DEANS KNIGHT
CAPITAL MANAGEMENT LTD

DK INCOME FUND

Quarterly Report
March 31, 2006

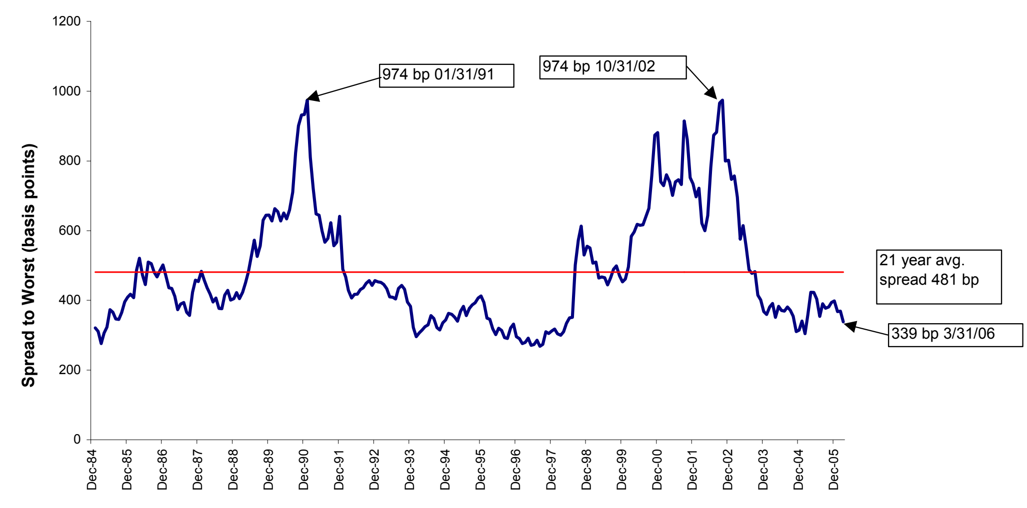
Rates of Return[1]

	3 Mths	1 Yr	2 Yrs	3 Yrs	4 Yrs	5 Yrs	10 Yrs	Since Inception June 30, 1993
DK Income Fund	**7.5%**	**21.0%**	**25.0%**	**25.6%**	**21.4%**	**18.1%**	**11.7%**	**12.2%**
SCM Universe Bond Index	-0.4%	4.9%	4.9%	6.8%	7.4%	7.0%	7.7%	7.9%
ML CDN High Yield (hedged)	2.5%	1.9%	3.3%	8.5%	7.0%	4.6%		
ML USD High Yield (unhedged)	2.9%	7.2%	7.1%	11.9%	9.7%	7.8%	6.7%	7.3%

As of March 31st, the portfolio was invested as follows: 51% corporate bonds, 30% income trusts, 4% common shares/warrants and 15% cash & short term. By contrast, three years ago 90% of the DK Income Fund was invested in corporate bonds. Corporate bonds are not as attractive today. Interest rates are near 50-year lows and corporate bond spreads are too narrow, as shown below.

Credit Spread History

Merrill Lynch High Yield Master Index Less 10 year Treasury Yield



Source: Merrill Lynch high yield

Despite this, there are still some opportunities in corporate bonds. For example, we added to our position in **Jean Coutu Group** 8.5% August 1, 2014 at an average cost of $92.32 for a

[1] Returns longer than one year are annualized.

9.9% yield. Jean Coutu's operations consist of 322 franchised drugstores in Eastern Canada and 1,853 drugstores operating under the Brooks and Eckerd banners in the Eastern United States. The price on Jean Coutu 8.5% subordinated bonds has fallen 10% in the last 7 months as delays in the integration of Eckerd drugstores forced the Company to amend the covenants on its senior secured credit facility. The cost of this amendment will increase the Company's annual interest payment by only $2.7 million to $204 million, which is a modest price to pay for the increased flexibility to improve the performance of the Eckerd drugstores. Jean Coutu generated $515 million in EBITDA in the last twelve months. After capital expenditures and interest paid, the Company is generating significant free cash flow to reduce the $2.48 billion in debt outstanding. Although we are not expecting strong growth in 2006, we feel investors in Jean Coutu 8.5% subordinated bonds are well compensated by the 9.9% yield.

As an alternative to corporate bonds, we have been increasing our investment in income trusts. For example, the largest holding in the portfolio is **Vicwest Income Fund** which increased in price by 34% during the quarter. Vicwest currently pays a distribution of $0.12 per month, or $1.44 per annum, implying an annual distribution of 8.5%. We forecast Vicwest will actually generate distributable cash of roughly $2.30 per unit in 2006. We expect Vicwest to pay out 80% of cash generated and this should provide a distribution yield of 11% for investors in 2006.

We also added to our position in **Avenir Diversified Income Trust** at an average cost of $13.55, implying an annual distribution of 10.6% on an indicated distribution of $0.12 per month, or $1.44 per annum. Avenir has three main divisions: Oil & Gas operations, energy services and financial services. We feel Avenir trades at a valuation discount due to the complexity of combining these three divisions. On April 5th, Avenir announced they would spin out to unitholders a new oilfield services trust comprised of its energy services division. Completing this spinout means the Company will realize a higher value for the energy services division than it contributed as part of Avenir. We forecast Avenir and the new trust combined will generate distributable cash of roughly $2.30 per unit in 2006. Given its current distribution and our estimates of cash flows, we would expect the Company to raise its distribution by 15% in 2006 providing a 12% income return.

We would like to insert a note of caution regarding income trusts. Investors are fleeing low interest rate deposits and buying trust units in order to earn higher income. Unlike interest, distributions from a trust are not guaranteed. During the past three years, there have been 83 new business trusts issued in Canada. Half of these business trusts are trading below issue price today and 11 have either reduced or suspended distributions all together. Ultimately, trust distributions can be no greater than cash flow generated by the underlying business. We believe the specific focus on yield by investors encourages some trust management teams to over-promise, particularly at the time of the initial public offering, which leads to problems. We focus on analyzing the underlying business and how much cash flow is being generated rather than yield. We look for opportunities, like Avenir and Vicwest, where the business is being priced at an attractive valuation based on the Company's ability to generate sustainable cash flows.

As mentioned in earlier reports, we have found the best income opportunities through expanding our focus to include private debt securities. For example, we entered into two private debt financings in the fourth quarter of 2005. On December 21st, we entered into an 18-month Promissory Note with **Anvil Mining Ltd.**, an Australian-based public company with low cost copper production in the Congo. The note paid a 2% commitment fee, an initial coupon of 8% and included 10 warrants as an equity incentive. On March 10th, Anvil Mining raised $150 million through an equity offering using a portion of the proceeds to repay our Note.

The Anvil Note provided an income return of 4.3% over 3 months. In addition, we received 10 warrants per $100 Note to buy shares at $6.25. Anvil Mining's shares closed at $7.40 on March 31st, meaning the 10 warrants add $11.50 of value bringing the 3 month return to 16%. We still hold these warrants and this "equity kicker" may further enhance the return to the portfolio.

The DK Income Fund also extended a fully secured credit facility of up to $4.5 million to **GBS Gold International Inc.** On November 1, 2005 GBS Gold had drawn down $1.5 million with a 6-month maturity. The loan paid an interest rate of 12% per annum over the first two months increasing to 15% on January 1st. In addition to the escalating coupon, the Fund was also entitled to two commitment fee payments totaling 7% of the amount drawn. GBS raised $67.2 million through an equity offering on February 23 with a portion of the proceeds used to repay this outstanding credit facility. Together with early redemption fee's paid in common stock, the Note provided a total return of over 13% in 4 months.

"Equity kickers" received from various debt investments, like Anvil, GBS, Petrobank Energy Services and Lionore Mining have resulted in a 4% portfolio weight in common shares/warrants.

As of March 31st, the 10 largest holdings were:

	% of Portfolio	
Vicwest Income Fund (Income Trust)	10.9%	Building & Construction
Sherritt Intl. Corp. (Bond)	5.9%	Natural Resources
Jean Coutu (Bond)	5.6%	Drugstores
Progress Energy (Income Trust & Bond)	4.7%	Oil & Gas
Paramount Resources (Bond)	4.7%	Oil & Gas
Baytex Energy Ltd. (Bond)	3.9%	Oil & Gas
Imperial Metals (Bond & Bridge Loan)	3.8%	Copper Mining
Royal Group Tech Mtn. (Bond)	3.4%	Plastic Building Materials
Saskatchewan Wheat (Bond)	3.1%	Agricultural Operations
Avenir Diversified Income Trust (Income Trust)	3.1%	Diversified Trust
Total	49.1%	