GOODWOOD INC.

THE

GOODWOOD

FUNDS

2004 Annual Report
Ninth Edition

Goodwood Inc.
Introductory Letter

This is the Ninth Annual Report and we are pleased to note that in 2004 the Goodwood Fund “A” units and the Goodwood Fund “B” units returned **15.15%** and **12.72%** respectively. The Goodwood Capital Fund achieved a **13.63%** return. In comparison, the S&P/TSX Composite Total Return Index (“TRIN”) appreciated by 14.48% and the S&P 500 Index gained 8.99%.

We are comfortable in being characterized as value investors, which by association, makes us contrarians. We do believe our investment discipline is repeatable. And due to our company specific approach, the Fund’s performance in the long term will not be dependent on the major markets moving higher. We prefer to limit the portfolio to 30 positions, not equally weighted, but rather concentrating the Fund’s capital to our best “core” ideas. We are most attracted to high quality assets that generate significant cash flow from operations or possess unrecognized assets that are not properly valued in the current share price, although this “value” definition would be far too limiting.

As significant co-investors in the Funds, we remain extremely cognizant of the downside risk inherent in investing and therefore, spend considerable time in our detailed analysis before an investment is allowed to become a “core” position. At Goodwood, we define a “core” holding as one that receives a 6% or higher weighting (at cost) within the portfolio. Each year we realistically hope to find three maybe four new candidates worthy of this capital allocation, and if successful, our historical results demonstrate that it can be very accretive to the Fund’s performance. As of December 31, 2004 the Goodwood Fund “A” units have achieved an annual compound return of **21.71%** (net of all fees) versus the S&P/TSX Composite Total Return Index of 8.10%.

One of Goodwood’s self-imposed investing rules is that we need to become acquainted with a company’s management team, board of directors, suppliers, customers, and competitors. It has been our experience, that this “grass roots” approach provides the foundation to better understand the investment opportunity. Thereafter, we will closely monitor the operating results achieved and hold them accountable to stated goals and industry comparables. Obviously, we are not passive investors (nor, despite our success with Creo, should we be characterized as activists) however, we do firmly believe that our “corporate coaching” approach improves the risk to return profile of the Fund.

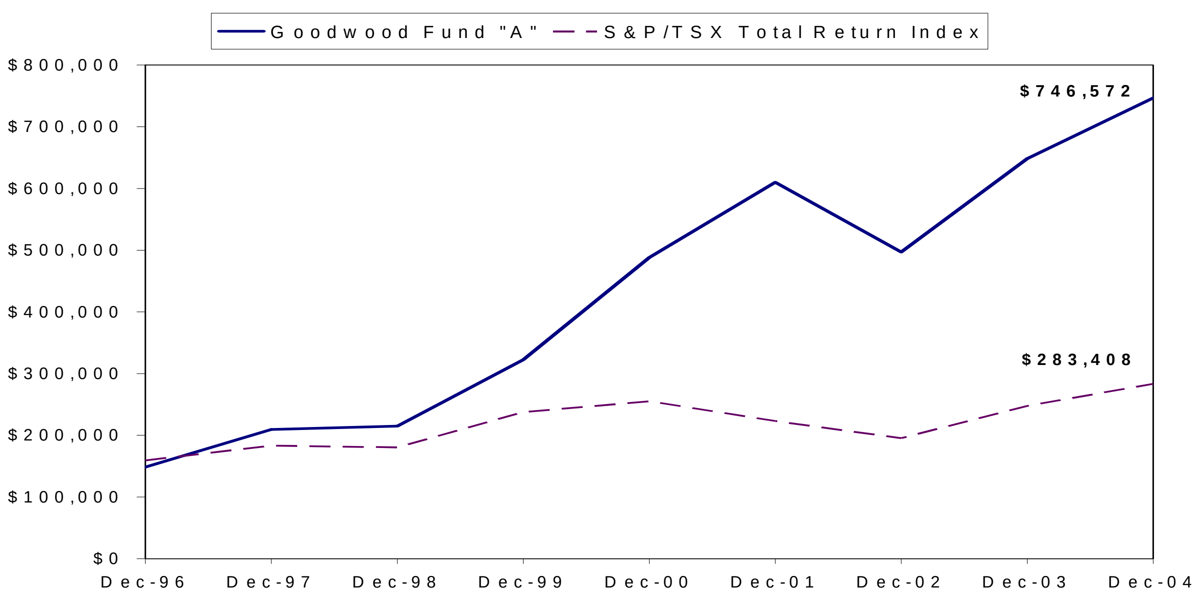
Consistent with the years past, a copy of the 2004 Annual Report will be mailed to all of our unitholders following the Annual General Meeting which this year, will take place on April 14th, 2005. If you were unable to attend the meeting we would certainly encourage you to read this Annual document. And importantly, if you are not receiving our monthly “Investment Commentary” (via e-mail), please let us know and we will gladly include you on our distribution list.

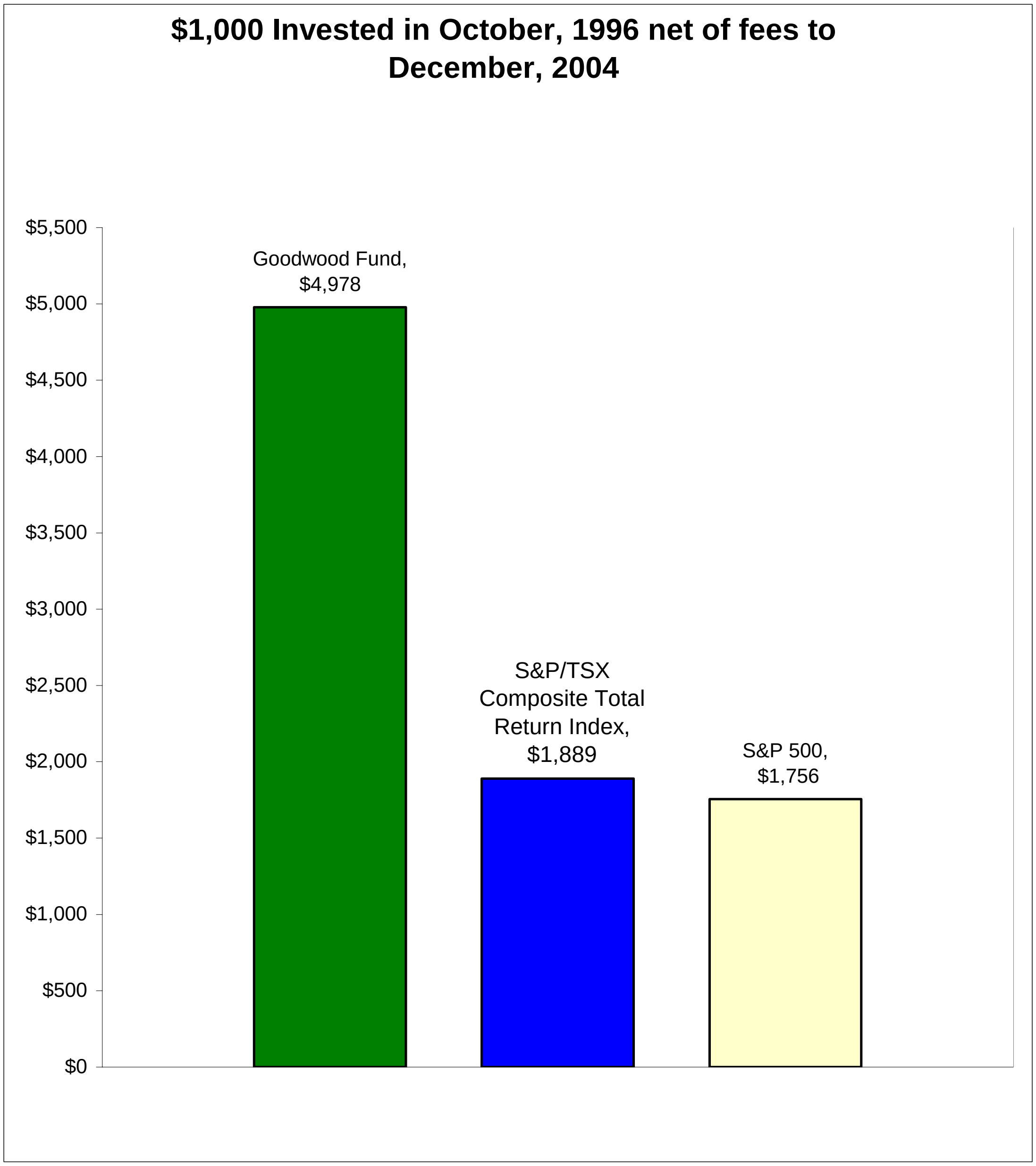
In order for Goodwood to continue our success we need to be strong proponents in providing timely and detailed disclosure. Trust and clear communication are very important in our business, particularly when we have a number of unitholders throughout Canada and the rest of the world with whom we have not personally met. However to be completely candid, our monthly transparency is somewhat self-serving. We are of the opinion, that if a Goodwood unitholder better understands how their capital is allocated and the investment rationale behind that commitment, that unitholder will become a more confident and a long-term investor within the Fund.

Year-Over-Year Returns

October 31, 1996	$150,000	
December 31, 1996	148,588	N.A.
December 31, 1997	209,628	41.0%
December 31, 1998	214,764	2.5%
December 31, 1999	322,253	50.0%
December 31, 2000	487,891	51.4%
December 31, 2001	609,864	25.0%
December 31, 2002	496,856	-18.5%
December 31, 2003	648,347	30.5%
December 31, 2004	746,572	15.2%

Goodwood Fund
Comparison of Change in Value of $150,000 Investment since October 31st, 1996





A common question poised to us each January is our return expectations for the new-year ahead. Given the low conviction we have in our "in-house" macro sooth saying abilities, we prefer to focus our collective efforts on individual opportunities and allocate capital based upon our own stated return objectives.

Return Objectives

- Focus on providing superior, risk-adjusted returns utilizing a bottom-up, fundamental, research driven stock selection discipline, which generate profits from both the long and short positions of the portfolio.
- Manage a substantially Canadian based long/short portfolio.
- Generate primary research through an extensive network of contacts and bottom-up fundamental research of companies and industries.
- Concentrate on businesses that trade significantly below their intrinsic value.
- Think long term.
- Goal is to average 20% plus per annum, not every year -- just average.

Once again, we would like to highlight our web site (www.goodwoodfunds.com) as a valuable and complete source of information. Visitors to this site do not require a password and will be able to freely review performance data, past Investment Commentary's, and all nine Annual Reports.

We would like to recognize and thank our staff and Advisory Board for their ongoing contribution and support. Your individual and collective efforts make Goodwood a much better company.

Lastly, we want our unitholders to know that we do appreciate their continued confidence in allowing us to manage a portion of their capital. It is a responsibility we take very seriously and endeavor to reward your decision with an attractive rate of return.

Respectfully submitted,

Cameron MacDonald, CFA
President and Chief Executive Officer
Goodwood Inc.
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March 31st, 2005

THE GOODWOOD FUND
2004 Annual Report

To the Unitholders of The Goodwood Fund:

For the year ending December 31, 2004, The Goodwood Fund's (the "Fund") "A" unit net asset value ("NAV") per share increased by **15.15%** while the "B" units increased by **12.72%.** The S&P/TSX Composite Total Return Index ("TRIN") increased by 14.48% in the same period.

From October 31, 1996 (the commencement of the Fund's public operations) through to December 31, 2004, the Fund has returned **21.71%** per annum net (after all fees) versus the TRIN's per annum return of 8.10%. [*]

The Fund's 2004 audited financial statements are attached for your review.

During 2004 (based on month end figures), the Fund averaged a **103.3%** invested position (i.e., market value of long positions plus market value of short sale positions as a percentage of the Fund's equity). At one extreme the Fund was **115%** invested, composed of **107.3%** long and **7.7%** short, leaving a "net market exposure" (i.e., longs minus shorts as a percentage of the Fund's equity) of **99.6%**. At the other extreme, **87.7%** invested **–** **78.1%** long and **9.6%** short for a net market exposure of **68.5%**. In summary, we carried a more net long than normal stance through much of 2004, which turned out to be a good thing.

While the Fund does not have a formal target ratio of percentage invested or percentage allocated to longs versus shorts, effort is made to maintain some balance of longs and shorts (with a preference for long ideas – for reasons explained below) and to minimize leverage.

In past Annual Reports, we have repeated some basics from the "Goodwood Philosophy". We view this as very important for our unitholders to <u>read and reread each year</u> – it provides a good overview of our style of investing and it's in our collective interests to have an informed unitholder. Please see "The Goodwood Philosophy" attached as an appendix after this letter.

[*] Note that the indicated rates of return are the historical total returns over the periods noted, including changes in unit value and reinvestment of all distributions. These indicated rates of return do not take into account any redemption charges that may have been payable by redeeming unitholders, which would have reduced the returns of redeeming unitholders in certain circumstances. Please refer to the Offering Memorandum for details concerning the redemption fee schedule of the Fund. In addition, note that performance data represents past performance and is not necessarily indicative of future performance.

The Goodwood "Activist" Fund?

For sure the highlight of 2004 for the Fund was our very successful effort at unearthing shareholder value at Creo Inc. ("Creo"), a company that we discussed in detail in last year's Annual Report. Given the considerable positive contribution that our Creo efforts made to both 2004 and early 2005 results, it seems appropriate to spend some time recounting the events leading up to our dissident proxy efforts and culminating in Eastman Kodak Company's ("Kodak") proposed acquisition of Creo.

Going into the fall of 2004 we had owned Creo stock for approximately two and a half years. We patiently waited for incumbent management to deliver an often-promised but not-yet-delivered earnings acceleration, which should have been a logical byproduct of Creo's inherent operating leverage. But, even long-term, patient shareholders (a label the Fund can rightfully claim) have their limits. The tipping point for us came with the realization that incumbent management's new, aggressive move into digital printing plate manufacturing carried great financial and operational risk (a move that had been endorsed by the incumbent Board of Directors ("Board")). The large amount of capital required to acquire and build new plate manufacturing capacity and to stock worldwide inventory would have likely depleted Creo's excess cash balance and possibly put the Company into a leveraged state for the first time. And, the manufacture and sale of digital printing plates put Creo up against the titans of the printing supply industry, specifically Agfa-Gevaert N.V., FujiFilm Co. and Kodak PolyChrome Graphics Ltd. - who, it is estimated, collectively control over 80% of the digital plate market. These companies have much deeper pockets than Creo and have established low cost plate manufacturing facilities and worldwide distribution infrastructure. It seemed to us that the outcome of this new strategic direction could be disastrous for Creo as the big three competitors gear up their production of digital plates (likely to happen as analog plates are supplanted by digital plates) and, in the process, drop prices across the board (analog plates, by far the most commonly used today, are priced at a fraction of the cost of digital plates).

It is fair to say that, at this point in the history of our Creo investment, the Fund could have simply tucked its proverbial tail between its legs and walked away quietly (this course of action certainly would have required less time and legal costs). However, our adamant belief that Creo had tremendous value potential much in excess of the then share price and the Company's reputation, product quality, industry brand name and dominant worldwide market share in "computer-to-plate" machines kept us from simply walking away. We felt strongly that, under the right cost structure and without taking undue capital allocation risk, Creo's shares could trade for a level much closer to its potential value.

Our attempts to get the incumbent management and Board to rethink their beliefs in regards to both cost structure (Creo's was clearly bloated) and the embryonic plate manufacturing business were going unheeded (to say the least). Through phone conversations, meetings and letters we pressed forward the notion that Creo's share valuation would be materially higher if its cost structure were brought in line with industry comparables and that its digital plate business invoked too much financial risk. An informal canvassing of other major shareholders revealed a high level of frustration at the lack of current earnings and the poor share price performance. While we were expecting many dissatisfied shareholders given the stock was trading just above tangible book value and was down 53% over the five years ending in October 8, 2004 (the last trading day before we made public our intentions), the overall level of disappointment surpassed even our expectations.

Having decided to not sell our next step was to figure out how we could help unlock Creo's underlying value. We began by approaching a select group of well-known "activist" investors (these are groups who specialize in fighting the incumbent Board and management team in an effort to unleash shareholder value) from both Canada and the U.S. with a well-prepared presentation rich in the details of Creo's foibles as well as Creo's potential upside. While all parties appeared interested, no group came forward to help us in our efforts. The next step proved to be a great move on our part, one that made us glad that none of the activist investors had bitten. We made a short list of individuals who could be parachuted into Creo (if we waged a successful proxy battle) and who could take the actions necessary to immediately bring Creo's cost structure to more normal levels thus paving the way for material earnings. At the top of the list was Robert G. Burton, Sr. ("Bob" or "Burton") who is to the printing industry what Michael Jordan was to the National Basketball Association. We called Bob to walk him through our Creo presentation and to gauge his interest. Shortly thereafter and to our delight, Bob expressed an interest in working with Goodwood and began to buy Creo stock along with us. His personal financial commitment amounted to some US$8 million, which we thought was one heck of a sign that he had confidence in our ability to get him installed as Creo's chief executive officer ("CEO") as well as confidence in his ability to bring meaningful, positive change to Creo.

Once our joint ownership exceeded 5% of Creo's outstanding stock we were required to file a Schedule 13D (this is a U.S. Securities & Exchange Commission requirement for any group acquiring 5% or more of a U.S. publicly-traded company – Creo was listed on both the Toronto Stock Exchange as well as the Nasdaq market in the U.S.). While we had always expected that the filing of the Goodwood/Burton Schedule 13D would cause a rally in the share price, we underestimated just how much of a rally. Burton's reputation for results combined with the great opportunity implicit in Creo's very inexpensive share price led to a 31% rally the day we filed. Over the next few weeks it became increasingly clear that there were numerous deep-pocketed institutional investors (particularly in the U.S.) who viewed the prospect of Burton running Creo as a very desirable outcome. As more and more stock traded, the percentage of stock held by Goodwood/Burton-friendly groups appeared to be ever increasing. By January of 2005, approximately three months after we filed, a large percentage of Creo's stock had turned over and the shares were trading roughly 76% above the price on the day before we filed. We realized that anyone purchasing shares at these new elevated levels was doing so only for two possible reasons: either Goodwood/Burton would win the proxy contest and Bob would have a shot at running the business (a good thing for the share price) or, Creo would sell itself to the highest bidder (also a good thing for the share price - Kodak was the clear front runner in that sense). It was pretty obvious to us that the buyers were not purchasing with the hope that the incumbents would continue as before. A return to the status quo would have been very hard on the share price now that Bob's managerial skills and/or a possible takeover were being priced in.

All of the above was not lost on the incumbents and so, not surprisingly, they began to market the Company in earnest to potential acquirers. Shortly thereafter, a takeover offer from Kodak was announced – this made imminent sense to us as we strongly suspected that the incumbent management team and Board would rather sell themselves to Kodak than face the ignominy of losing a proxy vote. Kodak's proposed acquisition price (the deal has yet to finalize although Goodwood has already sold its Creo stock) represents an approximate 88% premium to Creo's share price the day before we filed. And, this return was earned in a very short 4 months (if you ignore the two and a half years it took us to get around to being active with Creo!).

In spite of our Creo success, we want to assure our unitholders that the Fund has not changed its operating principles; we are not full time activist investors. However, if another Creo-like opportunity surfaced, we would not hesitate to evaluate the opportunity to be activist. After all, our value investment style means we are often invested in situations where the share price is well below intrinsic value. Why wait for the values we see as investors to be recognized by others if we know of a methodology to bring those values forward immediately? But, we must be realistic and cautious. There are costs involved in launching an action and so, one must be very sure of ultimate success. In retrospect, Creo was an unusually ripe example of activist opportunity as it had many favourable characteristics: a strong balance sheet (approximately US$1.27 per share in cash net of debt), a share price trading just a little above tangible book value (thus very cheap), a worldwide reputation for product quality, a worldwide leading market share, control was "in the market" as only 10% of the company was owned by insiders and a key was available to unlock shareholder value - Bob's willingness to roll up his sleeves and get involved. While always on the lookout, Goodwood will be fortunate to find more such situations in the short run.

RRSP Foreign Content Restrictions and the U.S. Dollar

Sharp on the heels of our Creo victory, the Canadian Federal Government shocked Bay Street in announcing that Registered Retirement Savings Plans ("RRSP") and Canadian pension plans would no longer face the antiquated foreign content restriction rules. We couldn't be happier. While we are primarily focused on Canadian situations, we can't help but be tempted by the sheer quantity of interesting U.S. small cap situations (a U.S. small cap situation is often equivalent in size to Canadian mid or even large cap). Just knowing that we can broaden our focus and not be tethered to a maximum of 30% non-Canadian content (a number that, if you add our longs and shorts together, we've been brushing up against for the last couple of years) has us salivating at the prospects. The fact is that we have already made major commitments in situations that are primarily U.S.-based (e.g., the Great Atlantic & Pacific Tea Company, Inc. and Laidlaw International, Inc., both discussed later) and that many of our Canadian holdings have significant business exposure outside Canada (e.g., Kingsway Financial Services Inc. ("Kingsway")).

However, we want to assure our investors that there is no radical, overnight change in operating philosophy here …we're just excited that our universe of potential money-making, special situations has broadened by a factor greater than 33X (if you estimate that the Canadian equity markets represent roughly 3% of global, developed market capitalization and less than that if you exclude Canada's disproportionate representation of oil and gas companies – Goodwood has tended not to invest in commodity plays).

The more perceptive readers have already jumped to the next logical question …what does all this imply for Goodwood's future non-Canadian dollar currency exposure – especially in light of the marked depreciation of the U.S. dollar of late? Well, let's begin answering this important question by making a few observations.

First of all, it is totally incorrect to assume that a Company that is listed on a U.S. stock exchange is by definition an entity that earns its net income in the U.S. and therefore in U.S. dollars (for purposes of this discussion we are assuming that net income is the only source of economic value). A large percentage of U.S. companies have significant earnings contributions from outside the U.S. For example in calendar 2004, that bastion of U.S. capitalism, International Business Machines Corp. ("IBM"), generated 42% of its revenues and approximately 58% of its net income in currencies other than the U.S. dollar and that's after factoring in its considerable hedging programs. Thus, while IBM is definitely a U.S. company in principle, in economic reality it is far from a U.S. company. Just how prevalent non-U.S. dollar earnings are in U.S. companies is hinted at by the crescendo of fear in the U.S. stemming from increased offshore outsourcing (as typified by many U.S. manufacturing jobs being effectively exported to low wage countries such as China and software jobs exported to India). So while these are U.S. companies by headquarters and by stock exchange listing, in many cases a large chunk of their economic value is located elsewhere and thus, their U.S. dollar risk is much less than initially thought. This point applies in reverse to Canadian stock exchange listed companies, which, while they would easily meet the RRSP guidelines for Canadian content, derive much of their economic value from outside Canada (e.g., Kingsway which generates approximately 70% of its sales from the U.S., in effect Kingsway is more of a U.S. company than IBM!). The key point being that an informed investor needs to actually look underneath the hood of the earnings engine to truly understand what sort of currency exposure is being taken. **A simple calculation of the percentage of the Fund's capital invested in U.S. versus Canadian names is too simple and won't yield an accurate reading of true currency exposure.**

Secondly, the Fund always maintains short positions, even if a relatively modest amount over the last couple of years. To the extent that these short positions are in U.S. companies (that is, U.S. companies that actually derive their economic value primarily from the U.S.) they act as an effective hedge against our U.S. dollar long exposures. Thus, if we wish to maintain a purely Canadian dollar composition, we need only worry about our net U.S. exposure (market value of longs minus market value of shorts).

Finally, the fund has tools at its disposal to hedge away our U.S. dollar net exposure even though we are prohibited (see the Offering Memorandum) from utilizing derivatives of any sort. The tool that we've used mostly to date in this capacity would be to short sell U.S. Government T-bills of various short maturities. The cost of our short is the T-bill yield, making the cost to short fairly inexpensive given the level of interest rates.

In summary, despite our likely increased activity outside Canada, we plan on maintaining a low net U.S. dollar exposure (or for that matter any non-Canadian dollar). We will achieve this through the use of offsetting short positions as well as any other low cost means that we may find. This is not a currency call by Goodwood (it has become trendy to be a U.S. dollar pessimist), rather this is an admission by us that we are primarily Canadian focused and we feel that we should maintain our net long Canadian currency bias.

Market Outlook

Yet again we plan on severely disappointing you with a nonexistent market prognostication. We have never provided a market call and we're not planning on starting to do so anytime soon. As readers of past Annual Reports know, we believe that a successful, long-term investment track record is most likely achieved through judicious bottom-up stock selection. It may not be as exciting as making a big, macro-economic market call but it is a repeatable process that we relish and enjoy. Goodwood's office morale takes a noticeable upturn whenever the next above average idea pops up, not when one of us believes that we have had a flash of brilliant insight that the S&P Index will end the year at some precise level.

Quantifying the Upside – Discount to Intrinsic Value

We estimate our current discount to intrinsic value to be 27% suggesting a potential upside in the portfolio of roughly 38%. As a reminder, this measure is meant to give our unitholders an idea of the potential upside inherent in our current long holdings if they were to rally to our estimates of intrinsic value – i.e., their values as businesses, which can differ substantially from their share prices. We believe that these estimates are conservative, which is backed up by our historical pattern of sometimes selling prematurely, and they do not factor in that we may buy more of these ideas, that the business value estimates may increase going forward and that we may find more ideas during the year. But keep in mind that this is not a one-way street. Future events could lower our potential portfolio upside as well. As well, remember that these are just estimates of intrinsic value, they are not meant to imply that we are certain that a given stock will trade for a given share price within a given period of time.

As always, we expect to take the portfolio return potential higher, in particular through adding to some of our lesser-weighted existing positions and/or through the introduction of new ideas. Adding one or two high quality ideas at a 5% or more weighting that have the potential to double (or more) in the case of long ideas and, the potential to drop materially in the case of short ideas, would add materially to the Fund's potential upside.

Review of Core Positions

The following is a review of our four largest current long holdings; all four of which will be familiar to readers of past Annual Reports. Note that the first three of these positions appear to be in the final innings of our investment holding period, as they are all close to our intrinsic value-derived sell targets. Collectively the three represent almost 25% of the Fund's capital. While we are inclined to hold them until our price targets are reached, the arrival of new, better quality ideas (some of which are already in the Fund working their way higher) would cause us to speed up our selling.

CanWest Global Communications Corp. ("CanWest"): CanWest's contribution to the Fund's 2004 results was modest: starting the year at $13.85, drifting as low as $9.15 by September of 2004 and ending the year at $14.46. However, our original cost was in the $5 range. CanWest continues to be a large holding of the Fund as we see additional upside in its share price. While the downside volatility in CanWest's share price had a negative effect on the Fund's reported net asset value at times during the year, it also gave us an opportunity to buy more stock well below what we believed to be ultimate intrinsic value, thereby allowing us to increase our return for the year (another example of why long term unitholders tend to outperform short term unitholders …over the long run).

There are many potential value drivers that could take CanWest's shares into the price range where we would become sellers, but one in particular comes to mind that being the conversion of CanWest's newspaper/Canadian media business to an income trust. The proliferation of income trust conversions in Canada has really accelerated as evidenced by even suboptimal candidates being "trusted" - e.g., companies whose cyclical histories and/or poor historical record of free cash flow generation wouldn't normally make them appropriate candidates for such a structure. Given the market's thirst for yield/income trusts, the substantial free cash flow generation of CanWest's newspapers and the barriers to entry, CanWest for sure would attract a very substantial valuation as a high quality, large trust.

Laidlaw International, Inc. (Laidlaw): We accumulated most of our Laidlaw stock between November 2003 and January 2004 and it is currently trading roughly 35% above our average cost. This is an example of a position where the declining U.S. dollar has eaten into our profits as the bulk of Laidlaw's earnings are derived from the U.S. notwithstanding the Company's Canadian roots. Nevertheless, Kevin Benson, President and Chief Executive Officer of Laidlaw, has done an exceptional job of increasing shareholder value with the tools he had at his disposal upon Laidlaw exiting bankruptcy protection and we fully expect more of the same going forward. The company has sold its non-core healthcare businesses for cash proceeds of US$775 million and used the proceeds to significantly reduce indebtedness. This puts Laidlaw one big step closer to an investment grade rating which will increase the valuation investors are willing to apply to Laidlaw's equity. Our initial target valuation is approximately 23% higher than current levels (we're being conservative, it could be higher) and, we wouldn't be surprised if that level was achieved in the near term.

Kingsway Financial Services Inc. ("Kingsway"): Kingsway stock began the year at $14.60 and finished 2004 at a price of $19.00, nothing spectacular but solid. And, importantly that performance was achieved for the right reasons - namely the Company generated improved underwriting results. We expect a continuation of this improvement trend during 2005 and, in fact, there are some early signs that Kingsway has flipped from chronically "under-reserving for claims" to maybe even "over-reserving" as of late. If it becomes generally understood that Kingsway's reserving is healthy, we should see a lessening of Kingsway's historical discounted-versus-the-comparables valuation multiples.

Unfortunately, these internal improvements are happening in the context of an external environment that is changing slightly for the worse in Kingsway's U.S. markets. Property & casualty insurance companies are getting more competitive with each other on pricing and policy terms. Kingsway has already begun exiting some of the U.S. states where management feels things have gotten too competitive. We applaud their discipline in doing so, however, if conditions continue to worsen and/or spread to other states, while management continues to exercise good discipline, the end result will still be a lower stock price as the Company's revenue and earnings power will be substantially lower (nonetheless, still a better result than producing large underwriting losses). Will the trend toward a more competitive landscape supersede management's steady action towards restoring investor confidence? We'll be watching closely.

The Great Atlantic & Pacific Tea Company, Inc. ("GAP"):

Our first two years of ownership experience of GAP shares was noteworthy only as a result of the stock's volatility, swinging widely between the US$6 range and US$10 plus and back again. This pattern allowed us to take some extra profit out of the position as we traded opportunistically, buying on dips and selling on rallies. However over the last five or so months we began taking our GAP weighting higher based on our sense that the timing was right. [As an aside, Sun Life Financial Inc. (on its initial public offering), Creo Inc. and GAP are the only positions in the Fund's history where we have gone to a full weighting]. During these last five months GAP has begun trading like an Internet stock of the late 1990's, rocketing from the US$6 level in October 2004 to its current US$14.90. Mind you, this was a stock that used to trade well north of US$30 per share and that had hit a bottom of US$3.85 in March of 2003.

This down-and-out collection of U.S. and Canadian grocery stores with a history going back to 1859 had fallen completely off the radar screen of investors, as often happens when a stock no longer has a market capitalization large enough to warrant being followed by mainstream analysts and investors. The losses reported over the last couple of years had not only made GAP an "orphaned" stock but had led to fears that GAP would go bankrupt. GAP's controlling shareholder is the Haub family of Germany, a family which Forbes magazine estimates has a net worth of US$4.3 billion (thus their investment in GAP, currently worth some US$328 million, is not that significant to the family's overall financial health). The Haub's own approximately 57% of GAP and so, the shares actually available for the public to invest in (referred to as the "float") is only 43% of the 38.6 million total outstanding or 16.6 million shares. This small float level exacerbates the "orphaning" phenomena.

While there is a very strong argument to be made that investing successfully over the long run is best achieved by focusing on the healthiest companies (i.e., the market leaders with strong balance sheets and strong competitive positions), a very substantial return can be made from time-to-time in GAP-like situations. If, through intensive research, an investor can come to understand that the market is wrong in assuming the imminent death of a particular company, then great investment profits can be made as the market eventually cottons on to this and the underlying equity value reflates.

In the case of GAP it became obvious to us that GAP's Canadian business ("GAP Canada") is very healthy and, in fact, carries substantial value - augmented by its strategic importance to GAP Canada's competitors (namely Metro Inc. and Sobeys Inc., both of which would like to gobble up GAP Canada's estimated 16%, prime Toronto-centric, Ontario market share). GAP Canada's value is disproportionately larger than its revenue contribution (approximately 70% of GAP's total sales come from its U.S. operations) as GAP Canada is more profitable than GAP's U.S. operations and as valuation multiples for Canadian grocery chains tend to be higher (another example of our earlier discussion of foreign currency impact on the Fund's non-Canadian investments and how each situation has to be evaluated on its own merits). In a valuemaximizing sale, we estimate that GAP Canada could fetch as much as US$26 per GAP share, more than enough to repay GAP's entire net borrowings of an estimated US$22 per share. As a reality check on our valuation work one needed to look no further than the trading prices of GAP's public bonds …they never traded at prices suggestive of a distressed situation even whilst the stock was making new lows.

Importantly, and in a much more behind-the-scenes-manner than our Creo activism, we have been encouraging GAP's management, controlling shareholder and Board to sell GAP Canada through numerous meetings, phone conversations and letters. However, in complete fairness to all those parties, we weren't telling them anything they didn't already realize or appreciate. The key point is that this was another situation that beckoned for us to speak up in an effort to do the right thing by our unitholders. We wanted to ensure that GAP's management, Board and controlling shareholder understood what the market would view as a good or bad step.

One of the main points that we keyed upon is that the status quo is clearly not an option. GAP's poor U.S. "earnings before interest, taxes, depreciation and amortization" ("EBITDA") performance, its large U.S. capital expenditure needs (a necessary evil if it is to seriously attempt to turn around its U.S. business) and interest costs on its not insignificant debt are conspiring to generate approximately US$100 million per annum of negative free cash flow (or about US$2.60 per share). In effect, every year that GAP continues in its current configuration, another US$2.60 of shareholder value is depleted. Regardless of just how wealthy the Haub's are having your investment waste away at such a clip, especially when there's a clear path available to stop the bleeding, is simply not acceptable. Selling GAP Canada would lead to a much higher share price (speculation about a sale of the Canadian business has really been behind the recent share rally) and the financial wherewithal to repay all or part of the debt and to undertake a meaningful reengineering of the U.S. business. The substantial negative free cash flow would be materially improved upon.

Our GAP average cost is approximately US$8.50 and our initial target, really just based on GAP Canada being sold for an attractive figure, is US$20 plus. Share price upside beyond this level will be a function of how well management and the Board can deploy capital and execute operationally. Until recently one would have been fairly skeptical that there was much value in GAP's U.S. business but recent events leave us more optimistic.

The Yucaipa Companies, LLC ("Yucaipa"), a Los Angeles based private equity firm just announced a US$150 million investment in a near-bankrupt competitor of GAP's – Pathmark Stores, Inc. ("Pathmark"). Ron Burkle, the billionaire founder of Yucaipa, is to the grocery business a sort of mix of Jack Welsh and George Soros, in that he is both a great operator and a great investor in grocery stores. That's how he made his money - by buying and selling grocery stores over the years for maximum profit. He and his talented Yucaipa management team plan to use Pathmark, whose stores represent one of GAP's main New York/New Jersey competitors, as a "platform for future consolidation". We believe that Yucaipa may help consolidate the crowded northeast U.S. market, with or without GAP's direct involvement, something that would help improve the overall level of profitability in the industry for the better (although, admittedly, a Pathmark bankruptcy would have been favourable too).

As well, we sense that management of GAP have adopted a new focus, one that doesn't shy away from taking meaningful steps to realign the U.S. store base. Illustrative of this new attitude is the apparent willingness to jettison non-core assets such as GAP's Detroit-based chain, Farmer Jack. Rumours abound that Farmer Jack's non-performing stores are being shuttered and that the bulk of the chain is being offered for sale. Again, this would lend a helping hand to GAP's stock as GAP's EBITDA would improve by an estimated US$20 million on a current estimated U.S. operations EBITDA run rate of US$145 million. As well, selling Farmer Jack would free up management time to focus on the core northeast U.S. operations.

While it is too early to tell, selling GAP Canada combined with improved U.S. operations could take the stock close to or even above the US$25 level.

Looking Forward:

As you know from past Annual Reports, we have been loath to make macro economic predictions (taking the point of view that our opinion has the same chance of being right as the majority of the population say, 50/50). Our focus continues to be "bottom-up", one company at a time.

On both the long and short side new ideas are constantly coming into view across many different sectors. As always our long emphasis will be on finding inexpensive, high quality situations that are not well followed or are misunderstood. When combined with dubious, expensively priced short positions, the portfolio has the ability to do well in any market environment.

Please call if you have any questions, thoughts or investment ideas.

Respectfully submitted,

Peter Puccetti, CFA
Chief Investment Officer
Goodwood Inc.

March 31, 2005

The Goodwood Philosophy

Expectations and Rate of Return:

To avoid any potential misunderstandings, we want to stress to you that we have no idea what the Fund's rate of return in any one-year period may be. Stock investing does not lend itself to accurate predictions of returns. What should be expected is to earn a return over the long run that is above the risk free rate of return (the risk free rate of return is commonly defined as the return of treasury bills issued by the Federal Government) thus justifying the extra risk incurred.

Our hope is to average at least 20% plus per annum, not every year - just average, which, if it is achieved, will be a mix of good years and bad years.

Frequently Asked Questions:

In meeting with prospective and existing investors some common questions recur as follows:

Why do we prefer longs over shorts?

The following three reasons are key:

i. A good long idea sometimes holds the potential for a double (100% return), triple (200%) or more of invested capital, while the most one can profit from a successful short idea is 100% (i.e., the security in question drops to $0.00).
ii. Equity markets, with some notable exceptions, have tended to rise most of the time (i.e., let's go with the best odds).
iii. Other investors are likely to recognize a good long idea faster than to act on a good short idea because management is often touting the positives (and usually not saying much about the negatives). Also, there is far more investment capital geared to buying stocks than shorting stocks.

Why doesn't the Fund employ derivatives and utilize more leverage?

We are prohibited from using derivatives and we have self-imposed (and mandated by the Offering Memorandum) restrictions on our use of leverage. While very bright people can and do make effective use of large amounts of leverage and complicated derivative strategies, it is interesting to observe that the hedge funds that "self-implode" tend to be voracious consumers of these tools.

Furthermore, we have no past expertise in derivatives nor in strategies that involve borrowing large amounts. Finally, our relatively large position concentration at the top end of the Fund gives us plenty of "zing" (obviating the need for leverage) in our results.

What risk control methods do you employ?

On the long side we will not take major weightings in Companies where our success is dependent on a “greater fool” existing at the time we wish to exit an investment (e.g., situations where the current stock price already reflects distant, assumed success). We limit our chances of incurring permanent loss of capital by focusing on Companies that have substantial tangible value underlying their share prices – a “safety cushion”.

In regard to short sale positions we apply a 15% stop loss against full positions (5% weighting or more). During past bull markets, this discipline has protected the Fund from capital erosion and, perhaps more importantly, allowed us to reinitiate the short idea at a later date (e.g., our ongoing short position in Nortel Networks Corporation in 1999 and 2000).

We limit the size of our total portfolio in relation to the Fund’s equity. We are often underinvested. The market value of our long positions plus our short positions is frequently below 100% of the Fund’s equity. In fact, over the 8 plus year life of the Fund we have averaged **93.2%** invested (i.e., market value of longs plus market value of shorts expressed as a percentage of equity).

We do pay close attention to our net long stance - the market value of our long positions minus the market value of our short positions expressed as a percentage of the Fund’s equity. Historically, we have not wanted this measure to read less than 50% nor more than 100%. Our average net long exposure during 2004 was **82%**. Thus, as compared to a traditional, long only mutual fund, we had less of our client’s (and our own) dollars exposed to market risk (a typical equity mutual fund would remain close to 100% invested at all times). When considered over the long run, this tendency of the Fund to always have much less net long exposure than a traditional equity mutual fund and, still post performance above the benchmark index, is the investment equivalent of the “best of both worlds”.

Finally, the process of amassing a core position is best done slowly. The more time available to analyze and understand the pros and cons of a holding, the less likely we are to make a mistake. We can’t emphasize enough that taking our time allows us to think through a situation, observe results and perform as much comparative research as we can before we make a major commitment. And, as has happened too many times in the life of the Fund – rushing our decisions can often result in an unsatisfactory investment.

THE GOODWOOD CAPITAL FUND
2004 Annual Report

To the Unitholders of The Goodwood Capital Fund:

For the year ending December 31, 2004, The Goodwood Capital Fund (the "Capital Fund") increased **13.63%**. The S&P/TSX Composite Total Return Index ("TRIN") increased 14.48% in the same period.

From December 23, 1999 (the commencement of the Fund's operations) through to December 31, 2004, the Capital Fund has returned **10.92%** per annum net versus the TRIN's per annum increase of 3.70%. *

No distribution was paid for 2004. The Capital Fund's NAV per unit as at December 31, 2004 amounted to **$14.43.**

The Capital Fund's 2004 audited financial statements are attached for your review.

For a more detailed discussion of Goodwood Inc.'s investment philosophy and some of the Capital Fund's core holdings, please refer to the Annual Report of The Goodwood Fund, which is attached.

Please feel free to call if you have any questions, thoughts or comments.

Respectfully submitted,

Peter Puccetti, CFA
Chairman & Chief Investment Officer
Goodwood Inc.

March 31st, 2005

* Note that the indicated rates of return are the historical total returns over the periods noted, including changes in unit value and reinvestment of all distributions. These indicated rates of return do not take into account any redemption charges that may have been payable by redeeming unitholders, which would have reduced the returns of redeeming unitholders in certain circumstances. Please refer to the Prospectus for details concerning the redemption fee schedule of the Fund. In addition, note that performance data represents past performance and is not necessarily indicative of future performance.