GOODWOOD INC.

THE

GOODWOOD

FUNDS

2005 Annual Report
Tenth Edition

Goodwood Inc.
Introductory Letter

This is the Tenth Annual Report, a small milestone, and we are pleased to note that in 2005 the Goodwood Fund "A" units and the Goodwood Fund "B" units returned **28.90%** and **26.13%** respectively. The Goodwood Capital Fund achieved a **29.80%** return making it one of the top performers in the Canadian equity category in 2005. Comparatively, the S&P/TSX Composite Total Return Index ("TRIN") appreciated by 24.13% and the S&P 500 Index gained 4.91%.

In keeping with our investment methodology employed since 1996, we remain active managers applying a value discipline to a concentrated portfolio. While we invest throughout North America we continue to view the Canadian market as an attractive opportunity to achieve above average returns. It has been our observation that Canada is generally viewed by foreign investors as a market to achieve oil, gas, and gold exposure. Conversely, U.S. investors typically do not look to Canada as the first stop in international asset allocation. However, given the significant cross border revenues, assets, plants, subsidiaries and inventories located on both sides of the Canadian and U.S. borders, we continually find quality assets that are ignored or misunderstood and as a result, improperly valued. Herein lays an investment opportunity.

This year's performance was achieved by a number of the core positions within the Fund, a few worthy of mention. On January 31st, Kodak announced a tender offer of US $16.50 for Creo Inc ("Creo"). As many of our unitholders will recall, in the fall of 2004 Goodwood Inc. (in partnership with Burton Capital Management, LLC) filed a Schedule 13D with the United States Securities and Exchange Commission seeking to remove and replace the Creo management team and Board of Directors. On October 8, 2004 the last trading day before the proxy contest was announced, Creo's shares traded for US $8.54 per share. Following our public filing and in anticipation of a change in corporate direction, Creo's share price appreciated to US $14.97 on December 31, 2004. Thus, Kodak's successful bid reflected a positive contribution to the Fund's performance in January 2005.

The Great Atlantic & Pacific Tea Company, Inc. ("A&P") started 2005 at US $10.25 and continued to appreciate in price throughout the year as the Canadian division was sold to Metro Inc. while the US operations were rationalized and reported improving results. A&P finished the year at US $31.78 and remains (as of March 31, 2006) one of the core positions within the Funds.

Laidlaw International Inc. ("Laidlaw"), a core position for the past two years continued to appreciate as management further enhanced shareholder value by selling off non core business's and recapitalized the balance sheet providing the Company with added flexibility.

In the second half of 2005 the Fund's position in Leitch Technology Corporation ("Leitch") a manufacturer of technical equipment for the television broadcast industry was acquired by a competitor, Harris Corporation for $14.00 per share (all cash). This represented a premium of 128% on our average cost of $6.16 per share.

In early September Goodwood announced the successful outcome to the proxy contest that was being waged to change the management of Cenveo, Inc. ("Cenveo"). Cenveo is one of North America's leading commercial printers, engaged in offset and digital printing, and the printing and manufacturing of envelopes, business forms and labels. This was our second venture with Burton Capital Management, LLC. On September 9th we reached an agreement with Cenveo's incumbent board of directors and Robert Burton, Sr. assumed the position of Chairman and Chief Executive Officer of Cenveo. The share price responded favourably and as such, the Goodwood Fund achieved an unrealized gain of 128.7% on our Cenveo position. As of March 31, 2006 it remains the second largest position within the Funds.

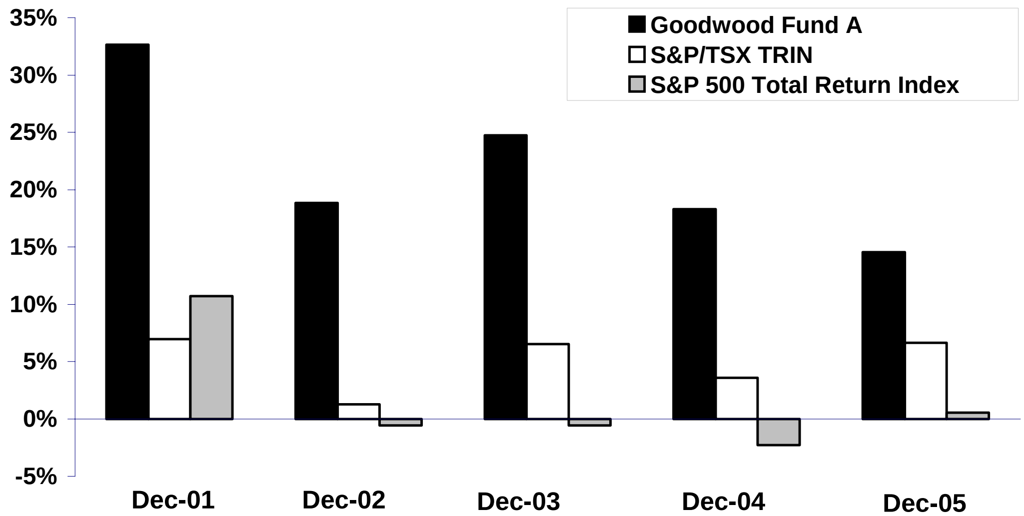
In mid-year 2005, Goodwood began accumulating a position in Dofasco Inc ("DFS") with an average cost of $37.18 per share. Our investment was not based on a high price for steel but on the fact that DFS is a very high quality business and that its capital structure was inefficient. We felt that the significant investments the company had made in its operations (approximately $2.4 billion over the past 11 years), its relatively low levels of leverage, its cash flow stability, and the maturity of the steel industry positioned DFS to begin a phase of returning more capital to shareholders. We believed that DFS could unlock significant shareholder value by moving to a more appropriate capital structure. Our Dofasco interest was not isolated as both Arcelor S.A. ("Arcelor") and ThyssenKrupp AG ("ThyssenKrupp") announced tender offers for DFS with Arcelor being successful at $71 per share.

Noticeably absent from the portfolio as a whole is oil, gas, and gold exposure. Right or wrong, we acknowledge that our low to no commodity exposure is rare for a Canadian based manager and has resulted in the Funds not participating in a sector that was up by over 60% and in fact, contributed to over half the S&P/TSX total return in 2005. While we are by no means "anti-commodity", we are also very cognizant of the significant capital being allocated toward this industry. With oil and gas prices achieving historic record levels, it would be difficult for us to find undiscovered "value" in this sector.

The Goodwood Fund and the Goodwood Capital Fund have enjoyed strong results since their respective inception dates and remain well positioned with attractive opportunities, some discussed in greater detail in the Annual Report. The Goodwood Funds have always been managed with the view to generate above average, long run returns. Our performance success has been achieved by focusing on the discount to intrinsic value of the individual company, which, when combined with additional investments, produces a portfolio of compelling opportunities. Since Goodwood's inception, October 1996, this "value" methodology has provided attractive results, and importantly, we believe the process is repeatable.

We have attached a “five-year rolling graph” that may provide investors with an interesting perspective toward consistent performance. The main theme of a rolling chart is to apply a proper investment time horizon but reduce the effect of a really good or poor year – therefore, limit the concerns of market timing.

Five Year Rolling Chart



Once again, we are grateful for your ongoing support and the confidence of all of our unitholders and encourage you to call directly should you have any questions.

Respectfully submitted,

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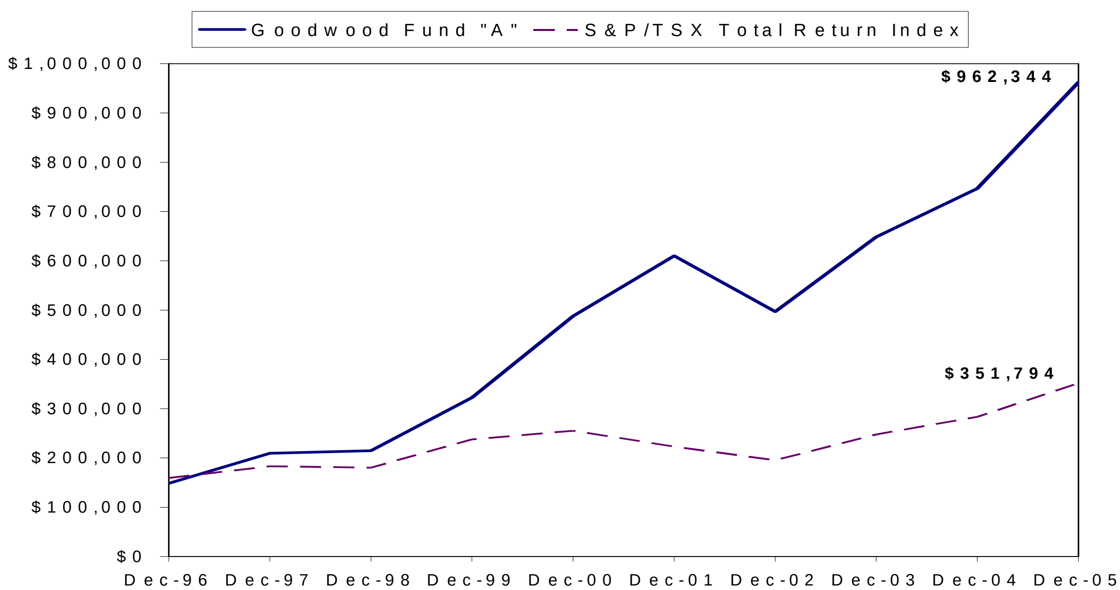
March 31, 2006

Goodwood Fund "A" 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%
December 31, 2005	962,344	28.9%

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



THE GOODWOOD FUND
2005 Annual Report

To the Unitholders of the Goodwood Fund:

For the year ending December 31, 2005, The Goodwood Fund's (the "Fund") "A" unit net asset value ("NAV") per share increased by **28.90%** while the "B" units increased by **26.13%.** The S&P/TSX Composite Total Return Index ("TRIN") increased by 24.13% in the same period.

From October 31, 1996 (the commencement of the Fund's public operations) through to December 31, 2005, the Fund has returned **22.48%** per annum net (after all fees) versus the TRIN's per annum return of 9.75%. [*]

A distribution of $0.05 per "A" unit and $0.02 per "B" unit was paid out on December 31, 2005. The Class "A" post-distribution NAV per unit as at December 31, 2005 amounted to **$32.84**. The Class "B" post-distribution NAV per unit was **$14.57**.

The Fund's 2005 audited financial statements are attached for your review.

During 2005 (based on month end figures), the Fund averaged a **100.39%** 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 **117.05%** invested, composed of **96.96%** long and **20.09%** short, leaving a "net market exposure" (i.e., longs minus shorts as a percentage of the Fund's equity) of **76.87%**. At the other extreme, **73.94%** invested **– 66.50%** long and **7.44%** short for a net market exposure of **59.06%**.

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 later on) 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 informed unitholders. Please see "The Goodwood Philosophy" attached as an appendix after this letter.

All figures in Canadian dollars unless otherwise noted.

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[*] 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.

Punching Above Our Weight Class

Goodwood's 2005 featured a number of notable events which led a good friend and client to make the observation that Goodwood was "punching above its weight class". Maybe we shouldn't be so quick to take it as a compliment but it seems that, for our unitholders, the concept that we are delivering results beyond our relatively small size is a good thing.

Our 2005 highlights included: a further acceleration in the value of our investment in Great Atlantic & Pacific Tea Company, Inc. beyond what we had outlined in last year's Annual Report. Following up on our successful Creo Inc. joint efforts in late 2004, we supported Robert G. Burton, Sr. in his winning proxy contest at U.S. printing company Cenveo Inc. And, we made a significant investment in Dofasco Inc. that yielded substantial profits.

All in all, a year that perhaps deserved our friend's above-noted witticism.

Like Kids in a Candy Store

Long time readers know that Goodwood's bottom-up investment process is all about finding the next potential large weighting winner. The office mood brightens considerably whenever an above average idea comes into focus. As of the writing of this year's Annual Report, while we haven't yet reached the point of being in a position to announce a new major weighting, we can say that we are absolutely bowled over by the number of potential new ideas we are seeing. Like "kids in a candy store" this is both terribly exciting and also daunting. We have to make sure that we can narrow down our list of potential ideas to the very best candidates thus freeing up the required time to perform the level of in-depth analysis that is a hallmark of ours in taking a significant position.

We remain committed to finding Canadian special situations and/or U.S. special situations that have a significant Canadian component (in our opinion, these situations offer the highest likelihood of inefficient pricing). However, we are also spending more time looking at pure U.S. special situations as we are no longer restricted by the former Canadian RRSP foreign content rules. Partly as an indirect result of accounting scandals and increased regulations, there is little research coverage on these names (a good leading indicator of inefficient pricing). There are many U.S. companies that fit our investment philosophy, most of which would be considered small cap in the U.S. but are equivalent to Canadian mid-cap (i.e., market capitalizations in the US$500 million to US$1.5 billion range). In considering Goodwood's capacity to deal with so many new ideas unitholders should reflect on just how much deeper our bench strength is now (it's a lot more than just Cam and I). In fact, we have more analytical "horsepower" per dollar invested today than since the very beginning of the Fund's history. We are truly excited about our ability to capitalize on opportunities going forward.

<u>**How Do You Define “Quality”?**</u>

It’s only natural that, when presented with a flood of potential ideas and a need to prioritize these ideas, a back-to-basics mindset surfaces. In Goodwood’s case, despite the significant amount of press that our activist-agenda-driven ideas attract, the firm’s interest in finding “quality at a valuation discount” (“QVD”) continues. Of course, activist investing and QVD are not necessarily mutually exclusive. It’s just that we would expect, over the long run, to have many more investments in the QVD camp than in the activist investing arena.

The most difficult aspect of QVD investing is defining quality. The discount part is easy as anyone armed with historical data and current financial results can see when a particular security is trading at a cheaper valuation than it usually has. Further, some part of the quality definition can actually be answered quantitatively as the “quality” in question should show up through above-average financial results over some reasonable measurement period (e.g., companies with above-average long term returns on invested capital). But, one needs to understand the qualitative factors underpinning these quantitative results in order to understand whether or not such quantitative excellence will continue.

Our definition of quality would include many notions taken from Charlie Munger (Warren Buffett’s under-the-radar but very impactful and I would say more fascinating partner).

> When he met Buffett, Munger had already formed strong opinions about the chasms between good businesses and bad. He served as a director of an International Harvester dealership in Bakersfield and saw how difficult it was to fix up an intrinsically mediocre business; as an Angeleno, he observed the splendid property of the *Los Angeles Times*; in his head he did not carry a creed about “bargains” that had to be unlearned. So in conversations with Buffett over the years he preached the virtues of good businesses. By 1972, Blue Chip Stamps, a Berkshire affiliate that has since been merged into the parent, was paying three times book value to buy See’s Candies, and the good business era was launched.
> *Forbes*, January 22, 1996

A business that has some defensible franchise is a good starting point. That defensible franchise is often what allows for the generation of above-average financial results. In our current list of new ideas we have a number of companies that, for different reasons, can be said to enjoy defensible franchises.

To the above we would add businesses that are not dependent on the cooperation of an underlying commodity price, businesses that generate good economic returns on invested capital regardless of the general economic cycle (in stark contrast to say, a legacy airline) and businesses that generate a significant amount of free cash flow (free cash flow is what’s left from a Company’s operating cash flow after paying for interest expense, cash taxes, changes in working capital and capital expenditures). Free cash flow is the cash that can accrue to the benefit of the shareholders through share buybacks, dividends and/or debt reduction.

Importantly, for those of us who are aiming for a reasonable fraction of Buffet’s and Munger’s wealth, we should keep in mind Buffet’s oft-repeated observation that he would be a lot poorer if he had stayed focused exclusively on a cheap price rather than “…buying a wonderful business at a moderate price”. Wonderful businesses have a tendency to recover quickly from extraneous shocks and, over the long term, generate superior returns on invested capital. And, though technological advances seem to threaten more and more wonderful business franchises, there are also cases where the technology makes the business even more wonderful.

Our Dofasco Inc. ("Dofasco") Experience

Humble Beginnings lead us to an Unusual Steel Company

Great things can be accomplished, even from the humblest of beginnings. No better example of this truism could be found for this Annual Report than our investment in Dofasco, as its roots reach back to our less-than bright (putting it mildly) investment in Stelco Inc. ("Stelco")(a small position we discussed briefly at last year's Annual Meeting - we're hoping those then in attendance suffer from recurring bouts of amnesia). Stelco's very significant short-term profitability and the presence of like-minded investors (misery loves company!) had us believing that there might be material value in Stelco's equity post its restructuring. But, in the final analysis, nothing could overcome the fact that Stelco personifies all that has been bad about the North American steel industry over the last few decades - no control over selling prices, out-of-control production costs, an older, heavily-unionized work force which burdens the Company with inflexible workplace rules, high wage rates and massive cash contributions to both under-funded pension and health care plans. In short, Stelco was and remains an operational basket case, the proverbial "bad business".

The saving grace of our small investment in Stelco was that it led us to speak with a competitor and friend of ours whom we hold in high regard. In the course of researching Stelco and the steel industry this investor became enthralled with Dofasco's noteworthy virtues which, thankfully, he shared with us. Thus, in a round about way, our Stelco misstep introduced us to Dofasco.

In sharp contrast and, paradoxically, just across the street from Stelco's main works, lie Dofasco's main facility (for the purposes of this discussion we focus on Dofasco's main operations, its Hamilton-based "Steel Operations", and ignore its other businesses). Dofasco represents an anomaly in the steel industry, a company that consistently produces a profit even while other steel companies are bleeding red ink. For example, in 2001 and again in 2003, Stelco's earnings before interest, taxes and depreciation/amortization ("EBITDA") was negative $(32) million and negative $(93) million respectively while Dofasco's Steel Operations generated EBITDA of positive $380 million and $497 million in each of those years.

The most striking thing about Dofasco's financial results to us was the consistency. Between 1995 and 2004 Dofasco's Steel Operations' EBITDA seem to hover around the $500 million plus level with the exceptions of $644 million in 2004 and $362 million in 2001 (2005 came in at a big disappointment relatively speaking, at $291 million – more on that later). This was a time span that encompassed numerous shocks to the North American economy and much spilled blood in North American steel. What accounted for this way-above-average financial performance? What were the qualitative factors that could cause such a schism to develop between these two Hamilton, Ontario neighbours?

There is no one single answer but rather an accumulation of numerous smart management and Board decisions made over the years that had the effect of leaving Dofasco in a far superior competitive position than Stelco. However, four specific factors stand out and probably account for a large part of the complete answer.

To start with, management of Dofasco has a much better relationship with its work force than Stelco. Dofasco's workers are <u>not</u> unionized and the corporate culture provides incentives to become more efficient through significant financial rewards accruing to the workers, such rewards being specifically tied to profitability. The workers at Dofasco's Hamilton facility participate in profitability to the tune of 14% of Hamilton's pre-tax income (or a minimum payment of three times contributions made by members to the Dofasco Employee Savings and Profit Sharing Funds and the Dofasco Employees' Deferred Profit Sharing Plan). In addition, every Dofasco Hamilton employee's compensation has a variable portion of 10% or greater tied to specific performance targets including health and safety, customer service, revenue, cost and return on capital employed. In 2004 these plans resulted in $150 million of payments made to Hamilton employees. As well, Dofasco spends more than $25 million annually on training, development and apprenticeship programs for its employees. This upside-focused, "we're all in it together" philosophy encourages work place productivity and flexibility resulting in a more manageable and efficient cost structure.

Secondly, Dofasco's Hamilton operations have been designed to allow for as much control over the manufacturing process as possible. The Hamilton works actually employ three different methodologies of producing steel all under the same roof - traditional oxygen blast furnace, electric arc furnace and refinement of slabs purchased from third party sources. This flexibility allows Dofasco operating management to maximize manufacturing efficiency and respond to differing economic conditions by converting a portion of its manufacturing costs from fixed to variable.

Thirdly, early in the 1990's Dofasco began moving itself away from being just another commodity steel producer to a specialty, high-value-added steel producer. This required massive and consistent capital investment in "downstream" finishing equipment and, to a lesser degree, in research and development. In the eleven years ending 2005, Dofasco has spent approximately $2.4 billion on its state-of-the-art, world-class facilities. The effect of this strategic move was that Dofasco ended up with a large percentage of its total sales under multi-year contract to customers who pay appreciably more per tonne to get this higher quality steel (the applications for this kind of steel would include exterior auto parts where blemished steel simply would not be acceptable).

Finally, Dofasco's senior management had the presence of mind to diversify its heavy auto exposure away from just the U.S. big three and into the "transplant" business (i.e., the various Asian and European auto manufacturers that have set up plants in North America). It took years of preparation and concerted effort but has paid off handsomely in the last few years as the Toyota's and Honda's gain more and more North American market share.

Thus, Dofasco, building upon its superb employee relations and productivity, manufacturing flexibility, focus on value-added product and diversified client relationships, managed to distance itself from the unpredictability of commodity steel and the infamously volatile "spot price". As a result, Dofasco's returns on capital invested (arguably the best single measure of a Company's results) have not only outdistanced other steel companies' returns but have also allowed for an unusual level of consistency (something investors will pay more for).

One Person's Treasure is another Person's Trash

While Dofasco's return on capital invested was clearly good from a steel industry point of view, for an investor who can move capital between industries, that return was not-so-good. Between 1995 and 2005 Dofasco's return on capital employed ("ROCE") has averaged just 8.4% (below the Company's own targeted cost of capital over a cycle of 11%). And, in keeping with its conservative financial management Dofasco's balance sheet had become much underutilized - depressing returns available for the equity owners and increasing their annual tax bill (i.e., by not prudently maximizing the amount of tax-deductible debt). Over the 11 years ending in December of 2005, Dofasco has paid $1.07 billion of taxes. Dofasco's overly conservative capital structure and focus on reinvesting in itself (despite the relatively low return on capital employed) was inhibiting the investment returns possible for its shareholders.

Through speaking with industry analysts and executives we also knew that Dofasco, should it ever become available for sale, would attract multiple potential buyers given the Company's competitive position and strategic importance as a premier, North American steel producer.

We began exploring and planning for the possibility that Goodwood, on its own and with the help of other like-minded investors, could bring enough pressure to bear to force Dofasco to unlock some of this latent value through large dividends and/or share buybacks, spinning off of operations (e.g., that remarkable consistency in profitability in Dofasco's Steel Operations argued for the feasibility of a highly-valued income trust) and possibly an outright sale of the Company.

We had only invested approximately 2% of the Fund's equity in Dofasco shares and were exploring our options when news broke that the Company was buying control of Quebec Cartier Mining Company ("QCM"). This extremely-earnings-accretive acquisition caught the investment community by surprise but, as we had already developed a good knowledge of Dofasco, we were able to react quickly and in very short order built the Fund's position up to approximately a 12% weighting.

Buying the vast majority of QCM (Dofasco now owned 98.7%) gave the Company a built-in hedge against ever-increasing iron ore prices, a major headache lately for blast furnace steel manufacturers as iron ore is an important input cost and has increased in price materially over the last few years. In fact, Dofasco was now "net long" iron ore as QCM's production much exceeded Dofasco's needs plus Dofasco owns 28.6% of Wabush Resources Inc., another iron ore producer. From a stock market point of view, the summer of 2005 was a great time to go net long iron ore, especially if such was accomplished at a really insignificant acquisition multiple - we estimate that Dofasco acquired control of QCM for approximately 2.5X 2005 earnings! Dofasco was now our largest position and represented only the fourth position in the almost 10 year history of the Fund where we had acquired such a large weighting.

And, our potential activist agenda was firming up. We believed that our value-unlocking plan could yield a target price of as much as $100 per share much more than the Fund's average cost of approximately $38.

Step 1 in our agenda was radical and, consequently, would not have been realistically achievable unless we managed to work with other Dofasco shareholders and apply significant pressure to the Dofasco Board. This step would have been so unpalatable to management and the Board that we speculated that they would favour an outright sale of the Company rather than allow such a financial step to occur. We would have pushed for Dofasco to cancel its tax-inefficient $100 million a year common share dividend program and replace that obligation with $100 million per year of interest obligation (as an aside, we speculated that the nature of the Steel Operations' variable compensation program, calculated on pre-tax but not pre-interest levels and, the small stock ownership level of management and the Board, collectively approximately 0.2% of Dofasco's outstanding stock, left little incentive for optimization of the capital structure in favour of the common shareholder). At an assumed 8% interest rate, this would have translated into a $1.25 billion loan (ignoring the fact that, at an assumed 32.5% tax rate $100 million in dividends, which is paid out of after-tax dollars, is equivalent to $148 million of pre-tax dollars). Our idea was to use this loan to execute a major share buyback. For example, at an assumed buyback price of say, $47.50 (a premium to the then trading price), Dofasco's 77.1 million shares outstanding would have been shrunk to 50.8 million.

Step 2 would be to convert QCM into an income trust and spin off approximately 80% to Dofasco's shareholders (Labrador Iron Ore Royalty Income Trust and Fording Canadian Coal Trust were a couple of highly-valued comparables that we used to benchmark potential valuations for QCM on its own). The 20% retained by Dofasco would allow it to remain fully hedged against iron ore prices. In fact, Dofasco management had announced that they would monetize the value of QCM through creating and listing QCM securities eventually settling on an income trust structure. But, while a spin out to Dofasco shareholders would give all the "excess" QCM value to Dofasco shareholders (which Goodwood favoured), Dofasco management favored an initial public offering of QCM ("IPO") which would allow Dofasco to decide what to do with the proceeds generated by the offering (possibly using the proceeds to make an acquisition of more steel assets – an idea we were not fans of).

We estimated that 80% of QCM, structured as an income trust, net of assumed capital gains tax on sale (incurred upon rolling QCM from Dofasco into the income trust), at an 85% payout rate on 2006 estimated distributable cash flow and at a market valuation of a 15% yield, would have a value of approximately $25 per the post-buyback shares outstanding.

Interestingly, it may have been more financially rewarding to reverse the order of steps 1 and 2 above. If 80% of QCM was spun off to Dofasco shareholders then the trading price of Dofasco stock would drop by the perceived value of what was spun out. This would have created a potentially much lower base price from which to calculate the major share buyback price and thus the loan amount required would have dropped considerably. Either approach though would create substantial value for those shareholders who did not tender to the buyback.

In the third step, we envisioned Dofasco selling its half interest in Gallatin Steel ("Gallatin") – a low-cost minimill in Kentucky. Gallatin appeared to us to be non-core and we feared that Dofasco would take the proceeds of a QCM IPO and attempt to buy the other half of Gallatin. Our conservative estimate of the value of Dofasco's share of was approximately $500 million (or $9.84 per share after our assumed share buyback).

In the eyes of Dofasco management and Board, our final step probably would have been viewed as being as extreme as the major share buyback. That being to convert Dofasco's Steel Operations into an income trust. The timing of such was opportune too as the Steel operations would be completing a major capital expenditure program in 2007 (the finishing division improvement program ("FDIP")) thus lessening future years' capital expenditure requirements and this structure would further minimize Dofasco's significant tax payments. We felt that the Steel Operations' historically consistent profitability and free cash flow would allow for an income trust. At our 2007 EBITDA assumption of $705 million (which included anticipated benefits of the FDIP), a conservative maintenance capital expenditure forecast of $135 million (versus management's guidance of $100 million) and, interest cost of $140 million (including interest on the share buyback loan) we foresaw distributable cash flow of $430 million. Assuming that only 85% of such cash flow would be distributed to Trust unitholders and assuming the Trust would be valued at an 11% yield, we envisioned a value of $65.41 per Dofasco share (again, calculated on the post buyback number of shares outstanding).

In summary, post a $47.50, $1.25 billion share buyback – we could see $100 of Dofasco share value realizable over a 2 year timeframe.

A Step Back

Alas, all was not to be. Goodwood had become fully-invested in Dofasco and we had found a deep-pocketed, similar-minded partner to buy stock with us and co-pursue this activist agenda. However, two developments interfered, having the effect, given our inherent conservatism, of making us sell down the Dofasco position to about half our peak position.

The first development was that Dofasco announced on September 14th, 2005 that its third quarter earnings (the quarter ending September 30, 2005) would be well below analysts' then forecasts. In fact, the Hamilton Steel Operations were expected to post a small loss! We had gotten to know Dofasco's history thoroughly and so we knew that this would be only the third time in at least the last 10 years that Steel Operations' quarterly EBITDA would be below $100 million (the other occasions being the fourth quarter of 2000 and the first quarter of 2001). This was not normal for Dofasco's Steel Operations. This gave us great pause.

The causes were varied but included higher electricity prices, higher natural gas prices, a stronger Canadian dollar (much of Dofasco's costs are in Canadian dollars and much of its revenues in US dollars), higher iron ore and coal prices (Dofasco's net long position in iron ore showed up in its QCM division thus not directly aiding the Steel Operations' results), weaker spot prices (for that portion of Dofasco's production that was sold into the spot market), significantly higher prices for purchased slabs that were then feeding their way through the system and, production declines due to plant interruptions. Compounding the unexpectedly weak third quarter was guidance given in the actual third quarter release that the upcoming fourth quarter would also show a paucity of profitability in Steel Operations. We feared that this was potentially more than just a one or two quarter blip, that maybe the new steel operating environment would no longer be as fruitful to Dofasco's business model.

The second development was that Ralph Goodale, the then Minister of Finance for the Canadian Government, shocked Bay Street with his September announcement that he had directed the Canada Customs and Revenue Agency to no longer grant advance tax rulings in regards to companies seeking to convert to an income trust structure. This vague statement created many questions but weighed heavily on the entire income trust space. For Goodwood, with the upside in our Dofasco position partially dependent on the viability of income trusts (both for QCM and, in the more distant future, for Dofasco's Steel Operations) any uncertainty was not good.

Thus, our prudent nature led us to cut our Dofasco position in half. We had made a good profit on the position, felt the Company continued to hold strategic value but, our upside was now not as clear. And, it looked like we might have the opportunity to buy the stock later for a cheaper price.

The Final Act

It's difficult to avoid the feeling that the final act of our Dofasco experience was unfair to us and other Dofasco shareholders. Beginning in May, 2005 and unbeknownst to us and other shareholders, Dofasco's Board and management were the recipients of multiple takeover offers by Arcelor S.A, the world's second largest steel company and, initially, Nucor Corporation, the world's most successful minimill operator.

If management and the Board had taken the point of view that Dofasco shareholders ought to be appraised of developments as material as takeover discussions regarding their company, whether or not such takeover discussions were desired by them, then Goodwood would not have sold any of its position – knowing full well that, in a takeover, Dofasco had value substantially beyond the valuation predicated on short-term fundamentals and Ralph Goodale's whimsical announcements. Unfortunately, the Board of Dofasco did not believe that the ever-increasing-in-value Arcelor-driven offers were important enough to share with shareholders. Perhaps if the Board and management owned more than just 0.2% of the stock they might have had a different point of view. The Board of Dofasco took the legally-justified (by the technical letter of the law) but lacking in common sense stance that, if they determined an offer was inadequate (even though the offer was materially above the then share price), that there was no offer and hence no requirement to make a public announcement. Somewhat akin to a child closing his or her eyes as a way of making something unpalatable disappear. This lack of disclosure effectively cost the Fund millions in lost opportunity. We're happy that beginning in 2006 the law in Canada has changed making it possible for disgruntled shareholders of a public company to sue for omissions in disclosure. It's unfortunate that the law wasn't in place in 2005.

Our simmering bitterness is exacerbated by the 456,600 options the Board granted to management on June 23, 2005. These options featured a strike price set off the then trading price of $37.75 per share which was well below Dofasco's ultimate takeover price and well below what the stock would have been trading for had disclosure been made. Arcelor and Nucor first approached Dofasco with a takeover offer on May 27, 2005, an offer that can rightfully be said to have been inadequate. But on June 21, 2005 they followed up with a much improved offer - $46 cash plus the value of the newly acquired portion of QCM – we think this package was easily worth $51 per Dofasco share, probably more. Two days later the new options were granted to management, their strike prices benefiting from being well below where the stock would have been trading had disclosure of the much improved June 21st offer been made.

The combination of disclosing weak operating results and not disclosing the takeover offers seems to be an assault aimed squarely at Dofasco shareholder's best interests.

When Arcelor realized that Dofasco's Board would never willingly entertain their takeover offer, they logically took their interest directly to the Dofasco shareholders. On November 23, 2005 Arcelor's initial public offer was $56 all cash. By January 16, 2006 and after competing offers made by Dofasco's white knight, ThyssenKrupp, Arcelor made the winning bid of $71 cash.

In the final analysis, our Dofasco experience was a winning experience. It was well thought out and executed, we understood the Company well and, the profits were significant. However, clearly it would have been an even more resounding win if a more shareholder-friendly approach to disclosure had been taken by the Dofasco Board. As well, it's a shame that we never had the opportunity to put our multi-step activist agenda to work.

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.

Quantifying the Upside – Discount to Intrinsic Value

We estimate our current discount to intrinsic value to be approximately 17% suggesting a potential upside in the portfolio of roughly 20%, reflecting a current, relatively high cash position. We would not read too much into the Fund's current cash position as this statistic can change very quickly when and if we decide the time has come to increase our weightings in some of our 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. Also, there are a number of already-in-place small to mid-size weightings that, under the right conditions, we would be willing to take materially higher – e.g., CanWest Global Communications Corporation, ShawCor Limited and Toll Brothers Inc.

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.

<u>Great Atlantic & Pacific Tea Company, Inc. ("GAP"):</u>
In last year's Annual Report we told you that "…selling GAP Canada combined with improved U.S. operations could take the stock close to or even above the US$25 level." Subsequent events proved that we were, once again, too conservative as GAP stock rose to as high as US$35.90. The extra upside came from GAP selling its Canadian business for a better price than we were expecting. In last year's Annual Report we told you that "…GAP Canada could fetch as much as US$26 per GAP share," or about US$1 billion. In fact, Metro Inc. ("Metro") ending up paying the equivalent of Cdn. $1.7 billion (Cdn. $1.2 billion in cash and Cdn. $0.5 billion in Metro class A, subordinate voting shares).

GAP remains our biggest weighting (approximately 10.8% of the Fund's equity) despite it not trading for an appreciable discount to our estimate of intrinsic value. We continue to believe that GAP and its New York/New Jersey competitor, Pathmark Stores, Inc. ("Pathmark"), have such a strong economic imperative to merge their operations (a possibility we brought up in last year's Annual Report) that it is just a matter of time. We believe that GAP stock, currently trading for US$34.93 could be worth US$45 plus in such a scenario. Let's hope we're too conservative again.

<u>Cenveo Inc. ("Cenveo"):</u>
Our Bob Burton ("Bob")-inspired Cenveo position was taken on during the spring of 2005. Like those old Victor Kiam, Remington shaver ads, you know - "I like the shaver so much, I bought the Company"- we like Bob so much, we bought part of Cenveo. In seriousness, when Bob approached us about supporting him in his Cenveo investment, we were thrilled. We not only bought stock and filed a Schedule 13D alongside him but we also agreed to add a Goodwood representative to the Cenveo Board of Directors. While that makes Goodwood an insider and thus restricts our ability to trade the stock, we felt that our longer term investment orientation and our comfort in supporting Bob and his people more than compensated.

Cenveo operates in Bob's sweet spot – commercial printing. And, it was clearly an inefficiently-run business as its margins were much lower than comparable printing companies. For the year ending December 31, 2004, Cenveo's adjusted EBIT margins (i.e., earnings before interest and taxes adjusted for restructuring, impairment and sundry other charges and divided by sales) were 4.5%. The same figure for Consolidated Graphics, RR Donnelley and Cadmus were 7.0%, 9.0% and 7.8% respectively. In effect, there would be plenty of low-hanging, cost-cutting fruit for Bob to pick. Since the September 9, 2005 agreement to end the proxy contest and hand the Chairman and Chief Executive Officer title to Bob, he has already moved to address Cenveo's costs. The fourth quarter of 2005 (quarter ended December 31, 2005) showed a 50% improvement in adjusted EBITDA from core domestic operations versus the year ago quarter, partially reflecting the US$100 million of cost savings that Bob has targeted.

As is Bob's modus operandi, he began by putting his money where his thoughts were and bought 2.56 million shares of Cenveo (or approximately 5.3% of the outstanding). Goodwood's position was approximately 1.46 million shares (or roughly 3% of the outstanding). With the March 31, 2006 closing price of US$16.58, the Fund now has a paper profit of 157% (which would be even higher if the Canadian dollar hadn't strengthened during our holding period). Both Goodwood and Bob have bought more stock as recently as this month and Bob's beneficial ownership is now over 3.1 million shares (or over US$51 million at current prices).

We're pretty excited about what Bob may be able to add to the Cenveo story through selective acquisitions. And, the wherewithal to make those acquisitions has been bolstered with the recently-completed IPO as an income trust of Cenveo's dominant Canadian envelope business, Supremex Income Fund (yes, the income trust universe has survived Ralph Goodale's scare). This raised US$190 million in proceeds for Cenveo (net of all costs), while still retaining a 36.5% interest worth approximately Cdn. $114 million at the IPO price (figures are before factoring in the potential exercise of the underwriters' over-allotment option).

I'm sure you'll agree that, if Bob could be parachuted in to manage the entire Dow Jones Industrial Average, there would be nothing average about its subsequent performance!

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. As well, Cam, I and others in the firm continue to increase our collective investment in the Fund. We've been eating our own cooking for a while but now the portion sizes are getting pretty big.

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

Respectfully submitted,

Peter Puccetti, CFA
Chief Investment Officer
Goodwood Inc.

March 31, 2006

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 9 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 2005 was **72.9%**. 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
2005 Annual Report

To the Unitholders of The Goodwood Capital Fund:

For the year ending December 31, 2005, The Goodwood Capital Fund (the "Capital Fund") increased **29.80%**. The S&P/TSX Composite Total Return Index ("TRIN") increased 24.13% in the same period. The S&P 500 Index gained 4.91%.

From December 23, 1999 (the commencement of the Fund's operations) through to December 31, 2005, the Capital Fund has returned **13.86%** per annum net versus the TRIN's per annum increase of 6.84%. *

A distribution of $0.07 per unit was paid for 2005. The Capital Fund’s post-distribution NAV per unit as at December 31, 2005 amounted to **$18.65.**

The Capital Fund's 2005 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 Management Report of Fund Performance and the Annual Report of The Goodwood Fund, both of which are 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 31, 2006

* 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.

Advisory Board

Mr. Robert Curl, CA
Mr. Robert Luba, CA
Mr. Cameron MacDonald, CFA
Mr. Peter Puccetti, CFA

	Goodwood Fund	**Goodwood Capital Fund**
FundSERV Code:	GWD022	GWD001
Valuation / Liquidity	Weekly	Weekly
Fund Type:	North American Long/Short Fund	North American Equity Fund
Launch Date:	October, 1996	December, 1999
RRSP Eligible:	Yes	Yes
Custodian:	National Bank Financial Corp.	CIBC Mellon Global Securities Services
Fund Accounting:	Citigroup Fund Services Canada	Citigroup Fund Services Canada
Auditor:	KPMG, LLP	Feldman & Associates, LLP
Trustee:	Computershare Trust Co.	Computershare Trust Co.
Legal Counsel:	Borden Ladner Gervais, LLP	Borden Ladner Gervais, LLP

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