TWO STEPS FORWARD, TWO STEPS BACK

July was yet another tough month for small caps, with the Russell falling just over 3% (although the TSX was up 2%, but alas we have little exposure to resource and financial services stocks). We managed a small gain of 2.4%, as the powers that be determined that we had taken enough pain in June (painful reminder: down 9%) and afforded us a reprieve. Earnings season thus far has provided us with reason for enthusiasm as all but three of our sixteen reporting companies have reported good-to-great results, but the short-term gains from these earnings reports seem to continually disappear as the continued weakness in the overall market drags them back down to pre-release levels in the ensuing days. Since inception, the fund is down 2.6% which is below our main benchmark of 0%, but better than all of the other benchmarks we look at with the exception of the TSX (see above parenthesis). We will have more to say about our relative performance in our six month review next month.

With regards to our market commentary, I think we can bluntly say that things are tough out there, and are likely to remain so. We have plenty of reason to be bearish, but the private equity guys are giving us plenty of reasons to be cautious with regards to our short exposure. We are of the belief that interest rates (which have gone up), are affecting housing prices (which have gone down), which will in turn affect consumer spending (which we are short); oil, gas and gasoline prices aren't helping either. As such we favor corporate spending as a sector (corporations have tons of cash, or have been smart enough to take advantage of cheap debt over the past several years). As a result of this plan in action, shorting has been easy (we have had only 3 out of 10 shorts go the wrong way on us post-earning/guidance). Unlike with our long positions, the shorts that have gone down have stayed down. We are currently only 25% short as a result of covering those that have gotten to our targets, but are looking to increase this exposure.

The month of August has continued to be rough for small caps. Our companies continue to post good-to-great earnings, allowing us to hold our own. That being said we can't help but feel that our portfolio could be doing much better in a market more receptive to small caps. We are very bullish on our portfolio of names, and firmly believe that it is only a matter of time before their solid progress gets recognized by the Street at large. As of this writing, the fund is 96% long (51% Canada, 44% US), and 24% short. We are finding some exceptional small cap opportunities here at home, as the local small cap money has been so focused on junior resources, it has resulted in some serious neglect in the industrial sector.

Next month marks the six month anniversary of the Venator Founders Fund, and we plan to have a comprehensive review of our outlook and strategy going forward.

Thank-you for your continued support,

Brandon Osten, CFA
President, Venator Capital Management Ltd.