VENATOR
CAPITAL MANAGEMENT LTD.

LOW RATES AND HIGH INFLATION? THE WORST OF BOTH WORLDS!

In April, the Venator family of Funds had a good month, with the Income Fund and Catalyst Fund posting gains, while the Founders Fund was flat. Our actual results are posted below.

Instrument	April's Return	Year-to-Date
Venator Founders Fund[1]	**0.0%**	**3.2%**
Venator Income Fund[2]	**1.5%**	**9.0%**
Venator Catalyst Fund	**2.0%**	**2.9%**
TSX Composite	-1.0%	4.5%
Russell 2000	2.6%	10.8%
S&P Toronto Small Cap	-0.6%	3.6%
S&P 500	3.0%	9.1%

1. *The performance of the Venator Investment Trust approximates the performance of the Venator Founders Fund. Return is for Class "A" units.*
2. *YTD of Fund is for Class "F" units net of distributions reinvested.*

This is the last of our mini-series on inflation and how to (try to) beat it (actually we have been talking about stealth inflation for over three years now). Over the last several weeks there has been a marked increase in press surrounding the guess as to the real rate of inflation. Unfortunately, as we are all aware, the official statistics are most definitely not to be trusted. Goods are, by our estimate, increasing at an average annual rate of around seven percent. In other words, most of the goods we use have nearly doubled in price over the last 10 years (food, clothing, houses, energy, etc). If you don't believe this you are either a government official, or not paying close enough attention. Thus far some items have been kept at bay due to increasing imports from China (think about toys or textiles at Walmart), but with China now increasing their interest rates, at what can only be defined as an alarming pace, I think the far east will prove itself to be a major contributor to inflation going forward. In other words, we are running out of places to shift imports from in order to keep inflation at bay.

Once you, the investor trying to protect the purchasing power of your money (because investment gains don't count if inflation outpaces your returns), have admitted that there is a problem and reset your return demands, you need to evaluate your options. This is not 1982, when inflation was high but so were interest rates. These time-safe investment instruments won't get you anywhere where you need to be in order to keep up. Heck, most newly issued junk bonds nowadays come out with less than seven percent yields!

Stocks look great off the bottom, but 10-year returns are not keeping up with this rate of inflation. Wages (outside of financial services) are most definitely not keeping up with inflation. The current political interest in keeping rates low to increase affordability of big ticket items is an interesting plus to the economy, but not one that will overcome some very serious minuses:

- Money printing will continue to devalue currencies and spur continued inflation;
- Low rates result in low investment returns for safer instruments designed to keep up with inflation; and,
- Eventually rates will have to come up, which may destroy the illusory returns of equities achieved through multiple expansion and inflationary pricing, leaving investors with continued inflation and poor investment results once the smoke clears.

The federal reserve, and its international equivalents, are supposed to adjust rates to keep inflation subdued. Instead, they are lying to themselves about inflation in order to keep rates low for political reasons. Put another way, they have lost sight of their original purpose. With the economy having come back from the brink it's time to let go of the stimuli before you lose control of the situation and the market does it for you (in the form of higher rate debt issuance due to investment demand for absolute returns, rather than relative ones).

This brings us shamelessly back to our Income Fund. It currently carries an underlying yield of around nine percent and is comprised largely of shorter term bonds so that we can sidestep the negative effects of the inevitable rise in 10-year-plus rates. It's not that we see a market crash on the horizon, or any such calamitous 2008-like event occurring in the near future. But you always need some safer investments to protect the purchasing power of the majority of your investable assets. As long as the government can pretend inflation is low, and peg rates to these fanatasyland assumptions, T-bills, government savings bonds and GICs just won't cut it anymore.

Yours Truly,

Brandon Osten, CFA
President, Venator Capital Management Ltd.

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 seeking long-term capital gains. Read the Offering Memoranda 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.