

ANYWHERE TO HIDE?

The Founders Fund experienced a good uptick of 2.4% in June, not bad considering that markets were generally down in the month (TSX down 1.7%, TSX Small Cap down 1.6%, S&P 500 down 8.6% and the Russell 2000 down 7.8%). This puts the Fund up 11.5% over the first six months of the year, which compares favorably to our benchmarks:

	Since March 2006 Launch (Cumulative)	Year-to-Date Return	12-Month Return
Venator Founders Fund	70.4%	11.5%	11.2%
Russell 2000	-5.5%	-9.9%	-17.3%
S&P Toronto SmallCap	-3.2%	-2.0%	-13.5%
S&P 500	-2.0%	-14.5%	-16.5%
TSX Composite	23.8%	4.6%	4.0%

While we have managed to escape what has been an incredibly tough market for small caps for the better part of three years, it's getting increasingly difficult to work against a backdrop that has become common knowledge: THIS MARKET SUCKS. Steve and I are working harder than ever to uncover the hidden gems in the market than can give us positive performance in difficult markets, with good success. Even our multitude of screens are pulling up fewer intriguing companies, as fundamentals have deteriorated for growth companies, leading us to believe that a renewed shift to value companies could be in the offing as people gravitate to safety over risk. The bottom line is that we see risk everywhere, and we have summarized some of our recent thoughts, below.

OIL: Demand is starting to push back. We are no longer talking about driving less, we are closing SUV and Truck plants (not just lines). We are not just seeing lower flight demand, we are cancelling service to towns. China is refusing to subsidize further hikes in prices which will probably curtail demand for that slowing growth, and still largely poor citizenry. Furthermore, it now appears that if oil prices stay up here, US politicians will have to allow drilling off the coast of America. A few statistics released by several sources (which may or may not be true, but still worth noting): the outer continental shelf is thought to contain a minimum of 18 billion barrels of oil (roughly 10 years of current US oil output). US oil shale and tar sands are believed to have between 800 billion (US government estimate) and 1.8 trillion barrels (Rand Corp. estimate) in Colorado, Utah and Wyoming (equal to 100 years worth of imports). There are another 10 billion barrels in the Arctic Wildlife Reserve. All of these estimates are for recoverable oil (even though some of these projects need \$100 oil to get started, they could subsequently be sustained at oil prices above \$60).

Inflation Rates: The Fed has finally woken up to the fact that oil and food inflation hurts the American consumer more than stagnant wages do (after all, wages aren't about to go up 50% in six months). The problem is that the rest of the world is figuring out this as well, as inflation in Asia is through the roof (over 20% by some measures). In other words, they will have to strengthen their currencies, too. We are not sure how you increase interest rates when no one seems willing to lend at low rates, but the world seems to need to find a way.

Bonds: We are quite concerned that rising inflation could result in rising rates across the globe. If everyone starts raising in tandem, then commodity prices can drop without countries worrying about the relative values of their currencies. Could interest rates go back to 10%? We think it's possible; although we are not yet sure it's probable. This would severely impact the values of securities like bonds and preferred shares. Regardless of the magnitude of the move one thing is clear: the next big move for interest rates is up, which means the next move for bonds is likely down, possibly for stocks as well. Just remember: don't count your coupons before your capital is cashed.

D-Emerging Markets: If you think U.S. markets dropping 13% is bad for headlines, try Shanghai dropping 47% and Bombay Sensex Index dropping 32% over the same time period. Fortunately Latin American strength has resulted in the popular iShares Emerging Market ETF only dropping 11% this year. This is why taking advice on foreign trends from local money managers talking on the television is often not a good idea. Markets down 40%+ and inflation up 20% in Asia doesn't quite jive with the more popular views of these markets, but it's happening.

Cash is Crap: As tempting as it may seem for us to lock in our 10% YTD returns and go all cash for the balance of the year, inflation is killing your purchasing power and we would be doing you a great disservice by “playing it safe”. You need to be invested to keep up, and we need to work hard to find the few stocks that can go up sustainably in such a tough economic environment.

DOES ALL THIS MEAN IT’S TIME TO BUY? Tough to say as I don’t think we are being pessimistic, only realistic. Pessimistic would be calling for a big downturn in corporate profits, whereas we are only looking for a low-to-no growth scenario. Stability isn’t the end of the world, but it’s not enough to get us to “pay-up” to high multiples. This is why we are still out there looking for defensive, inexpensive companies, rather than chasing high-growth/high value or cyclical companies. Our motto at Venator is *Preservation, Appreciation, Performance* and while a 10% gain over six months would normally have us shifting into *Appreciation* mode, we are staying in *Preservation* mode until things settle down, and we can get a better sense of direction in the market (or at least a little less volatility).

THE VENATOR INCOME FUND: A GOOD PLACE TO HIDE?

Markets are tough, and finding a safe place to hide is proving difficult for many (and remember what we said above: Cash is Crap in the current inflation environment). We have therefore decided to open a new Fund designed to provide more predictable returns through investing in higher yield instruments such as income trusts, bonds and preferred shares. This Fund is not designed to provide the superior returns we target in the Founders Fund; rather, it will target 8%-12% returns with safer, and hopefully less volatile underlying investments. The Fund will initially target the Canadian Income Trust market as yields are high and we can still find some non-cyclical companies carrying very low valuations in this sector. Given our above concerns about interest rates and the capital risk inherent in bonds and preferreds, we will not be investing in these instruments at the outset. Since this investment vehicle is designed to provide lower returns, albeit with a safer strategy, fees and terms will be reflective of these criteria. The Income Fund will carry a 1% management fee and a 10% performance fee over a 5% threshold. Investors will be required to invest for a minimum term of six months. If you are interested in knowing more about this investment vehicle please contact JoAnne at 416-934-7994.

A FUND BY ANY OTHER NAME...

On June 16th, the name of the Venator RSP Trust was changed to the Venator Investment Trust. All other aspects of the Trust remain the same – it is still structured as a Fund of Funds that currently invests 100% in the Venator Founders Fund, and it is still available on FundServ on code VCM100/101. The Investment Trust can accept both RSP and non-RSP money – and we believe the new name makes it clearer to all that it is not exclusively an RSP-only vehicle.

Yours Truly



Brandon Osten
President, Venator Capital Management

This is intended for informational purposes and should not be construed as a solicitation for investment in any of Venator’s Funds. The Funds may only be purchased by Accredited investors with a medium-to-high risk tolerance who are seeking long-term capital gains. Read the Offering Memorandum in full before making any investment decisions. Prospective investors should inform themselves as to the legal requirements for the purchase of shares. It is important to note that past performance should not be taken as an indicator of future performance.