VENATOR
CAPITAL MANAGEMENT LTD.

MIND IF I TAKE A MULLIGAN???

This was as tough a month for Venator as for anyone. As the chart below indicates, our Hedge Fund fell approximately 15%. On the other hand, our Income Fund (which doesn't hedge) actually managed to post a small gain!

Instrument	Monthly Return	Year-to-Date Return
Venator Founders Fund[1]	**-14.8%**	**-12.3%**
Venator Income Fund[2]	**0.7%**	**-6.2%**
TSX Composite	-16.8%	-29.4%
Russell 2000	-20.4%	-29.8%
S&P Toronto Small Cap	-24.0%	-45.0%
S&P 500	-16.8%	-34.0%

1. *The performance of the Venator Investment Trust approximates the performance of the Venator Founders Fund.*
2. *As the Venator Income Fund was launched in August, 2008, YTD represents three months of performance. Benchmark results for the S&P/TSX Income Trust: Monthly Return -14.1%, YTD -24.5% (since inception of the Venator Income Fund).*

Venator Founders Fund: With North American stock markets facing their worst month in decades, our hedges failed to adequately protect us from the severe drop in markets and, more specifically, from the severe drop in some of our less liquid small-caps, which suffered from collapsing markets, a lack of buying interest in small caps, and the forced selling by other funds experiencing redemptions in this difficult environment. Surprisingly, our Hedge Fund managed to stay slightly ahead of the markets, which is somewhat uncharacteristic of our performance in months where markets have early collapses followed by late, sharp rebounds. For those of you who are new to our Funds, we historically tend to experience a "lag effect" in sharply rebounding markets, as our small cap stocks don't rebound so quickly (they don't tend to get a lot of buying interest as a lack of liquidity make them a poor vehicle for traders to get back in the market quickly). Conversely, our more liquid, mid-cap shorts tend to move up in-line, or more sharply than the markets. To illustrate the point, when markets were down about 30%, the Founders Fund was down less than 20%; however during the late 10% market bounce in the final week of October, the Founders Fund only managed to pick up about 5% of performance.

Venator Income Fund: The Income Fund, which finished with a small gain despite being 100% invested, managed to stay comfortably ahead of the market collapse throughout the month. We took the opportunities provided by the market bottom to initiate some new positions which caused us to lever up by 15%, but have subsequently reduced the fund to 100% invested. The Fund currently has a yield of approximately 11%.

We figured, given the difficult month, it would be illustrative to provide a longer, more comprehensive, overview of how we are dealing with these markets, and our views and strategy going forward.

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What We Like (assuming low valuations):

Doing something special: We like companies with very specific plans to increase earnings during the next twelve months. Hammond Power Solutions represent just such an opportunity, where the falling Canadian dollar is set to increase US sales by 25% (so if same-currency sales go down 10%, reported growth will still be 10%) and lower copper prices will also serve to reduce costs while they keep expenses on a tight rein. Furthermore, by moving more standard product manufacturing to Mexico, the Company is set to increase margins further. Finally, new distribution relationships with major buying groups will bring in sales from new channels they previously didn't have. In short, if industry sales dropped 10% in Canada and the US, Hammond could still pull off modest revenue growth and better than 10% earnings growth. We can't say that this will happen, but the pieces are in place to give this scenario a decent probability.

Gaining Market Share: We recently got back into Research in Motion and Apple. Big caps aren't normally our thing, but these companies were both recently trading at under 10x our earnings expectations and we couldn't resist the no-growth scenarios the market appeared to be discounting. These companies both have very small market share (under 10% combined) of the global cell phone market. If smartphones can increase their market share of the overall cellphone market (and Apple can continue to build its market share in PCs) then these two companies can grow, even in a cellphone sales environment that shrinks by 5% and a PC market that goes flat. The main caveat is these companies sell some relatively expensive products, with the offset being that these are products that people *really* want.

Canadian/US dollar trade: This is an important trade that really hasn't received the air time it deserves. The Canadian dollar is down over 25% from its highs. While this is a boon for Canadian exporters, we are sufficiently worried about the economy and uncertain of how much the currency effect will be able to offset economic weakness. But considering that Canadian companies which primarily manufacture and sell to the United States (or deal in US dollars) will get a straight 20% gain on their earnings in Canadian dollar terms, we believe there are some great opportunities. As previously mentioned, this includes Hammond Power, and we have re-purchased Neo Materials which reports in US dollars but only trades in CDN. We note that investors in Research in Motion hit the stock when the company announced that it would see gross margins drop by 5%, but hoped to recover 2% through economies of scale for a net loss of 3% on operating margins. What the Street has failed to recognize is that a significant portion of personnel expenses are in Canadian dollars which can go a long way to recouping the other 3% of potentially lost margin.

Defensive and Cheap: Cheap isn't good enough. There are a lot of cheap companies, and you can find cheap companies in any market environment. Many of them are cyclical or turnarounds, both of which you don't want to bet on in a recessionary environment; however, really cheap AND economically defensive is a good mix. Companies like Pet Valu (Ontario's leading pet supply retailer, which sells mainly pet food rather than other more discretionary items) and Futuremed, the leader in selling disposable medical supplies to nursing homes in Ontario and Quebec, exemplify defensiveness. Pet

Value trades at 7x earnings while Futuremed trades at 8x taxed-equivalent earnings expectations and pays a better than 10% dividend - cheap and defensive.

Dividends/Yield: As the relative outperformance of our Income Fund is demonstrating, the market seems to agree that high dividends are a good place to be, and better than higher yielding debt. If you can stay cheap and defensive, such as the aforementioned Futuremed, you can make 10% even in a flat market environment.

What We Don't Like:

The Commodity Cycle (cycles don't last three months): Is this just a violent price correction in a long-term secular bull market for commodities, or is this a cyclical downturn? Rising supply capacity over the past several years and lower demand suggests the latter. Natural Gas production is going to go a lot higher for the next four years; oil production cuts mean more spare capacity (bearish until demand growth reinvigorates and catches up), and copper demand likely weakens with the economy while $1.50 copper is fine with the major producers in terms of expansion plans. Fertilizer prices are weakening in North America and North American producers are always one contract negotiation away from a 50% price cut from China. Coal and Molybdenum prices, to name two more recent fads, are just starting to roll over now. Zinc and nickel have possibly bottomed as they started their plummet last year, but in general investors should look for a tough year in commodities. Commodity cycles don't last three months, so don't count on a quick sustained bounce.

Gold (ignore conspiracy theorist Gold Bugs): We have said this before, but we believe that gold is not likely to zig when the market zags. With commodity prices collapsing, we no longer need a hedge against inflation. Gold bug conspiracy theorists have maintained that central banks have managed to keep currencies strong by holding gold down through reserve sales. Times have changed. Governments need money to deal with financial crises and gold bugs should be thankful that central governments aren't dumping reserves in order to raise funds! Do people really think that the roughly $250BB that the US holds in gold reserves is in any way strategic at this point? I am guessing that if the US government could sell it without killing the price, and redirect the proceeds towards the financial bailout, they would do it in a second.

The coming REIT disaster: If your broker still has you invested in Real Estate Investment Trusts in order to generate income we would advise you to shift into industrial income trusts. REITs are in a horrible position as virtually all of them have huge debt refinancing risk (whether it's sooner or later doesn't matter, it is inevitable). In many cases, a mere 2% increase in interest rates on their mountains of debt could wipe out 40% of their cash flow. But it gets worse. Unlike income trusts, REITs have no avenue through which to pay down debt other than share issues. This is because REITs must distribute nearly all of their operating cash flow in order to maintain their tax-advantaged status. Therefore, all else being equal, a REIT that cuts its distribution from $1.00 to $0.50 in order to prudently pay down debt before it matures will only be able to use $0.15 to pay down the debt, while the other $0.35 goes to government in the form of tax. You are better off with less leveraged Income Trusts that will likely start paying down what debt they have in two years when the Trust structure disappears.

High Debt Growth: We are on the lookout for low growth companies that managed to look like growth companies due to easy access to capital. REITs obviously qualify, but so do lesser names like Iron Mountain. Iron Mountain (which we are short) has piled on a lot of debt recently because its capital intensive growth results in little free cash flow. Yet this 10% organic growth, highly levered, low cash flow business continues to maintain a P/E in excess of 20x earnings. These are the kinds of companies that are getting into trouble as the market recognizes their inability to grow or generate cash if more debt does not become available to them.

The Euro vs. the Greenback: We continue to believe that Europe is in the early stages of dealing with what the US is the later stages of dealing with in terms of the financial crises. It is amazing that Europe has held its interest rates in the 4% range while its economies flounder and inflation concerns dissipate with commodity prices. Couple this with stronger demand for the more stable US dollar (so much international debt is denominated in US dollars, but the US is in the enviable situation of having its own debt denominated in its own currency) and we think the Euro should move closer to parity over the next six months. This is going to hurt a lot of exporting companies, including those servicing the international infrastructure markets and big cap tech. Certain consumer products plays will also run into issues if they get too much of their revenues from overseas.

What We Are Doing Now:

We believe that the recent market collapse has created some great buying opportunities for larger, more liquid, big cap companies. As a result, we are seeing better opportunities in this area than we are seeing in our bread-and-butter small cap universe. All else being equal from a valuation standpoint (i.e. P/E, PEG, cash flow ratios etc.), we would rather buy a larger company over a smaller company, and a more liquid over less liquid stock. In other words, we would rather buy Research in Motion at 10x our internal earnings estimate (which is where it was at US$40.00), than RuggedCom (a great little Canadian company, but a very illiquid stock) at that same multiple. As a result, we have been shifting our assets into some of these more liquid opportunities as we fear that Fund closures, tax loss selling, and general market caution could keep these small caps under pressure for the next little while. To be clear, we do not forecast a long-term change in our small-cap mandate, and when RIMM gets back through 17x earnings (or $70.00) we will be shifting back to our beloved small caps, as they will likely be selling for good relative value at that time.

Unfortunately, volatility continues to be more our enemy than our friend. For one thing, protracted and large market drops eventually wear our small caps down, as panicked investors inevitably hit the thin bids for these stocks, while short sharp upturns leave our small caps behind temporarily. Furthermore, we try to avoid shorting companies where we can lose a lot of money in too short a period of time. This is largely why we did not capitalize on our prescient bearish calls on oil and fertilizer stocks that we had made earlier in the year. Shorting oil at $90.00 and Potash Corp. at $140.00 would have been extremely painful as these investments would have gone 50% against us before working out. Furthermore, as our exposure increased we likely would have reduced our short positions on the way up, and may have only ended up breaking even on these calls. Sometimes, we will need to be satisfied with our avoidance of popular mainstream investment themes that collapse, even when we are disappointed that we didn't profit on our prescient contrarian calls directly.

At the end of the day, it's better to be too early than too late. There is a lot of money sitting in cash investment funds that are down well over 20% YTD. These Funds cannot afford to fall further behind the market in the event of a rebound (if you think it's hard to tell investors you are down 40% when the market is down 30%, try telling them you are down 35% when the market is only down 15% two months later) and will deploy cash quickly if they feel the bottom is behind them. In the event of a rebound, we will probably shift back to a more defensive posture, but right now we stand at 100% long and 20% short (the low end of our historical 20%-40% short range). However, volatility, deleveraging, and redemptions remain the big "X" factors in the market. While we believe that the deleveraging of equity investments is more or less complete, the redemption cycle is likely to continue which could lead to continued volatility. At the end of October the market was 15% off its bottom. This means that a further 5% move in November puts us, technically speaking, in a new BULL market. Yes it sounds crazy, but if the market jumps a mere 5% over the next 50 weeks (ending November 1, 2009), the media will be talking about the market being up 20% over the past 52 weeks (mid-October 2008 to mid-October 2009), 15% of which happened in the first two weeks. If there is anything we did correctly, it was sticking to our guns at the bottom, and not making a bad situation worse.

Thank you for your continued support,

Brandon Osten, CFA
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. All stated Venator returns are net of fees. It is important to note that past performance should not be taken as an indicator of future performance.