September 30, 2015

DK EQUITY GROWTH FUND

DEANS KNIGHT

CAPITAL MANAGEMENT LTD

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Quarterly Report
September 30, 2015

Rates of Return[1]

	3 Mths	YTD	2 Yrs	3 Yrs	5 Yrs	10 Yrs	15 Yrs	20 Yrs	Since Inception March 31, 1993
DK EQUITY GROWTH FUND	**-12.4%**	**-3.9%**	**8.1%**	**6.4%**	**3.0%**	**5.7%**	**15.1%**	**12.8%**	**14.5%**
S&P/TSX Composite Index	-7.9%	-7.0%	5.0%	5.7%	4.5%	4.8%	4.2%	7.9%	8.4%
S&P 500 (in U.S. Dollars)	-6.4%	-5.3%	9.1%	12.4%	13.3%	6.8%	4.0%	8.1%	8.8%

The U.S. and Canadian stock market indices have had a correction in the past few months. From peak to trough the S&P/TSX declined by 16% and the U.S. S&P 500 12%. We commented on this in the interim note to clients dated August 25, 2015. It is always worth rereading what we wrote and we have attached a copy with this report (Appendix I). The most important take away from that note is market corrections (-10%) and bear markets (-20%) are not abnormal events.

The weakness in the oil price has been in the headlines regularly for the past year. We have also included a separate note that we prepared for non-Canadian investors who have recently made inquiries of us asking about the opportunity in Canadian oil and gas (Appendix II).

The obvious question about share prices now is "*will the correction become a bear market*?" (a decline of 20% or more). As we pointed out in our August note, bear markets are not unusual. They have occurred on average every 6 years over the past 70 years. So, it would not be out of the ordinary for this correction to become deeper and track into bear market territory. That is not a prediction. It is simply an observation.

It has been 6 years since the last bear market . . . 2008/2009. That one was big, and it coincided with a financial panic and a recession. We do not make market predictions . . . but circumstances are quite different today than at the time of the last bear market. The U.S. economy is growing. Canada, after negative growth in the first half of this year (severe winter weather and lower oil prices) has shown positive growth in July. The global economy is also growing at a rate of 2.5 – 3%. It is not impossible, but it is unlikely to see a severe bear market in an environment of continued growth. Again, not a prediction, just an observation.

[1] Returns longer than one year are annualized gross of management fees.

We cannot control nor predict market action . . . bull markets, corrections, bear markets . . . If we can accept that thesis, then we are best to spend our time working with the CEO's that run our companies to ensure that operations are on plan, and in addition to that, looking for value opportunities.

There were a number of developments concerning our companies during this past quarter, all on plan, and all indicating the continued creation of long-term shareholder value. To us, this is much more important than short-term share price action.

Héroux-Devtek Inc. . . . our landing gear and manufacturing business is our largest shareholding. If you recall, Héroux-Devtek is the third largest landing gear designer and manufacturer in the world, serving the commercial and military markets. On September 18, 2015, Héroux-Devtek Inc. announced that they were awarded a new long-term contract to design, develop, fabricate, assemble, test, and deliver complete landing gear systems for AgustaWestland's new AW609 aircraft. AgustaWestland is the fourth largest helicopter manufacturer in the world. The nature of the contract is significant. It further validates Héroux-Devtek's position in the industry as a Tier 1 supplier, providing value-added turnkey solutions for complete landing gear systems.

In August, Warren Buffet's Berkshire Hathaway Inc. made its largest ever acquisition . . . paying $37.2 billion for Precision Castparts Corp. Precision Castparts is one of the largest suppliers in the world of aerospace components. In fact, Héroux-Devtek sold their industrial division to Precision Castparts in 2012 and with part of the proceeds the Company paid us a whopping $5 dividend. Héroux-Devtek sold this nonstrategic division in order to concentrate on landing gear design and manufacture. The point is that Buffet likes the aerospace industry . . . and he likes it a lot.

We have also studied a copy of a September report on the aerospace industry from the Teal Group. Teal is a leading Virginia-based aerospace and defense market intelligence analysis and forecasting group. The headline of the report says it all:

"Still Doing Better Than Any Other Industry"

The report shows strong trends in dollar value of deliveries of new aircraft (civil is outpacing military); strong airline traffic numbers; growing backlogs; recurring orders for business aircraft. Moreover, the report also points out that Boeing's 777/X aircraft program, where Héroux-Devtek was selected as the sole supplier of landing gear, is estimated to be the world's fourth largest aviation program over the next 10 years.

AutoCanada Inc. continued to make acquisitions and expand its network of auto dealerships.

On August 24, 2015, AutoCanada announced the acquisition of a GM dealership in Kelowna, B.C. and then on September 28, 2015 they announced the acquisition of Grove Dodge Chrysler Jeep in Spruce Grove, Alberta (a suburb of Edmonton). This brings AutoCanada to 50 dealerships, one of Canada's largest multi-location automobile dealer groups.

Winpak Ltd., our packaging company, announced a special dividend of $1.50 per share, payable October 15, 2015. The total amount to be paid is $97.5 million. Winpak had $190 million of cash on the balance sheet at the end of Q2, with no debt. Special dividends from Winpak are not unusual. They paid us a special dividend in March 2014 of $1 per share.

Uni-Select Inc. is the largest distributor of automotive paint in North America and the largest distributor of after-market auto parts in Canada. In Q2, Uni-Select closed on the sale of their U.S. parts division to Carl Ichan and paid down all of their debt. Uni-Select is now in a strong position to make acquisitions. The Company announced 7 acquisitions over the past quarter . . . 3 automotive paint distributors in Colorado, Wisconsin, and Northern California; an auto parts distributor in Atlantic Canada; one on Vancouver Island and two in Quebec. At the close of Q2, Uni-Select had $78 million cash on hand and no debt. Uni-Select continues to return money to shareholders through their normal course issuer bid and a modest 1.1% dividend yield.

Cott Corporation continues to expand its operations and to diversify its business base. Cott's transformative acquisition of DS Services of America, Inc., late in 2014, took Cott's carbonated soft drink business to below 20% of total revenues. DS Services is one of the largest direct-to-office/home, water and coffee delivery providers in the U.S. The Company's footprint covers approximately 90% of the country. Following the closing of a $150 U.S. equity issue June 3, 2015, Cott redeemed a like amount of outstanding preferred shares. The preferreds had a restrictive clause prohibiting acquisitions. Subsequently, DS Services has made two acquisitions, one in Pennsylvania and another that serves South Carolina, Georgia and Florida.

In recent weeks, we have seen a pick-up in the number and size of deals in the Energy sector. As we said in our August letter (Appendix II), the cheapest place to buy a barrel of oil today is on the TSX. Since this quarter ended, Suncor Energy made a $4.3 billion hostile bid for Canadian Oil Sands and Encana announced a $900 million asset sale to the Canadian Pension Plan. We are also awaiting an announcement of who will purchase an asset package from ConocoPhillips, which is expected to be worth nearly $1 billion. The assets, which were put up for sale earlier this year, are producing 35,000 boepd in Western Canada.

Pinecliff Energy Ltd., one of our core holdings, has put its hat in the ring to bid on parts of these Conoco assets. Pinecliff has been opportunistically acquiring natural gas properties since its founding in 2012. The Company currently produces 12,000 boepd of low cost, low decline natural gas. We have known the Founder and Executive Chairman, George Fink, for over 20 years. He is a proven operator and value creator. The management team is committed to the Company and collectively owns 16% of the stock, mostly George Fink and CEO, Phil Hodge. We would not be surprised to see this team add significant value to the Company in the near term. Whether it be part of these Conoco assets, or something else, we have great faith in this management team's ability to execute the best deals for shareholders by acquiring quality assets at competitive prices.

It is important to note in our attached piece about the opportunities in Canadian oil and gas today; that our companies, Pinecliff included, continue to grow production and resources per share in spite of the lower commodity price environment.

Appendix I **August 25, 2015**

CORRECTIONS AND BEAR MARKETS:
THE STOCK MARKETS
THE CANADIAN DOLLAR

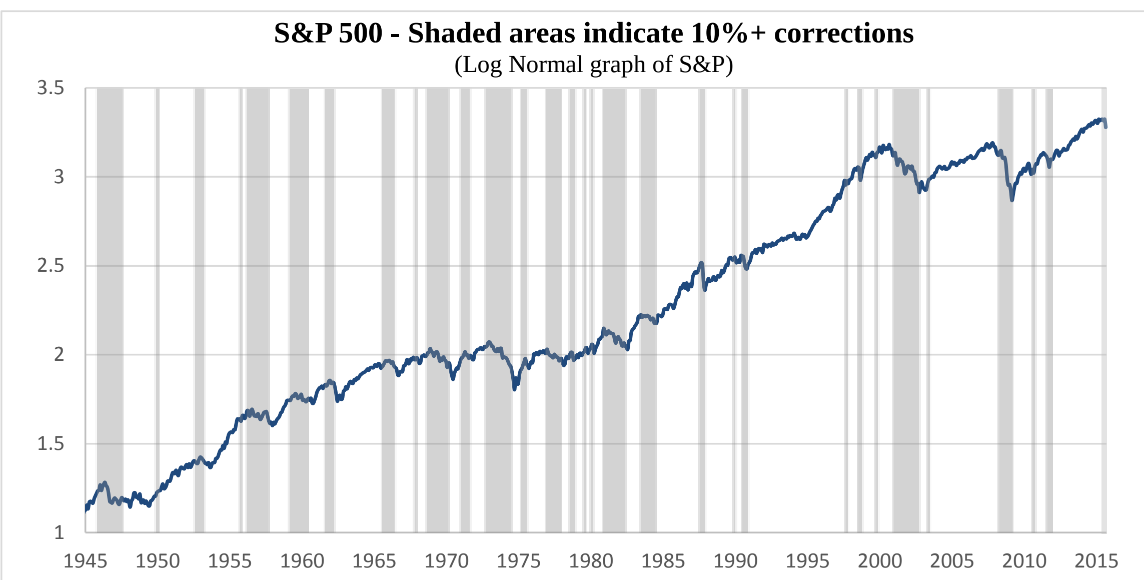
We have seen this movie before. Many times. Big news lately . . . Global Stock markets are "plunging". The "Canadian dollar hammered by oil rout". This is not the first time, nor will it be the last. Based on our experience, if we can gain an understanding of the context of these events it can be helpful in understanding what might happen in the future.
"... It is not so difficult to foresee what will happen, but it is difficult to determine when it will happen."

THE STOCK MARKETS

Let's focus on the North American stock markets. As a matter of common practice, we have come to define a stock market correction as a decline from peak to trough of at least 10%. Moreover, we define a bear market as a decline of 20% or more. All three broad measures of the North American Stock market indices are into market correction territory. The Toronto TSX has declined 16% from its peak of 15,451 reached on April 15, 2015. The U.S. Dow has declined 13% and the U.S. S&P500 has declined 11%.

History has taught us that corrections, and bear markets, are normal occurrences. They recur with regularity along with changes in economic activity and with investor mood swings.

Looking back over the past 70 years, (the post WWII period) and using the broad S&P500 Index as a measure, the market has had corrections (-10% or more) on 34 occasions. In other words, on average every 2 years. On 12 of those occasions, the declines have extended beyond 20% into bear market territory, on average every 6 years.



The takeaway from the graph…corrections and bear markets are not abnormal. Moreover, every market correction and bear market has been followed by a recovery that ultimately has taken the index higher than the previous peak.

How far will the indices decline this time? Neither we, nor anybody else, knows. Will the market recover at some point? Yes.

The financial media would have us believe that the end of the world is at hand. A sample from headlines from last week:

'Stocks Fall Most in 4 Years as China Dread Sinks Global Markets'
- Bloomberg News, August 20, 2015

'Global Stocks in "Panic Mode" as Chinese Factory Slump Drags on Markets'
- The Guardian, August 21, 2015

This type of reporting occurs with every market downturn. It is useless information and noise.

In times like this we like to remind readers of our 20th Anniversary book that we published in 2012, ***"Don't Listen to Everybody With an Opinion . . . 20 Lessons Learned".*** (For those who do not have a copy of the book, or have misplaced it, feel free to contact us for one.)

These lessons are worth rereading from time to time, particularly during market downturns. We draw your particular attention to four of these lessons…..

No. 4 *'If Your Financial Advisor Says He Knows What's Going to Happen Next Year, Get a New Financial Advisor'* (page 29)

No. 7 *'Don't Get Your Investment Advice from the Media'* (page 49)

No. 8 *'Recessions and Bear Markets: Not Abnormal and Not All Bad'* (page 55)

No. 13 *'Mr. Stock Market is Bipolar and Refuses to Take His Meds'* (page 81)

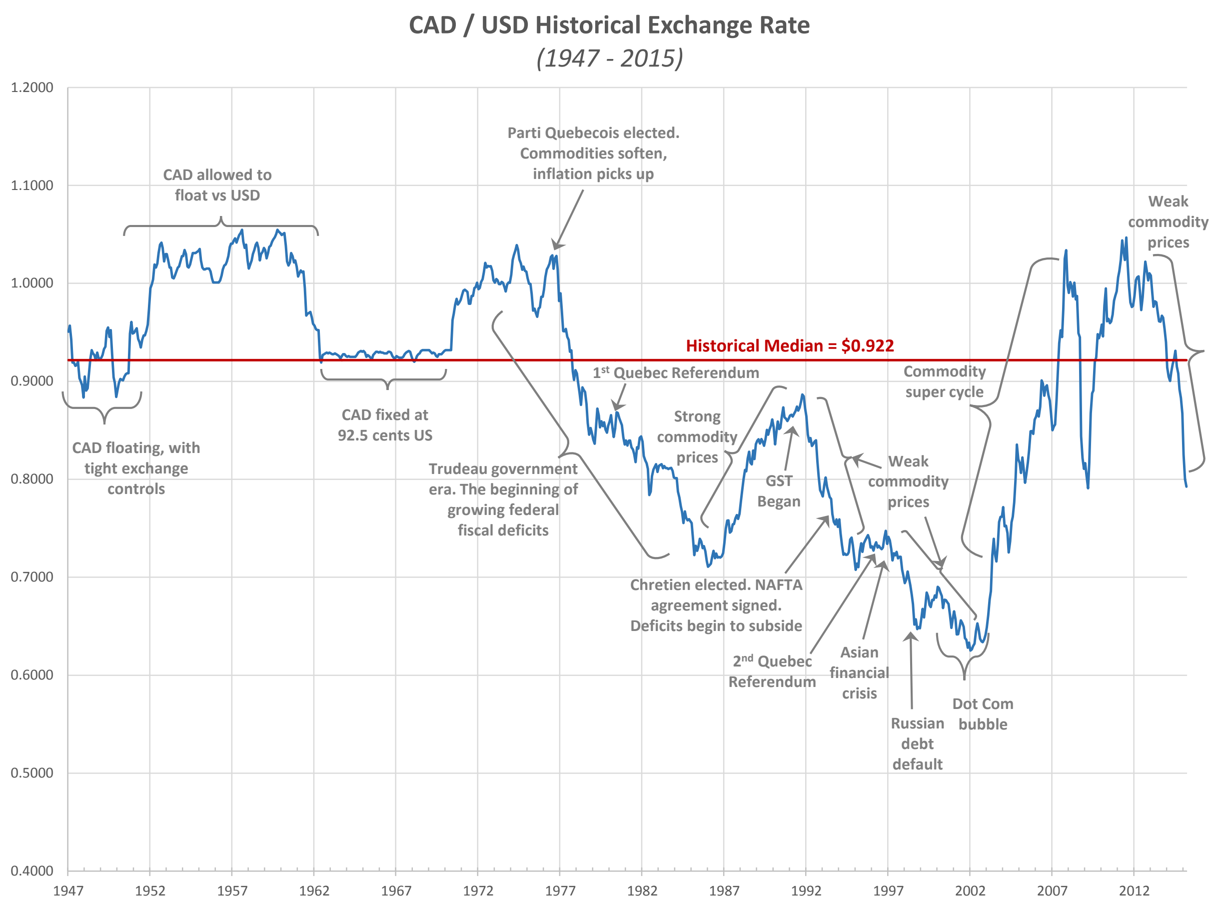
All of these lessons apply today. Everybody seems to know what will happen, even though they don't; the media is rife with hyperbolic warnings of doom; it is as if we have never before witnessed a market decline; and Mr. Market is definitely in a depressive phase.

The blame for this correction is apportioned to the "China Dread" . . . that a slowdown in China's economic growth will lead to a global economic and financial collapse. Well perhaps . . . or perhaps not. The hype in the past decade that China would drive global growth and a commodity super cycle forever was, and is, unrealistic. We remind readers of what we wrote in our quarterly letter of June 30, 2011. In that note, we highlighted the math, and demonstrated that our generally accepted and expected economic growth rates are unrealistic and unsustainable. Click here to view the excerpt from our June 30, 2011 quarterly letter.

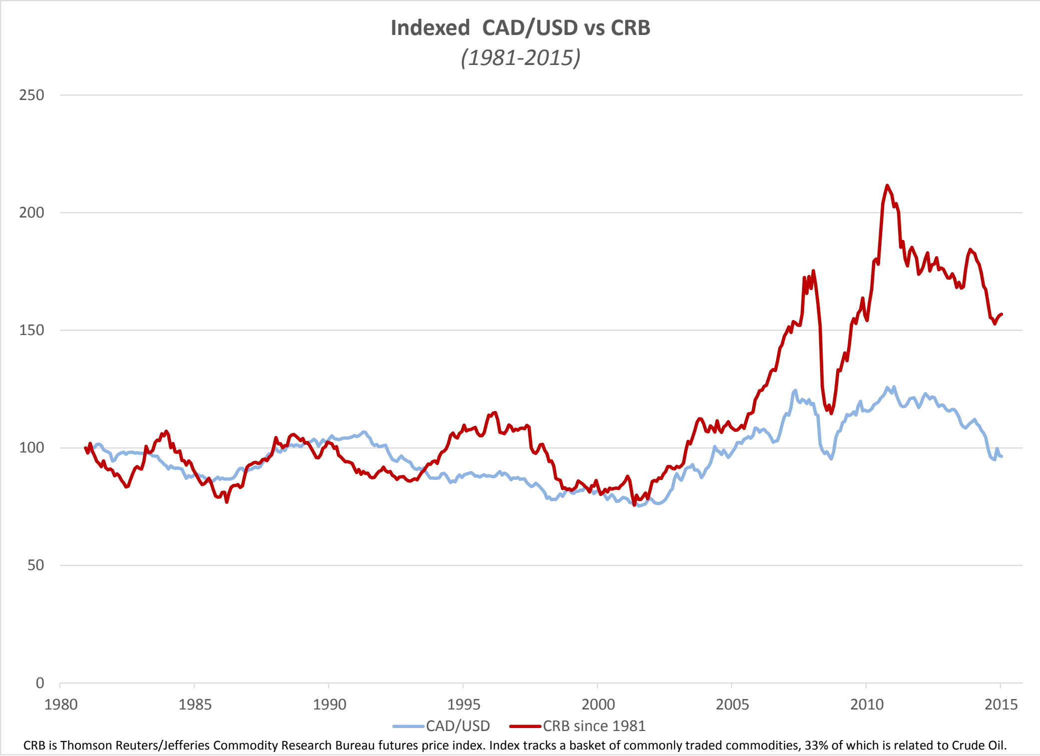
Following our visit to China in April 2012, we came away with the feeling that to ensure the health of its economy, China needed to deal with two things . . . corruption and pollution. The country's leaders are clearly tackling the first. They are doing it at a time when the economy is going through the difficult transition from an export driven economy to a more balanced economy. The changes and the transition will be difficult and challenging, but it is unlikely to be the end of the world.

THE CANADIAN DOLLAR

The other correction, which has turned into a bear market, is the Canadian dollar. Not that long ago the Canadian dollar was the darling global currency. We were lauded as a model of fiscal responsibility and discipline during the financial crisis and recession of 2008/09. Since a peak on July 21, 2011 of $1.06 versus the U.S. dollar, we have seen it decline to $0.75 U.S.



The trajectory of the Canadian dollar has demonstrated an uncanny correlation to commodity prices.



It appears that nothing much else matters outside of commodity prices, especially oil, which is the dominant commodity in the index. If we put aside the commodity index for a moment, Canada stacks up very well indeed.

In the past 10 years, all Group of Seven countries went through a severe recession, slow economic growth, and large accumulations of debt. Until early this year, Canada had the best rate of GDP growth and the smallest increase in debt of all the countries in the group. Canada's population is one of the fastest growing in the developed world, a critical ingredient for a strong economy. The Fraser Institute (ranked by the University of Pennsylvania as one of the top 20 think tanks in the world), measures the "Human Freedom Index" of 152 countries. More "Freedom" is a major determinant of a healthy long-term economic performance. The latest study ranks Canada 6th out of 152 countries. The U.S. ranks 20th, and has been slipping in the ranking over the years. China ranks 132. Moreover, Canada still carries the yoke of a country thought of as "hewers of wood and drawers of water". That no longer describes a country which today is 70% dominated by service and knowledge industries.

Overriding all of this fundamental background information is the angst in the media about the current oil price induced recession in Canada. Let's look at the facts. Q1 numbers show the Canadian economy contracted by 0.6%. The U.S. economy, by the way, contracted by 0.2%, which was blamed on severe winter weather. Guess what? We had the same weather, perhaps worse. April and May numbers for Canada came in slightly negative as well. Therefore, Canada has been through a technical recession in the first half of 2015 (by the definition of two quarters of negative GDP growth). What the media do not tell us is that it is highly likely the recession is now over. We are now in the third quarter and we will not get third quarter numbers for a while yet.

The price of crude oil (WTI) is down from a high in July of 2014 of $95.59 USD per barrel to roughly $40. What we are witnessing is an old-fashioned price war. . . a classic race to the bottom. We have seen this before in many different industries. “Let’s drive down the price and grab additional market share”. It seldom works. All producers are now suffering . . . OPEC and non OPEC. Price wars always end . . . badly for some, better for others. Who will blink first? We cannot tell you. But someone will. It makes no sense to continue to produce and sell non-renewable product below cost, and for many the current price is below full cycle all-in costs.

Justifiably or not, when the oil price bottoms, so will the Canadian dollar. But in reality, Canada is much more than oil. Canada has and will continue to punch well above its weight.

Appendix II **September 2015**

Looking at Canadian Energy From a Non Canadian Perspective

Deans Knight has been investing on behalf of clients for 22 years. We take a private equity approach to investing in the public markets. We own businesses, not stocks. Our belief is if you buy one share of a business, you should be prepared to own the entire company.

We look for businesses that have the following characteristics:

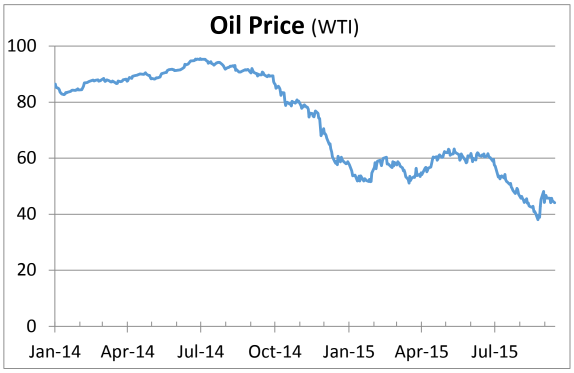
- Experienced and reputable management teams who are financially invested in their company.
- Low cost, efficient operations.
- A sustainable competitive advantage.
- Existing or potential recurring free cash flows.
- Strong balance sheets.
- Sum of the parts worth more than the whole.
- Hidden value.

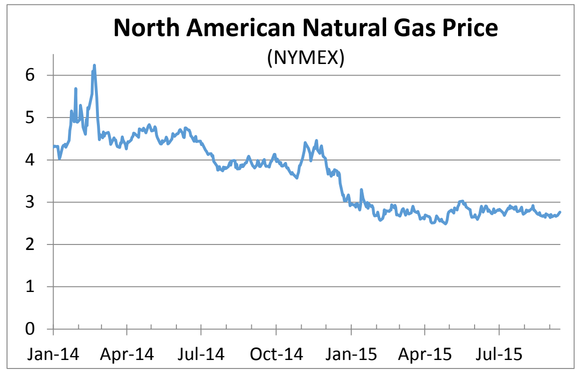
We are meaningful shareholders in a concentrated portfolio of businesses in a variety of industries. We target Canadian registered companies with assets and operations that reach globally. Our top ten holdings, (56% of the portfolio), include:

- **Heroux Devtek**: The world's 3rd largest manufacturer of aircraft landing gear.
- **Cott Beverages**: The world's largest producer of private label soft drinks, juices, alternative beverages, bottled water, and America's largest direct to home and office beverage delivery.
- **Winpak**: A leading manufacturer of consumer product packaging and packaging machinery.
- **Velan**: A global supplier of industrial valves for various industries.
- **West Fraser Timber**: The largest, and lowest cost, lumber producer in North America.
- **Uni-Select**: Canada's largest distributor of after-market auto parts, and the largest distributor of automotive paint in North America.
- **Linamar**: North America's 2nd largest manufacturer of auto parts.
- **Parex Resources**: A Canadian-based international oil producer with assets in Colombia.
- **Martinrea International**: North America's 3rd largest manufacturer of auto parts.
- **Tourmaline Oil Corp**: Second largest natural gas producer in Canada.

Our sweet spot has been acquiring positions in companies that have our target characteristics but are currently deeply out of favour with the market…..oil & gas.

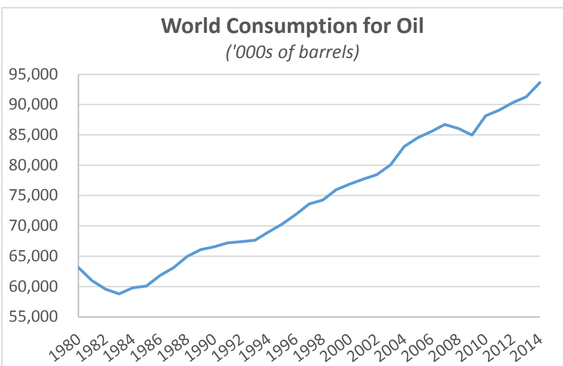
Over the past year, the price of both oil and natural gas have declined 60% from the 2014 peak.

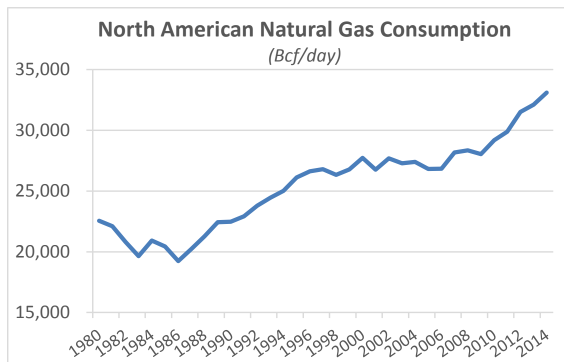




The dynamics of the oil and natural gas markets are different. Oil transports easily and trades at a global price. North American natural gas is largely land locked within the continent, and trades according to North American pricing.

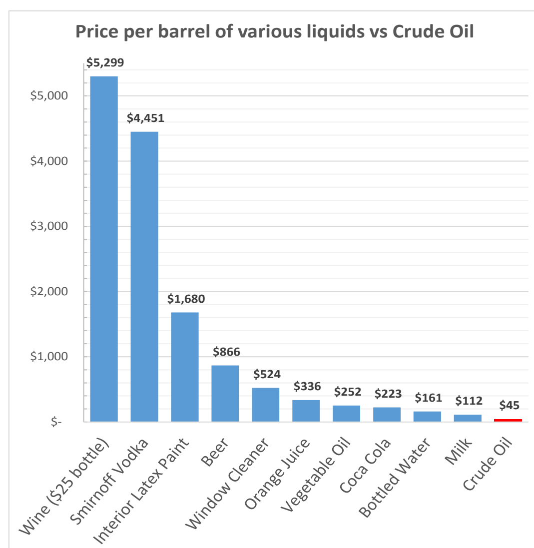
Consumption of both oil and gas have continued their steady upward march.





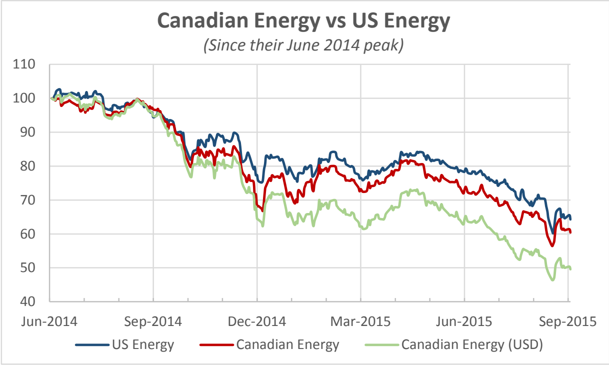
In the global oil market, we are witnesses to a typical price war. We've seen price wars before….they always end. Who will blink first? We do not know. But someone will. It makes no sense to continue to produce and sell non-renewable products so cheaply.

Notice the accompanying chart that compares the price of oil (a non-renewable resource) to various everyday renewable liquids.



The oil and gas markets will rebalance at some point. The strongest operators will not only survive, but will ultimately prosper.

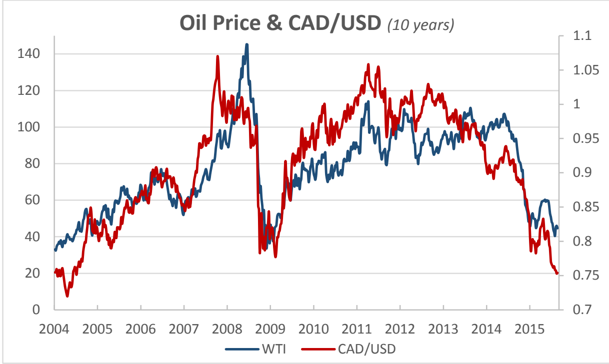
The US Energy Index and the Canadian Energy Index (in CAD terms) have both dropped similar amounts (roughly 38%) since their 2014 peak.



So why Canada?

Over the past year, the CAD has declined by more than 20% to a 10 year low of 75 cents. The Canadian Energy Index in USD terms has dropped 51%.

The Canadian dollar is closely correlated to the price of oil. A rise in the price of crude oil will likely trigger a rise in the Canadian dollar.



The cheapest way to buy a barrel of oil in the ground today is on the Toronto Stock Exchange. A sample of 45 TSX-listed energy companies showed they currently trade for less than $8 per barrel of reserve…..far cheaper than it costs these operators to explore and find new barrels.

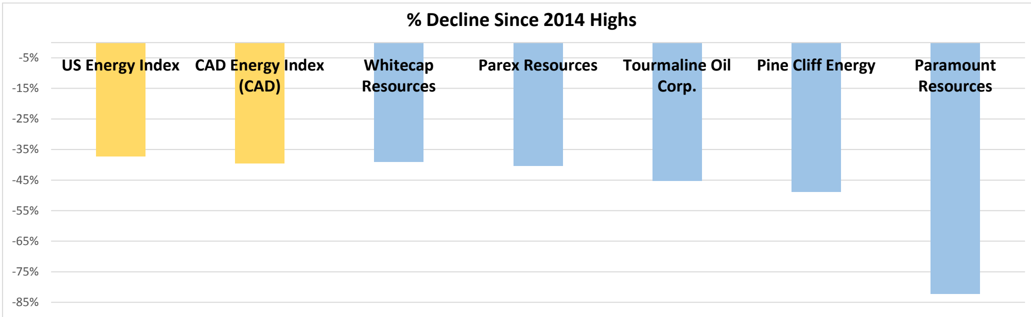
Canada has often been referred to as an "Energy Superpower". While it may only account for just 2% of world GDP and less than 0.5% of world population, Canada is ranked in the top 5 globally for the production of many of the major energy commodities.

Canada's position in global production of energy:

	Crude Oil	Natural Gas	Coal	Uranium	Hydro-electricity	BioFuels
Production	5th	5th	12th	2nd	3rd	5th

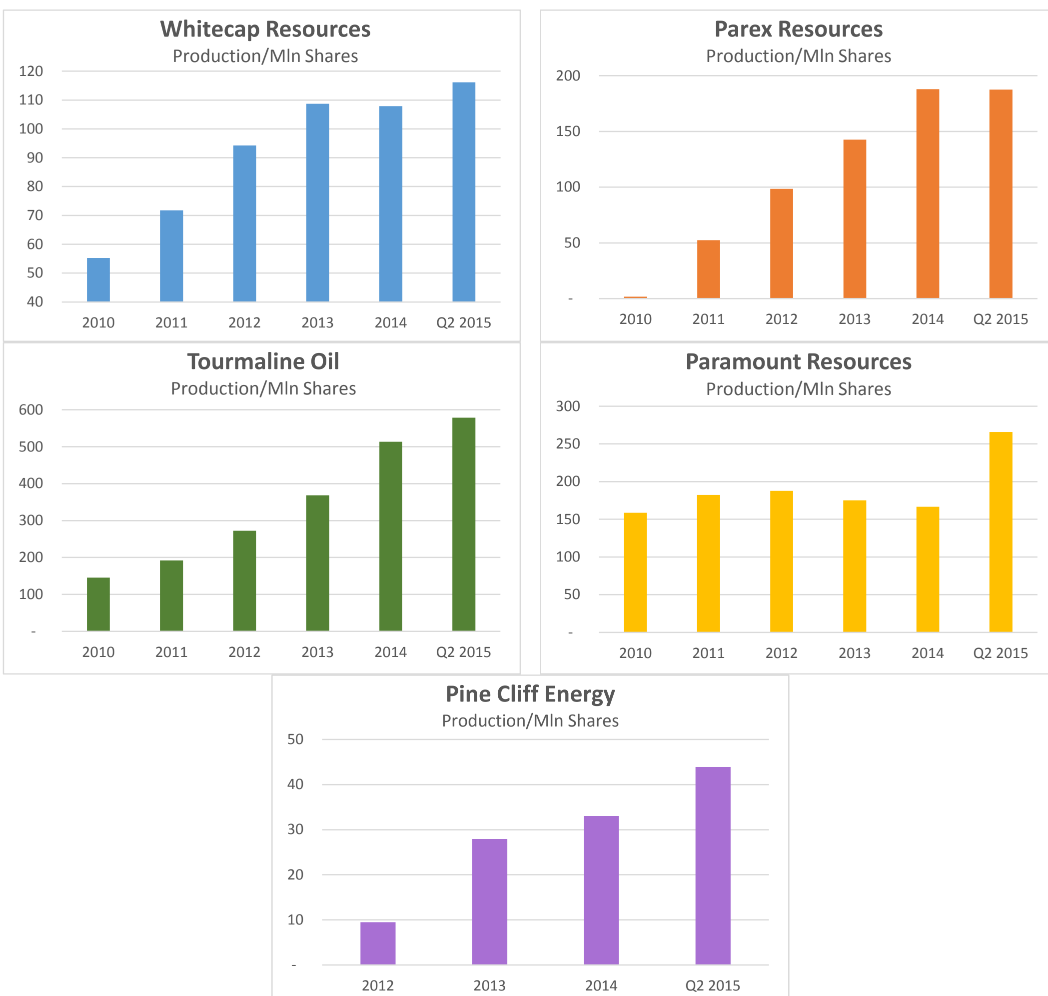
Canada is an ideal place to invest in energy. Aside from its vast resource, Canada has been at the forefront of developing drilling and completion technologies and has thus developed world class operating teams.

We highlight 5 oil & gas companies which have declined more than the energy index. Unjustifiably in our opinion. These companies are the best operators, with balance sheets that can withstand a prolonged down turn in energy prices.

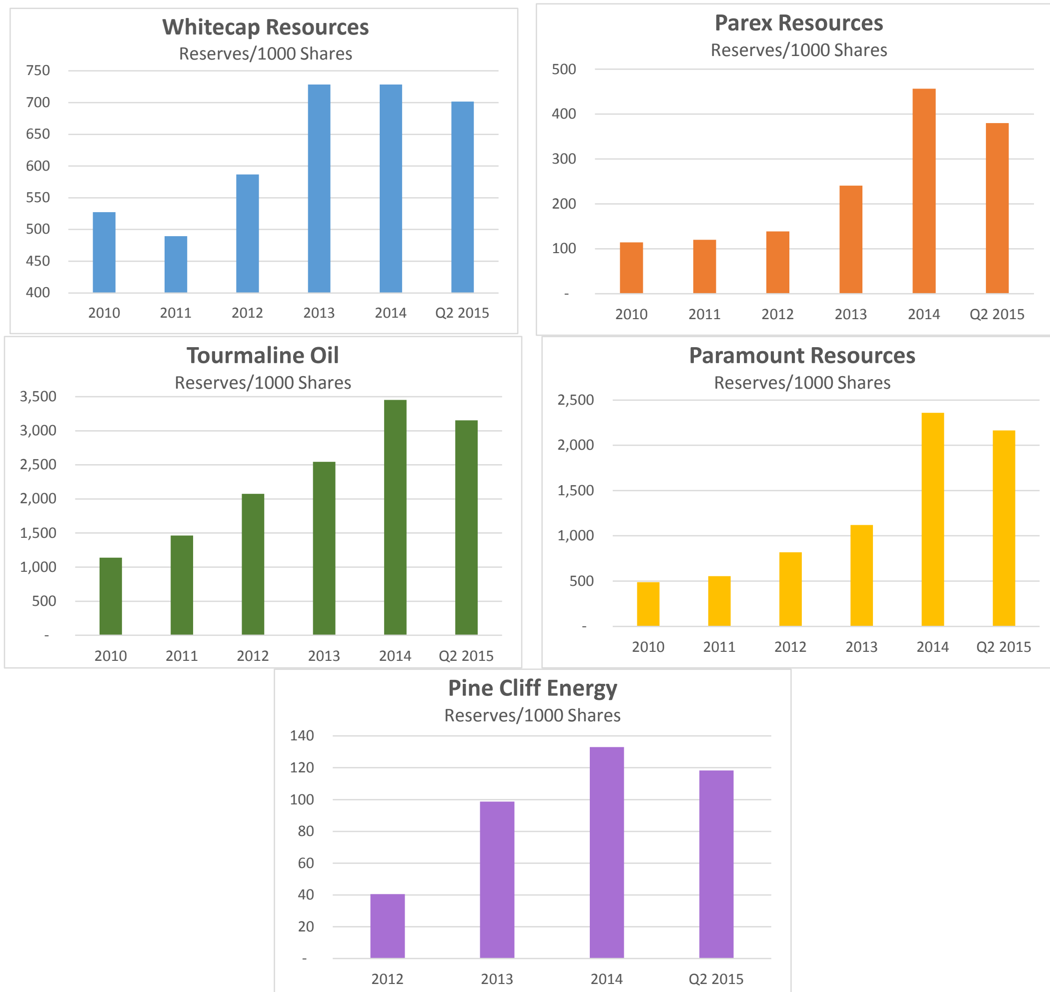


Why have these companies declined so much more than the index? Partially because the index is heavily skewed towards the largest operators, who tend to be viewed as a "safe" place to invest in tough times. However, these large producers have difficulty growing, and have failed to show per share value creation like that of our chosen operators. The management teams of our companies have demonstrated that they can operate efficiently and add shareholder value in a depressed pricing environment by growing production and reserves per share, at a low cost without putting undue pressure on their balance sheets.

Production/Share (Debt-Adjusted)



Reserves/Share (Debt-Adjusted)



The best operators in the business don't need higher prices to be profitable. Their continuous focus on efficient operating and drilling techniques leads to dramatic improvements in well costs and well production. For example, since 2011, the team at Tourmaline Oil have decreased the cost of their Montney wells by 60% to less than $3 million (the best of any operator in Canada), all while increasing initial well production rates by 40%. They've also decreased operating costs by roughly 1/3rd to $4/boe.

We believe that the Canadian energy business presents an opportunity for US investors today. The benefit of a recovery in energy prices should be amplified by a rising Canadian Dollar. In the meantime, we use our extensive network built from our 22 years of experience to seek out the best opportunities in Canadian energy. These are companies run by teams that have demonstrated track records of value creation and operational efficiency, but are being overlooked by the market, and thus poised for an outsized recovery.