December 31, 2009

DK EQUITY GROWTH FUND

DEANS KNIGHT
CAPITAL MANAGEMENT LTD

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Quarterly Review

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Rates of Return[1]

	3 Mths	1 Yr	2 Yrs	3 Yrs	4 Yrs	5 Yrs	10 Yrs	15 Yrs	Since Inception March 31,1993
DK Equity Growth Fund	**14.4%**	**60.5%**	**-7.5%**	**-4.4%**	**8.2%**	**12.9%**	**20.9%**	**17.5%**	**18.1%**
S&P/TSX Composite Index	3.9%	35.1%	-4.9%	-0.2%	3.9%	7.7%	5.6%	9.3%	9.6%
S&P 500 (in U.S.Dollars)	6.0%	26.5%	-10.7%	-5.6%	-0.7%	0.4%	-0.9%	8.0%	7.6%

As Yogi Berra once said, *"you can observe a lot by watching"*. We can observe a lot and learn a lot by looking back not only at 2009, which was a historic year in many ways, but also by looking at the past decade, which counted a variety of events never seen before in our lifetime.

Let's wind back to the beginning of this past year. We entered 2009 mired in the worst global recession since the 1930's. We had witnessed the collapse of Lehman Bros., the biggest bankruptcy in global history. The global banking system was on its knees and by March, the major North American (and many global) indices had declined by 50% or more from their previous peak levels. Major governments and central banks pumped unprecedented billions of dollars into the global economy to rescue teetering industrial giants and financial intermediaries. And then, remarkably, since March, we witnessed the biggest rebound in North American stock market indices on record. In 2009, the TSX was up 55.2% from the March lows, the Dow Jones up 59.3%, and the S&P 500 up 64.8%.

Looking back on the past decade, known now as the "aughties" or the "double o's", we began with the media scaring the wits out of us about Y2K. Remember, computers were going to crash, planes were going to fall from the sky, and stock markets were going to tank, all because systems were not built to handle the date 2000. We entered the decade with the biggest stock market folly since the tulip mania . . . the tech stock bubble. That is the bubble that told us Nortel was really worth $450 billion, when it turns out it was closer to zero. When the bubble popped later in 2000, more total wealth was lost in the ensuing tech bear market than in any market correction ever before. On 9/11, we witnessed the biggest loss of life on U.S. soil in history, as a result of the terrorist attacks on the World Trade Center and the Pentagon. This was coincident with a recession in the U.S. We saw Avian flu scares; Swine flu scares; food scares (human and pet); Hurricane Katrina, the

[1] Returns longer than one year are annualized.

costliest hurricane and one of the deadliest in U.S. history; the election of a black President; the Enron and WorldCom bankruptcies and corporate scandals; and the invasions of Afghanistan and Iraq. We watched the real estate lending practices in the U.S. become ridiculously sloppy. Credit to buy homes became available to anyone who was breathing, and this resulted in the biggest real estate bubble in history. When rising real estate prices became unsustainable, the prices began to turn lower in late 2006; the resulting mortgage defaults sent seismic shockwaves through the global financial system and brought us to where we are today.

"Observe a lot by watching" . . . none of the major events of 2009, or the major events of the past decade were predictable or predicted. We have written many times over the past 18 years about the folly of making predictions. However, we humans have a basic need to predict and control future events, even though it has been proven we cannot do it. We still fool ourselves by taking comfort in the misplaced belief that some pundits have the capacity to tell us what will happen, where the "market" will go, where the economy will go. Basic fundamental advice to clients . . . if you ask your financial advisor what the market will do in 2010, and they give you any answer other than "I do not know". . . get a new advisor.

The most important fundamental to understand for investors is to "know what you do not know". Those investors that do not are ultimately doomed to failure. Never forget what Confucius say, *"forecasting is difficult, especially the future"*.

That we cannot predict the future, is the single most important lesson we have learned over 40 years in the financial business. Another important lesson we have learned is, that of those who think they can, their predictions are overly influenced by the tone of current events or most recent events, as reported by various forms of media . . . positive or negative. When the media is positive, most pundits are bullish. When the news is negative, they are bearish. In fact, most humans respond to uncertainty in particular, with more emotion – fear, blame, paralysis – than is advisable. Uncertainty has a nasty way of making us imagine the worst outcomes.

When we began 2009, the world was bearish. However, the outcome was surprisingly positive. When we entered the last decade, the pundits were overwhelmingly bullish. It was a new "technology era". Fundamental principles of valuation no longer applied. It was to be a golden decade. However, what resulted was the worst decade of U.S. stock market performance ever, including the 1930's with the S&P 500 (-0.9% annualized). Canada fared little better, with the TSX annualizing a return of 5.6%, well below the long-term trend line.

Those who have followed these pages over the years have NEVER witnessed a single economic or market prediction. I believe we understand what we don't know, and attempt to focus our time and efforts on what we do know. What we do know is what we can see and measure in the present, not the future.

What we strive to do is find, and buy into, businesses that have something of overlooked, measurable value. It is also important for us to have a shared understanding, and a trusting relationship with the management of the companies in which we are involved. It is the same type of relationship that we strive to have with our clients.

In our experience, the best time to purchase businesses is when the economic environment is negative, when the media is peddling doom and gloom, and the pundits are bearish. Conversely, it is wise to be cautious when the mood is buoyant.

We have also learned that you don't always have to get it right. In fact, as Bill Gates has said, *"success is a lousy teacher"*. We have gotten many things wrong over the years, and this is where we have learned. Not all of our investments have panned out, but fortunately, many have.

Our results over the past decade (annualized return of roughly 21%) demonstrate that we do not need to be able to tell the future and we do not need to always get it right . . . and we do not need to trade. What we need is a number of companies that can deal with obstacles thrown in their paths, that can solve problems, that can grow their businesses with efficient use of capital, and that can create enhanced value for the owners over many cycles. What we also need is our unique network of very knowledgeable brokers, analysts, industry contacts, friends, and clients, all of whom help in identifying and vetting investment opportunities.

What should we be doing today? Well, firstly let's stop worrying about the future that we can't predict. Let's stop worrying about what the market will do in 2010. Let's focus on our businesses and ensure that we own those that meet our two main criteria – some measurable overlooked value and a shared understanding and trust relationship with management.