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Dear Partners and Friends:

January of 2009 was the worst January for U.S. stocks since the 1930s. The S&P/TSX Composite Index (the “TSX”), although one of the better performing indices in the world in January, was still down 3.3%. As I write this letter, the major North American indices are down year-to-date anywhere from -6.9% (for the NASDAQ Composite Index) to -13.9% (for the Dow Jones Industrial Index), with the TSX down 9.0% year-to-date as of the close yesterday.

In that context, it felt good to see some stability in the returns of the Innovation mandate for the first time in a while. The Northern Rivers Innovation Fund LP (the “Innovation Fund”) was up 1.23% on the month and the Northern Rivers Innovation RSP Fund (the “RSP Fund”) was down 1.51%. It was actually frustrating, however, that the January returns weren’t higher: unexpected hits from two of our private oil and gas holdings took back some of the gains seen in the core, public holdings.¹

	Average Annual Returns to January 31, 2009*							
	2009 YTD	1 mo.	3 mo.	6 mo.	1 Yr.	3 Yr.	5 Yr.	Inception**
Northern Rivers Innovation Fund LP	1.23%	1.23%	-20.27%	-58.28%	-60.35%	-14.67%	-3.25%	9.03%
Northern Rivers Innovation RSP Fund	-1.51%	-1.51%	-21.16%	-58.19%	-60.71%	-14.52%	N/A	-5.88%

**Northern Rivers Innovation Fund LP inception date: May 8, 2001.
 Northern Rivers Innovation RSP Fund inception date: March 1, 2004.

So 2009 is off to a rough start in the investing world, and the economic news has continued to worsen. As discussed in prior letters, however, this was to be expected: the 40% or greater declines in global equity indices seen in the September to November 2008 time frame had *already* told us that the economic news will continue to get worse *at least* until May of 2009 and probably through until August. (This statement is predicated on the fact the equity markets historically discount developments six to nine months out.) This is a critical point: *if* the U.S. and global economies are able to bottom out by August of 2009, *then* there is a good chance that the overall markets will put in an ultimate bottom within plus or minus 5% of the November 20-21, 2008 lows. On the other hand, *if* we continue to see sequential (quarter over quarter) declines in the major economies through the end of 2009 or longer, *then* we will almost surely see new lows in the equity markets too.

Importantly, nothing that has happened so far this year invalidates my base case for the 2009 North American equity markets seeing returns in the -10% to +10-% range for the year as a whole. Fortunately, it appears that fiscal and monetary authorities around the world have woken up to the

¹ It is worth pointing out that our exposure to resource stocks is very low currently, at less than 10% of the portfolio.

seriousness of the issues before us, and most have started to demonstrate both the willingness and ability to implement the necessary measures. We have a check-list of items that will give us more confidence that the necessary actions are being taken, including the ECB finally moving their target rate closer to the rates of other Western central banks. With respect to the equity markets in general, we are clearly in a scary re-testing phase now, during which we will almost surely see the November 2008 lows re-tested multiple times. For those with a long time horizon, financial ability and emotional fortitude, however, this still appears to me to be one of the best opportunities to invest in equities that has presented itself in decades.

Some notes on the private companies in the portfolio

In this and each of the last several letters, I have made reference to write-downs and write-offs taken in the portion of the portfolio that is comprised of private companies. It is definitely a larger portion of the portfolio than I am happy with. This state of affairs came about largely because of the enormous declines seen in the value of the publicly-traded holdings in 2008. Indeed, it was the wholesale downward adjustment in valuations applied to ALL companies (public and private) during the crash of 2008 that was the driver for most of the write-downs we took on our private holdings in the October-December timeframe.

Importantly, as I have gone through the painstaking process of doing thorough revaluations of each company since October 31st, I have actually come away with some pleasant surprises, and the feeling that the private part of the portfolio has the potential to be a source of some good returns over the next two years. For starters, I was shocked (in a good way) to learn that eight of the private companies in the Innovation mandate had managed to raise money in the September to December time frame. This is truly a remarkable feat—I can't remember a single financing that was done for a public company during that timeframe (other than the desperation financings done in the U.S. financial sector). The October to early December period in Canada was particularly barren, so I think the fact that eight of our *private* companies were able to raise money during that period of extreme duress is a testament to the quality of those companies, and their future prospects.

A partial list of the companies—and positive things going on—in the private portion of our portfolio seems appropriate here:

- 1) Trilliant is a company in the “smart metering” space that is a centerpiece of Obama’s “smart grid” portion of the fiscal stimulus package. This is no start-up: Trilliant did about \$100 million revenue in 2008, and management is targeting over \$130 million in profitable revenue for 2009. If any company can go public in 2009, it is Trilliant.
- 2) eAsic is a company that I wrote about in the October 2008 letter. Their technology remains the most disruptive technology that I have ever come across in my career, with a semiconductor platform technology that consumes 1/10th the power for 1/10th the cost of its most comparable commercial technology. They continue to be well-supported by their two globally-renowned VCs, Khosla Ventures and Kleiner Perkins Caufield.
- 3) A company in the video-surveillance-analysis sector has recently landed a number of key global reference accounts (including Munich Airport), and has a very credible path to profitability this year. Their enormous gross margins means that a large portion of incremental revenue this year will go straight to the bottom line.

- 4) A company in the warehouse “pick systems” space just landed two of the largest operators of warehouses in the world (including a Warren Buffett company with \$25 billion in revenue that is the world’s largest distributor of products to convenience stores) as customers. Given that these are the two largest customers in the “pick systems” space, these wins have turned this industry on its ear, and give this company a five year potential revenue pipeline of \$100 million from these two companies alone.
- 5) An innovative consumer products company (that already has distribution in major chains like Wal-Mart, Home Depot and Autozone) has just made a company-changing acquisition of a company that has about \$15 million in profitable revenue from selling a widely distributed line of biodegradable plastic bags. This company will shortly be closing on a US\$8 million financing from a U.S. based private equity boutique.
- 6) The only biotechnology company currently in the portfolio also happens to be a private company. In the context of a biotech environment which has seen a record number of bankruptcies over the past eighteen months, this company has been astoundingly successful, raising money as recently as January of 2009 at the same value at which we last put money in. With very promising research going on at the M.D. Anderson Cancer Centre (arguably one of the top three cancer research centers in the U.S.), and an article in a top, peer-reviewed journal about to be published, the valuation for this private company looks to go higher this year.
- 7) A company we were considering writing to zero only last summer has had a dramatic change of fortune. A global distribution partnership with a global leader in network and computer security has already led to contracts that will make this company profitable by the end of March. I believe their partner will acquire them within six months, as this space has seen a number of acquisitions (large and small) even during the recent wipeout, and the global distribution deal is exceeding both participants’ expectations so far.

These seven companies represent about 20% of the Innovation Fund, and I am very excited about what they can do for the fund and its investors over the next two years. There are other private companies with global partners and growing revenues in the portfolio, but I will save some for mention in future letters.

Speaking of future letters, my plan is to go through in detail the investment case for each of the publicly traded core positions, one per month, over the coming months, with Neptune being the likely subject next month. Having said that, I would like to provide a brief note on two of them here.

Webtech Wireless

On January 21, 2009 (overshadowed by the market mess that was unfolding in and around Obama’s inauguration) AT&T announced a significant relationship with Webtech Wireless, as well as a first customer win for the AT&T/Webtech offering. A potential relationship with a U.S. wireless carrier had been discussed on past company conference calls, but the actual deal that was announced was far better than I was expecting, and is probably the most significant business development for Webtech since they won the Fedex deal.

I was expecting a white-label deal, very similar to the Rogers “mfleet” deal (where Rogers does not allow Webtech to be identified in any way). As it turns out, this AT&T deal is BETTER than

a white-label deal, because AT&T will be marketing the system as “Webtech Wireless from AT&T” i.e., Webtech gets to use their own name and logo in the software and hardware AND sales and marketing materials (which is different than the “white label” deal with Rogers), so AT&T will be promoting and advertising the Webtech name across the U.S. (and U.S. territories). The most important element of the Rogers white-label deal, however, is intact: the AT&T sales force will be carrying quotas on Webtech systems.

I offer the following as a comparison between what AT&T might be able to do for Webtech, versus what Rogers “mfleet” offering has done for Webtech since it was launched over a year ago. The Rogers deal is generating \$250,000 to \$1,000,000 per quarter in sales for Webtech. AT&T is about ten times the size of Rogers in terms of their wireless operations, so one might extrapolate to expect \$2.5 million to \$10 million per quarter in sales from the AT&T channel (once the sales force is fully trained six months from now). I’m going to set my own expectations in the \$1 million to \$4 million per quarter range.

Last but not least: a wonderful aspect to this relationship is that the announcement makes it clear that WEW/AT&T stands to be a beneficiary of the massive Obama-led infrastructure spend over the next three years. Who would have thought? Webtech is an infrastructure play.

The only “sad” thing about the press releases is that they weren’t out until 10 a.m. on the day they were released (Wednesday, January 21), so not a lot of people saw them. (Speaking with various people I know that own WEW in the weeks following, I discovered that few had seen the release.)

As good as this news is, I don’t expect the stock to be able to really get going until they announce a move by GNP (the Carlos Slim-controlled Mexican insurance company) to fully roll-out, or an assembly line deal with a Brazilian auto manufacturer (this time with the relationship being *directly* with the auto manufacturer), or a large government deal. Either way, I believe this is a company that will continue to grow strongly, even in the face of the most severe recession since the Great Depression.

Vendtek Systems

I wrote about this company in detail in the November 2008 letter, and would encourage interested readers to take another look at that letter. I continue to be very pleased with the way the business is developing, including their relationship with Privinvest, a business partner of Vendtek’s that now owns almost 20% of the company. Unfortunately, a press release on February 11, 2009 informed investors that Vendtek will be delaying the release of their fiscal year 2008 results—essentially to allow the company to address inventory accounting errors made in the fiscal year ended October 31, 2007. I want our investors to know that I am monitoring the situation very closely, but most of all I want you to know that, *fundamentally*, any accounting mistakes made have NO bearing on the past, present or future free *cashflow generating ability* of Vendtek, and hence NO bearing whatsoever on the intrinsic value of this company. Of course, in a market like we are in, the stock is bound to take a hit—a hit that will feel like a particularly unfair punch in the stomach in these trying times. Nonetheless, I believe that Vendtek will prove before long why such a hit is unjustified. Importantly, Privinvest maintains their support of the company, remains a believer in the business model and continues to work on growing Vendtek’s business outside of North America.

In closing

So how does one balance the strength of the fundamental developments within these companies (public and private) against the headwinds of a severe recession and horrible financial markets (and in Vendtek's case, an accounting error)?

To answer this, I will quote from the last letter: "On a one year basis, I believe that the core positions have very likely put in their bottoms already; how large the gains in their share prices will be this year will depend partly on [what happens in the markets], and partly on how powerful the fundamental developments are on a company-specific basis. Importantly, given my macroeconomic view (that the U.S. and global economy bottoms somewhere between May and December of this year), I am much more confident *on a two year basis* that each core position will be at a multiple of its current price by then. I still believe that in the long-term, the best way to invest in the stock market is to invest in the shares of companies that are on long-term secular growth paths, and *I believe that the secular growth path for each of my core positions remains intact.*"

So again I say: based on those facts, I can do nothing but resolve to persevere, believing that we will ultimately thrive again, and work to realize the value that I know is being created by the companies in these portfolios.

Best regards,



Hugh Cleland, CFA
Portfolio Manager

*Commissions, trailing commissions, management fees, performance fees and expenses all may be associated with investment funds. Please read the offering memorandum before investing. The indicated rates of return are the simple returns (YTD, 1 mo, 3 mo, 6 mo) or the historical annual compounded total returns (1 yr, 3 yr, 5 yr, and since inception). All returns are net of fees but do not take into account sales, redemption, distribution or optional charges or income taxes payable by any security holder that would have reduced returns. Investment funds are not guaranteed, their values change frequently and past performance may not be repeated.

The Innovation Fund and the RSP Fund invest primarily in North American equities with a sector focus on technology, healthcare and resources. Geographic and sector allocations may, however, vary significantly over time. Investments made are primarily in small cap companies believed to be trading at a discount to their intrinsic value and which offer innovative products and services and a sustainable competitive advantage. The funds normally follow a more concentrated investment approach where the manager may overweight selected core holdings and industry sectors in which the manager has particular conviction and/or specialized expertise. The funds may engage in short selling and may also use specified derivatives, such as calls and puts, warrants, index futures and exchange traded funds. In addition, the fund is permitted to hold private entities that are not included on any public markets or indices. This may result in portfolio weightings and investment performance being substantially different from that of the S&P/TSX Composite, TSX Venture, Dow Jones Industrial or other market indices.