Investment Advisers

We do not recommend or select other investment advisers for our clients nor do we have other business relationships with those advisers that create a material conflict of interest.

ITEM 11: CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING

Code of Ethics

Cape Ann Capital has a Code of Ethics that provides the standard of conduct for all employees. The Code is somewhat unusual in that it requires that *all employees have all of their personal investment managed by the company*. Employees are not allowed to own or otherwise have a beneficial interest in any securities held in an account not managed by the company. Employees are not allowed any personal trading and their portfolios receive no preferential treatment over client portfolios. Every employee is held to a strict fiduciary standard which requires that they always act in the best interest of the client and to treat all clients fairly. A copy of the Code is available upon request.

The Code of Ethics requires that all employees will conduct themselves in accordance with high ethical standards, which should be premised on the concepts of integrity, honesty and trust.

The following is a summary of certain provisions of the Code of Ethics:

Confidential Information: As an investment adviser, we have a fiduciary duty to our clients not to divulge or misuse information obtained in connection with our services as an adviser. Therefore, all information, whether of a personal or business nature, that an employee obtains about a client's affairs in the course of employment with us should be treated as confidential and used only to provide services to or otherwise to the benefit of the client. Such information may sometimes include information about non-clients, and that information should likewise be held in confidence. Even the fact that Cape Ann advises a particular client should ordinarily be treated as confidential. Cape Ann's Code of Ethics sets forth steps employees should take to help preserve confidential information.

Material Inside Information: The Code of Ethics advises employees that purchasing or selling securities on the basis of material nonpublic information for their own or a client's account or "tipping" is a crime.

Fiduciary Duty and Conflicts of Interest: Cape Ann and its employees have a fiduciary duty to Cape Ann's clients to act for the benefit of the clients and to take action on the clients' behalf before taking action in the interest of any employee or Cape Ann. Cape Ann and its employees must act for the clients' benefit and treat the client fairly. The manner in which any employee discharges its fiduciary duty and addresses a conflict of interest depends on the circumstances.

Unfair Treatment of Certain Clients vis-à-vis Others: The Cape Ann Code of Ethics contains policies relating to prohibiting employees preferring one client over another.

Personal Trading Policy: Each employee must submit an initial holdings report disclosing to the Cape Ann Chief Compliance Officer the identities, amounts, and locations of all securities owned in all accounts in which he or she has a "beneficial

ownership interest." In addition, each employee must disclose similar information within thirty (30) days after the end of each calendar year while employed by us. Such reports must be current as of a date not more than 45 days prior to the employee joining Cape Ann (for an initial report) or the date the report is submitted (for the annual report). Each employee must report to the Chief Compliance Officer within 30 days after the end of each calendar quarter all securities transactions in all of the employee's covered accounts during the preceding quarter.

Participation or Interest in Client Transactions and Personal Trading

Employee portfolios look just like client portfolios. Each employee selects a long-term asset allocation target and we run our optimizer to select the portfolio from our Buy List that comes closest to the employee's long-term asset allocation target.

ITEM 12: BROKERAGE PRACTICES

Selecting Brokerage Firms

Cape Ann Capital recommends TD Ameritrade for all client brokerage transactions. Cape Ann Capital reviewed other brokers' fees and services and believes that TD Ameritrade offers excellent service and a wide array of investment options at reasonable, competitive rates. Currently, TD Ameritrade offers about 14,000 mutual funds, about 3,500 of which can be purchased or sold with no transaction fee. Transactions in the remaining mutual funds are \$24 each way. TD Ameritrade assesses a \$49.99 redemption penalty for no-transaction-fee funds sold within 90 days of purchase. TD Ameritrade also offers 100 commission-free exchange traded index funds. Transactions in the remaining exchange traded funds are \$9.99 each way. As noted earlier, Cape Ann Capital generally invests only in mutual funds and exchange trades index funds for its clients.

Research and Other Soft Dollar Benefits

Cape Ann Capital accepts no research or soft dollar benefits from any broker.

Brokerage for Client Referrals

We do not consider whether we receive client referrals from a broker in selecting or recommending broker-dealers.

Directed Brokerage

We routinely recommend to our clients that they use TD Ameritrade for custody and for the execution of all mutual fund and exchange traded index fund transactions because of the reasons set out under the sub-heading "Selecting Brokerage Firms". Not all investment advisers recommend particular brokers to their clients. We have no affiliation or other economic relationship with TD Ameritrade. It is possible that another broker might offer lower fees for certain mutual fund and/or exchange trades

index fund purchases. Accordingly, there is the potential that we are unable to achieve the lowest price on client transactions when we use TD Ameritrade and the use of TD Ameritrade may cost our clients more money than the use of another broker. However, we believe that TD Ameritrade offers competitive pricing and service for mutual fund and exchange traded index fund transactions.

Aggregation of Client Accounts

Mutual funds exchange shares at the market close. All clients buying or selling that day receive the same price. Accordingly, we do not aggregate trades as we do not have to be concerned with one client getting a better price than another.

ITEM 13: REVIEW OF ACCOUNTS

Periodic Reviews

Cape Ann Capital reviews each client portfolio at least monthly. If the asset allocation of the portfolio is off target, we take steps to correct it. If any individual mutual fund is off target we take steps to correct that too.

Cape Ann Capital reviews every mutual fund in the country at least annually. If we identify a fund that has demonstrated a higher skill level than a fund on the Buy List we then go through our due diligence check list to determine whether we should make a substitution on our Buy List and adjust client portfolios accordingly.

Review Triggers

Cape Ann Capital monitors every mutual fund on the Buy List on a daily basis. If a fund displays a pattern of out-of-the-ordinary underperformance relative to its style benchmark, we drop it from the Buy List and from client portfolios.

Regular Reports

Cape Ann Capital provides a written Portfolio Review to every client every month. The Portfolio Review contains commentary on the markets, month-end holdings, portfolio performance for three intervals (since inception, year-to-date and latest month), performance of each individual holding for the latest month and all transactions for the month. TD Ameritrade sends monthly statements to clients as well. After year-end TD Ameritrade sends 1099s to clients and Cape Ann Capital sends realized gains reports.

ITEM 14: CLIENT REFERRALS AND OTHER COMPENSATION

Incoming Referrals

Cape Ann Capital does not pay anyone for referral business.

Referrals Out

Cape Ann Capital does not receive any income for referring business to anyone.

Other Compensation

Cape Ann Capital's only compensation is the monthly fee referred to in Item 5 of this brochure, which TD Ameritrade debits from client accounts. Cape Ann Capital does not have any arrangements under which we receive any economic benefit, including sales awards or prizes.

ITEM 15: CUSTODY

Except for two accounts for which David Umstead, a principal of Cape Ann Capital, acts as trustee, Cape Ann Capital does not have custody of client assets. All Cape Ann Capital clients use TD Ameritrade as their primary custodian. Investors for whom we are also the trustee, should carefully review and compare the statements we send with those account statements received from TD Ameritrade.

ITEM 16: INVESTMENT DISCRETION

Cape Ann Capital has investment discretion over all client accounts. All clients have given Cape Ann Capital limited power of attorney to execute trades on their behalf. In spite of having discretionary authority, we are more than willing to discuss pending transactions in advance if desired by the client. Once each client gives us a long-term asset target, they can be as involved or uninvolved as they wish in our investment process. Typically if a transaction will generate meaningful taxable income we will ask for client approval before making the trade.

ITEM 17: VOTING CLIENT SECURITIES

If a client so desires, Cape Ann Capital will accept the authority to vote proxies on their behalf.

Proxy Votes

Cape Ann Capital's written Proxy Voting Policy is available upon request. As Cape Ann Capital's clients generally invest in mutual funds and exchange traded index funds rather than directly in securities, this issue is not of the same importance that it otherwise would be. Our objective in voting proxies is to support proposals and director nominees that maximize the expected long-term value of client investments. Proxy proposals are varied and complex. As such, Cape Ann capital's Proxy Voting Policy guidelines can only provide a framework for assessing each proposal. The Policy

stresses Cape Ann Capital's role as a fiduciary with responsibility for evaluating each proposal on its merits, based on particular facts and circumstances as presented. Cape Ann Capital gives substantial weight to the recommendations of the company's board, absent other specific facts that would support a vote against management.

ITEM 18: FINANCIAL INFORMATION

Since Cape Ann Capital invoices its fees in arrears, it is not required to include a balance sheet for its most recent fiscal year.

ITEM 19: REQUIREMENTS FOR STATE-REGISTERED ADVISERS

Cape Ann Capital is an SEC registered adviser and not a state-registered adviser.
