VENATOR
CAPITAL MANAGEMENT LTD.

HIDDEN IN PLAIN SIGHT

The market had yet another good month, and Venators' Funds managed to achieve some good gains as well. All three Funds managed to finish in record territory and are off to pretty good starts for the first quarter of the year. At the same time, our Funds remain fairly cautiously positioned with healthy short (Founders), bond (Income) and cash (Catalyst) allocations depending on the Fund. It just seems a bit too easy to make money right now, meaning that the level of skepticism feels like it's at a recent historical low. Yes, the market has its share of vocal minority skeptics, but the overall mood is one of cyclical recovery, and that nothing can stop things from improving, valuations be damned!

Instrument	March's Return	Year-to-Date
Venator Founders Fund[1]	**3.9%**	**11.5%**
Venator Income Fund[2]	**3.6%**	**5.9%**
Venator Catalyst Fund[3]	**1.4%**	**5.7%**
TSX Composite	3.8%	3.1%
Russell 2000	8.1%	8.9%
S&P Toronto Small Cap	3.5%	4.9%
S&P 500	6.0%	5.4%

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.*
3. *The Venator Catalyst Fund has no benchmarks.*

March represents the anniversary of the huge twelve month market rally (up 50% to 100%+ depending on what index you are watching) after the disastrous six month 50% fall. It also represents the twelve month anniversary of our *It's Not Different This Time* March 2009 review, where our main points were that: P/Es would get back above 10, that debt would be a viable source of financing, that stocks would again trade above book value, and that commodity prices would succumb to the forces of supply and demand (3 out of four ain't bad). The point of the article was to illustrate that there was a lot of low hanging fruit that could allow us to find 20%+ gains without taking on much risk. However, we admittedly didn't see the massive cyclical rally that would unfold, and we are still not sure we will from a business standpoint, despite what the stock market is telling us.

That being said, the massive fall, followed by the massive rally, coupled with our stable/low growth expectations has again left us again with some low hanging fruit comprised of companies whose businesses actually improved over the bad two years, yet whose multiple expansion has severely lagged the rally, leaving these companies at a discount to the market despite their exceptional three year performances. While we don't usually talk about our stocks by name, we thought it would be illustrative to throw a few out there to demonstrate what we are talking about:

- **IBM:** While supposedly no longer a growth company, Big Blue has doubled its earnings per share in the past four years. Yet at 12x GAAP earnings, IBM trades at its largest multiple discount to the S&P500 in decades. While its stock trades at 12x earnings, its ten-year bonds yield around 5% (suggesting the stock should trade at 20x

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earnings if you believe that earnings per share won't shrink over the next ten years). Whether you view IBM as a stealth growth story, or a cyclical technology story, we believe IBM deserves to trade higher. Looking at IBM's contemporaries: pure play technology consultancies trade at 16x earnings, software companies trade higher. Their customers – the S&P500 – trades at 16x earnings. Do we think IBM will outperform the market by 25% in the near term? Yes we do! IBM – sometimes it's just that simple.

- **Destination Maternity:** One of our largest holdings, DEST is the largest retailer of maternity wear in the United States (90%+ market share of standalone stores, 50%+ market share of all maternity wear sold). While the rest of the retail sector trades well in excess of 13x earnings, DEST trades at a lowly 8x current year earnings. While not as cyclical as some more discretionary retailers, this isn't a very competitive market either. It's not as though this is hidden either, as the Company (currently trading at $25.00) has guided to non-GAAP earnings of approximately $3.00 per share. The Company has never earned that much before, but its stock as seen the high-$30s on two previous occasions. Hidden in plain sight.
- **Skechers:** We Canadians might not be aware of this, but the hot new thing in shoes is the "toning" category. These shoes supposedly "tone your butt" while you walk. When shoe retailers in the US talk about a resurgence in shoe demand, essentially one-half of the growth is coming from this nascent category. Two companies have grabbed the whole toning market: Skechers (Shape-Ups) and Reebok (EasyTones). Unfortunately, Reebok didn't see the demand coming from this market and under-produced their "Easytones". Our conversations with leading retailers have suggested that Skechers, which has ramped up production, may enjoy as much as 75% of this market this year. Skechers has made a nice run from the market lows moving from $6.00 to $36.00 (obviously we didn't own enough of this one!), but at 12x earnings, Skechers trades at a severe discount to the footwear industry as a whole, even though they are the company that is driving the industry. Another growth company trading at a discount to the S&P500.

All three of these companies are large companies and market leaders in easy to understand businesses, illustrating that you don't need to search for obscure names and micro-cap start-ups. You don't need to look for "hidden assets" or turnarounds when good value is staring you right in the face. A severe market crash followed by a huge rebound is inevitably going to leave a significant number of companies behind. To the extent that we still hedge a large proportion of our portfolio, we only need outperformance of our names to create some solid returns.

Yours Truly,

Brandon Osten

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.