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October 10, 2008

Dear Partners and Friends:

The Northern Rivers Innovation Fund LP (the Innovation Fund) was down 17.56% in September, and the Northern Rivers Innovation RSP Fund (RSP Fund) was down 16.41%. The returns, as of September 30, 2008, are presented below:

	Average Annual Returns to September 30, 2008*							
	2008 YTD	1 mo.	3 mo.	6 mo.	1 Yr.	3 Yr.	5 Yr.	Inception**
Northern Rivers Innovation Fund LP	-36.12%	-17.56%	-34.77%	-29.16%	-33.68%	10.87%	12.57%	18.63%
Northern Rivers Innovation RSP Fund	-37.44%	-16.41%	-34.15%	-29.33%	-34.94%	11.87%	N/A	6.44%

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

September was a month of building financial panic in the equity markets (underlaid by accelerating distress in the credit markets), and was marked by, for example, the S&P/TSX Composite Index (TSX) being down 14.7% during the month. That panic (and increased seizure in the credit markets) is accelerating in October, with the TSX now down 18.1% between September 30th and the close on October 9th. As I write this at 6:00 a.m. on the morning of Friday October 10, the European indices are all down in the 8% to 10% range. These are historical times.

I found it odd then, that on October 9 Dennis Gartman wrote in his daily commentary that “panic appears to be receding.” I hope he is correct, but I am not yet prepared to make such a statement (based on the indiscriminate selling I continue to see in fundamentally strong companies). I know that many of my most respected competitors (who find themselves down anywhere from -20% to -60% year-to-date) would also have a hard time agreeing with Mr. Gartman. (It is a testament to the viciousness of this bear market that virtually no investment manager has been spared startling declines: optimists, pessimists, value managers, growth managers, long-short managers, market neutral managers, merger arbitrage managers—almost all that I am aware of have been hit extremely hard. Truly stunning.) Nonetheless, I am encouraged that at the very least, the European Central Bank—which up until yesterday had been acting like the U.S. Federal Reserve Bank in the 1930-1932 period—has finally awoken

to the enormous magnitude of the problems facing the global financial markets (especially the credit markets) and economies, and has stated that, it too, will “do what is necessary” to restore confidence and liquidity to global financial markets. More on this later.

It is an appropriate juxtaposition to Mr Gartman’s comment to point out that yesterday, October 9th, was the 1 year anniversary of the S&P500’s all-time high. On October 9, 2007, the S&P500 hit an all-time high of 1,565.2. It closed at 984.5 on October 8, 2008, representing a peak-to-trough decline to date of 41.9% so far. More relevant to the Innovation Fund, the peak-to-trough declines for the TSX and TSX Venture Exchange (from which the vast majority of the Innovation mandates investments are selected) are -36.7% and -69.1% respectively. In fact, the TSX Venture Exchange Index is *now up only 4.2% since its inception* in December of 2001. That 4.2% is *not* an annualized number. The index began at 1,000 in December of 2001, and now stands at 1,041.7 as of the close Thursday October 9, after having hit at an all-time high of 3,372 on May 11, 2007. Truly stunning.

How is the base case evolving amidst the current financial panic?

In the last letter, I discussed “necessary but not sufficient on their own” conditions for a market bottom. I outlined a number of necessary conditions that were already in place, and more are in place *now* than when I wrote the last letter. But the fact is, many necessary conditions for a bottom have still *not* been put in place. For example, the European Central Bank probably needs to cut their benchmark rate another 1.5% or more. Of course, compounding the difficulties, it’s *very* difficult to know when enough “necessary” conditions are in place to be “sufficient” to put in a bottom.

From the last letter:

“...bear market bottoms cannot be put in while the majority of central banks are in a tightening stance. Recent developments with oil [now in freefall] and the financial system should allow most central banks around the world to move rapidly to an easing stance, and probably to embark on dramatic easing campaigns by the end of the year (and hopefully sooner!)...My guess is that the growing clarity among Western central banks and governments that this is an unprecedented crisis will lead to concerted action beginning in September or October. A “Resolution Trust Corp”-type entity set up by the U.S. Federal Government to deal with toxic mortgages is probably another ‘necessary but not sufficient on its own’ ingredient to a healing process that gains traction. What does this mean for the markets? My best guess is that there is another 10% downside in the overall indices before we finally get a lasting bottom. The thing is, the way things are unfolding, it looks like that 10% will be viciously swift, probably being over by the end of October...”

I got a few things right in what I wrote, but I was very wrong on the magnitude of the decline (i.e., most major equity markets are down well over 20% since I wrote the September 17 letter), and my expectation that measures such as the introduction of a “Resolution Trust Corp-type entity would at least result in bounces lasting a few weeks (or longer) was also wrong. In fact, as it stands as of the close yesterday, the Dow is at 8,500—a number I simply was not

expecting to see ever again, and a number that is only 10% to 15% away from the October 2002 bear market lows!!! I still think that the declines ahead “will be viciously swift”, however, and they will probably be over by the end of October (or perhaps November, in that it is very notable that *every bear market in history has ended in either September, October or November!!*)

Indeed, we are ‘so close, and yet so far’ from having the ‘necessary AND sufficient’ conditions in place for a lasting market bottom. Although it appears that we likely have a long way to go in terms of necessary policy response and that we have another 10-15% downside in the major indices from the October 9 closing levels,¹ I believe that we are VERY CLOSE in *time* to getting to the October 2002 lows, and VERY CLOSE in *time* to getting the necessary policy responses to be sufficient to put in the low. (For example, I am expecting *very soon* a MUCH MORE SIGNIFICANT COORDINATED RATE CUT than the laughably small one we saw on Wednesday, October 8.) The irony is that the “best case” (and one I am actually hoping for now) is a very swift (almost 1987-like) trip to the October 2002 lows. I strongly believe that has the best chance of setting the stage for a very strong 2-3 years to follow.

Especially in these extraordinary times, it bears repeating that the core companies in the portfolios continue to get *stronger* fundamentally, and are putting the building blocks in place for dramatic share price appreciation once the markets return to some sense of normalcy. It also bears repeating that I believe that the best way to generate wealth in the stock market is to identify and own the stocks of companies that have a “sustainable competitive advantage” and are on a long-term secular growth path that will allow their stocks to rise over periods of 2-5 years, no matter what the macroeconomic environment throws at them.

On a related note: as I have re-read my last letter many times over the last month, it has become apparent that portions of that letter are a “manifesto” of sorts about my investing style and approach, philosophy and beliefs. I would encourage anyone who can make the time to re-read that letter to do so, and better yet, I would encourage everyone to read the book “Common Stocks, Uncommon Profits” by Phil Fisher.

The genesis of my investing philosophy and approach is Phil Fisher, commonly considered to be the “father” of growth investing.

His philosophy and approach was born in and tested during the 1930s. He had the “horrible misfortune and great good luck” to start his investment firm in 1931, just as the Great Depression was really kicking into gear. It is based on his writings that I developed my “off the beaten path due diligence” methods (identifying odd little industry conferences where I can mix with the salespeople and ‘foot soldiers’ of an industry), and it is based on his ideas that I have developed my approach of constructing the portfolio around large “core positions” that I hold through big ups and big downs, as long as the “core investment hypothesis” is intact. In fact, his beliefs, philosophies and due diligence methods are so key to what I do that I have bought 30 copies of his book “Common Stocks, Uncommon Profits” in hopes that some of you

¹ That would represent a return to the October, 2002 bear market lows.

will ask for a copy, and make the time to read it so that you will better understand what I do, and where my beliefs come from, and why I believe so strongly that *this* approach is the best way to generate wealth in the stock market over the long-term. To be clear: I am offering a copy of this book to whomever would like to make the time to read it. Please contact Jeffrey Zicherman at 416-597-8508 to arrange to have a copy picked up or sent to you.

Indeed, three statements from the last letter may as well have been written by Phil Fisher himself:

- 1) “Powerful bear markets like the one we are in represent major “re-sets” in future potential return. Yes, they take back a lot of the gains made during a bull market [even in the secular growth stocks!], but they load the spring for future returns when the market conditions allow fundamentals to drive stocks once more.”
- 2) “As long as the ‘core investment hypothesis’ is intact for a core position, I am a buyer as its stock goes lower. This is because, if I am right that the core investment hypothesis is intact and that the company is on a secular growth path, then FUTURE RETURNS GET HIGHER THE LOWER THE STOCK GOES. (This is why Phil Fisher held—and bought more—Motorola between 1955 and his death in 1984, even as the stock experienced enormous peak-to-trough declines on several occasions.)
- 3) (Drawing directly on points 1 and 2) “...whether we bottom in the next month, three months, or longer, this far into a bear market is not the time to be pulling capital out of the market. Rather, it is the time to be committing more capital (in stages) to the [secular growth stocks].²

I made further contributions to the funds I manage on August 31, and—putting my money where my mouth is—will contribute more at the end of October

As discussed in the last letter, the Innovation Fund has now been reopened. It is a strong signal that Likrilyn Capital Corporation (the family office parent company of Northern Rivers Capital Management Inc.) has already made a new investment on September 30, and plans to make a further investment in the LP between now and year end. I am also encouraged that a number of family and friends have also indicated they will make a further investment before the end of the year.

Thank you for your trust and patience

In the midst of this unprecedented volatility, I want to thank all of our partners and unitholders for the patience and understanding they have exhibited. Redemptions have not been a major factor for our funds and we are gratified that some of you are investing new money in these difficult times. We are confident your patience will be rewarded in time as we stick to our

² Of course, whether it is Phil Fisher saying this or me, we would both recognize varying circumstances often result in less than optimal situations and perversely, it is often the case that when we should be committing the *most* to the market is when we feel we can least afford it.

investment discipline and manage through these difficult times. Thank you again for your support.

Next closing

The next closing for the Northern Rivers Innovation Fund LP, the Northern Rivers Innovation RSP Fund, the Northern Rivers Conservative Growth Fund LP, and the Northern Rivers Global Energy Fund LP is October 31, 2008. I would like to remind our investors that I am always willing to take time to meet with them over the phone or in person, and would encourage people to set up a breakfast, coffee or lunch by contacting Robyn Lyle at 1-866-902-7060, ext. 222.

Please contact Jeffrey Zicherman, Sales Associate (ext. 237) or Robyn Graham, Vice President Sales and Marketing (ext. 236) for more information regarding the other funds offered by the Northern Rivers team, or you can reach any of the portfolio managers at Northern Rivers to discuss the specific funds under their management by calling the same toll free number above.

Best regards,



Hugh Cleland, CFA
Portfolio Manager

*Notes: 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. Short selling may provide the funds with opportunities for gains and risk mitigation when markets are volatile or declining. The same fundamental analysis is used in determining whether securities of a particular issuer should be sold short. The funds may also use specified derivatives, such as calls and puts, warrants, index futures and exchange traded funds. 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 and S&P500 indices.