March 31, 2010

DK EQUITY GROWTH FUND

DEANS KNIGHT
CAPITAL MANAGEMENT LTD

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Quarterly Review

March 31, 2010

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	**16.9%**	**87.7%**	**4.4%**	**-0.8%**	**7.6%**	**13.9%**	**23.3%**	**18.0%**	**18.9%**
S&P/TSX Composite Index	3.1%	42.1%	-2.0%	0.0%	2.7%	7.4%	4.7%	9.3%	9.6%
S&P 500 (in U.S.Dollars)	6.2%	50.9%	-3.3%	-3.9%	-0.2%	2.1%	-0.6%	7.8%	7.9%

Looking back over the past 12 months is very instructive. The broad North American measures of stock market values hit their correction lows in the early part of March 2009. The TSX had lost 50% of its value, the Dow Jones 54%, and the S & P 500 57% . . . the most severe bear market since the 1930's. However, between that time and the end of this calendar quarter, these same indices have appreciated by roughly 60 - 70% . . . the biggest post bear market rally in the history of North American stock exchanges.

One year ago who could have predicted this outcome?

Rewind to March 2009 . . . investors, the media, the analysts, were all paralyzed by fear. The consensus promoted by the media was that the world as we knew it had come to an end. The media promoted panic at a time when common sense and calm were required. As we pointed out in these pages in late 2008, there had been 20 stock market corrections, prior to this one in North America, since 1900. We asked the question . . . how many recoveries from those corrections had there been? The answer . . . 20. Our readers know that we avoid making sweeping predictions. However, based on history, it was highly probable that following this 21st stock market correction, there would be a recovery. This is not about making a bold prediction. This is simply common sense. As a wise man once said "*there seems to be a perverse human characteristic that likes to make easy things difficult*".

One year ago, many of our holdings were valued in the market at levels that suggested they were no longer going concerns. High quality car parts companies were valued as if the world would stop buying cars; lumber companies were priced as if no more homes would be built; copper producers as if the world would no longer use the metal. With the benefit of hindsight, this thinking was totally irrational.

[1] Returns longer than one year are annualized.

Two of Warren Buffet's simple rules should always apply:

"Attempt to be fearful when others are greedy, and to be greedy when others are fearful."

and in his most recent letter to Berkshire shareholders when referring to the many attractive opportunities available one year ago . . .

"When it's raining gold, reach for a bucket, not a thimble."

Has greed returned and should we be fearful? We don't think so. There is still a healthy dose of skepticism out there. There is a lot of concern about the global economy; government deficits; the sorry state of the U.S. consumer; the U.S. housing market; the U.S. commercial real estate market; and more. Greed will surface at some point, but it does not feel that way yet.

We have written about our lack of skill regarding predicting the future of economies and markets many times in our letters to clients. We have also had the temerity to suggest that the rest of the economists, analysts, and market pundits are no better than we are.

The biggest inhibitor to being able to see into the future is the fact that we are subject to the frailties inherent in being human. We are subject to being overly influenced by the mood of today, or the most recent past. In good times we speak of a new world order; this time is different; we have eliminated the business cycle. There was a lot of that going around prior to the 2008 meltdown.

Now the collective outlook is cautious because we are still strongly influenced by what has occurred in the past two years. Are we too cautious?

Let's look at some facts. These are not predictions. In 9 of the last 10 stock market recoveries from bear market lows (back to 1932) stock market indices gained in the second year of recovery from the bear market, albeit at a lesser pace. Will it happen again this year?

Moreover, looking at economic statistics, the past decade (2000 – 2009) in the U.S. was the worst on record since the 1930's. Key measures of economic performance such as GDP growth, personal consumption growth, personal income growth, and non-farm payroll growth for the past decade were at the lowest levels since the 1930's. And more importantly, in the past decade the U.S. stock market recorded one of its worst performances in nearly 200 years of recorded stock market history. In the past decade stocks traded on the S&P 500 lost an average of .2% per year, largely because of two big bear markets in the decade. Investors are disappointed big time. They had been lured into the market in a big way, fueled by the greed created by what they saw in the previous decade, the bull market of the 1990's. That bull market provided the best decade on record with average annual returns of over 18%.

The point is investors entered the 2000's with a sense of optimism which was driven by what they had seen in the previous decade. Similarly, investors enter this decade, jaded and cautious because of what they witnessed in the previous decade. Fact . . . as rare as it is for the stock market to post losses for a 10 year stretch, it is even rarer for there to be two consecutive decades of losses. The last time this happened was in the 30's and 40's. The conclusion . . . this is not a prediction . . . just a common sense observation . . . it would not be unusual, given the level of concern and caution, if the stock market this decade did surprisingly well compared to the past decade.

The valuations on many of our portfolio companies continued to appreciate during Q1 of this year. These valuations are coming off extraordinary lows of March 2009. The gains continue to be driven by the gradually improving global economy; the improving operating environment for many of our businesses; and the gradual receding of the climate of fear and impending disaster that gripped the market in late 2008 and early 2009.

Although the market value of many of our companies increased in Q1, it is worth highlighting the contribution **Athabasca Oil Sands Corp.** made to the portfolio valuation in the past quarter. Athabasca was established a mere 3 years ago to acquire leases to explore and develop prospective acreage in the oil sands region of Northern Alberta. The oil sands is the second largest oil resource in the world next to Saudi Arabia. By late last year, the company had established a resource of approximately 10 billion barrels of oil in place. Athabasca sold a 60% interest in two of its development properties (keeping two) for $1.9 billion, and then this past month launched what has turned out to be, at $1.55 billion, the largest IPO in Canada since Manulife in 1999. In addition to the appreciation in share value, Athabasca shareholders received a non taxable cash dividend of $4.25 per share, a major contribution to the portfolio value. We plan to continue to be significant owners of the company because as we see it, Athabasca can continue to add barrels of oil to this resource and continue to add value for their shareholders.

Also worth noting, **West Energy** received a combination of cash and stock takeover bid from Daylight Resources Trust in early March at a value that represented a 25% premium to West's 10 day average weighted price. We have been involved with West since the Company's inception in 2003. We are large shareholders. We are pleased with the offer. We intend to support the transaction and intend to accept and hold Daylight Units in exchange for West shares.