

# **MANAGEMENT REPORT OF FUND PERFORMANCE**

## **December 31, 2009**

### **CHOU BOND FUND**

This annual management report of fund performance contains financial highlights; it does not contain the complete financial statements of the Fund. You can obtain on request at no cost a copy of the interim or annual financial statements by calling Toll-free: 1-888-357-5070, or by writing to us at 110 Sheppard Ave. East, Suite 301, Box 18, Toronto, Ontario M2N 6Y8. The Fund's complete financial statements are posted on our website at [www.choufunds.com](http://www.choufunds.com) and SEDAR at [www.sedar.com](http://www.sedar.com).

Unitholders may also contact us as above to request a copy of the Fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

This document may contain forward-looking statements relating to anticipated future events, results, circumstances, performance, or expectations that are not historical facts but instead represent our beliefs regarding future events. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. There is significant risk that predictions and other forward-looking statements will not prove to be accurate. We caution readers of this document not to place undue reliance on our forward-looking statements as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed or implied in the forward-looking statements.

Actual results may differ materially from management expectations as projected in such forward-looking statements for a variety of reasons including, but not limited to, market and general economic conditions, interest rates, regulatory and statutory developments, the effects of competition in the geographic and business areas in which the Fund may invest in, and the risks detailed from time to time in the Fund's Simplified Prospectus. We caution that the foregoing list of factors is not exhaustive, and that when relying on forward-looking statements to make decisions with respect to investing in the Fund, investors and others should carefully consider these factors, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. Due to the potential impact of these factors, the family of Chou Funds does not undertake, and specifically disclaims, any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by applicable law.

Chou Associates Management Inc. ("the Manager") manages the overall business of the Fund, including selection of the securities in the Fund's portfolio and promoting sales of the Fund's units. For the purposes of this document, the terms Chou Associates Management Inc. and "the Manager" are interchangeable. Full contact information is located at the end of this report.

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## Management Discussion of Fund Performance

### Investment Objective and Strategies

The Fund's objective is to provide conservation of principal and income production with capital appreciation as a secondary consideration. The Fund invests primarily in Canadian and US bonds. These bonds include, but are not limited to, Government of Canada, provincial, municipal and corporate issues, including convertibles and high yield bonds. Investments may be made in bonds outside of Canada and the U.S.

### Risk

The risks of investing in the Fund are disclosed in the Fund's most recently filed Simplified Prospectus.

For the reporting year, there were no material changes that affected the Fund's overall level of risk.

### Results of Operations

For the year ended December 31, 2009, Chou Bond Fund (the "Fund") returned 42.5% for Series A units and 42.6% for Series F units while Citigroup WGBI All Maturities Index was down 11.5% and Barclays U.S. Corporate High Yield Index returned 34.4% in Canadian dollars. In \$US, the Fund returned 65.9% for Series A units and 66.1% for Series F units while Citigroup WGBI All Maturities Index returned 2.6% and Barclays U.S. Corporate High Yield Index returned 58.2%.

The historically high spread between U.S. corporate debt and U.S. treasuries narrowed in 2009 and was a major reason for the gain in the Chou Bond Fund. Three years ago, the spread between U.S. corporate high-yield debt and U.S. treasuries was 311 basis points; at December 31, 2009 it was 657 basis points, down from its December 2008 peak of 1,900 basis points. Three years ago, the spread between U.S. investment grade bonds and U.S. treasuries was about 85 basis points; at December 31, 2009 it was 162 basis points, down from its December 2008 peak of 592 basis points. (Source: JP Morgan)

The gains on forward currency contracts helped minimize the negative impact the stronger Canadian dollar had on the results of the Fund. The Fund gained US \$5,631,385 on the currency contract that expired on June 10, 2009. On December 31, 2008, one U.S. dollar was worth approximately \$1.22 Canadian, whereas one year later, on December 31, 2009, one U.S. dollar was worth approximately \$1.05 Canadian.

Positive contributors to the Fund's performance were debt securities of Primus Telecommunications, Pinnacle Airlines, Goldman Sachs Capital, Mannkind Corporation and James River Coal.

We suffered most declines in the debt securities of Abitibi-Consolidated, CanWest MediaWorks LP and Taiga Building Products.

The Fund added debt securities of the following companies to the portfolio: International Coal Group, Wells Fargo Capital XIII, French Lick Resorts & Casino and SFK Pulp Fund.

The Fund sold debt securities of the following companies: Nortel Networks Limited, JetBlue Airways Corporation, Interstate Bakeries and Catalyst Paper. The Fund also sold preferred shares of Doral Financial and common shares of Tembec Inc.

We tendered 190,000 Global Crossing UK Finance 10.75% debt maturing in 2014 but only 5,000 were accepted at par by the company.

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We also exchanged 4,781,000 Primus Telecommunications 14.25% debt maturing in 2013 for 3,409,158 new 14.25% debt maturing in 2013 and 132,532 common shares.

The value of Hollinger Inc. 11.875% and 12.875% debt maturing in 2011 was written down to zero (0) because of uncertainties with the timing of collection (claims) and the amount to be collected.

Net redemptions for the year were approximately \$3,708,000. Our average month-end cash position was 21.7% of net assets.

### **Recent Developments**

#### ***Amendments to Section 3862, Financial Instruments - Disclosures***

In June 2009, the Canadian Accounting Standards Board incorporated the recent amendments to International Financial Reporting Standards 7, Financial Instruments: Disclosures, into CICA Handbook Section 3862, Financial Instruments – Disclosures. The amendments expand the disclosures required in respect of fair value measurements recognized in the financial statements. For the purpose of these expanded disclosures, a three-level hierarchy has been introduced as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- Level 3: Inputs for the asset or liability that are not based on observable market data. Additional quantitative disclosures are required for Level 3 securities.

#### ***Future Accounting Standards***

The Canadian Accounting Standards Board has confirmed its plan to adopt all International Financial Reporting Standards (“IFRS”), as published by the International Accounting Standards Board, on or by January 1, 2011. Accordingly, the Fund will adopt IFRS for its fiscal period beginning January 1, 2011. The Fund will issue its financial results for the semi-annual period ending June 30, 2011 on an IFRS basis, which will include comparative data on an IFRS basis, and an opening statement of net assets as at January 1, 2011.

The Manager has commenced planning for the changeover to IFRS. Elements of that plan include identifying key differences between Canadian GAAP and IFRS and evaluating the likely impacts on business activities.

Based on the Manager’s current evaluation of the differences between Canadian GAAP and IFRS, the adoption of IFRS is not expected to have a significant impact on the calculation of NAV per security. IFRS is expected to affect the overall presentation of financial statements and result in additional disclosure in the accompanying notes. However, our current assessment may change if new standards are issued or if interpretations of existing standards are revised.

#### **Independent Review Committee**

Under the provisions of National Instrument 81-107 Independent Review Committee for Investment Funds (“NI 81-107”), which came into force on November 1, 2006, it is required that all publicly offered investment funds, such as the Fund, establish an independent review committee (“IRC”) to which the Manager must refer for review all conflict of interest matters. This instrument further mandates that the IRC be composed of at least three independent members and that they report at least annually to the Manager and shareholders in respect of the IRC’s duties.

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The Manager has established an IRC as required by NI 81-107. The members of the IRC are Sanford Borins, Bruce Kerr and Joe Tortolano.

The 2009 IRC Annual Report is available on our website [www.choufunds.com](http://www.choufunds.com).

### **Related Party Transactions**

The Manager manages the overall business of the Fund, including selection of the securities in the Fund's portfolio, and promoting sales of the Fund's units.

The Manager is also the trustee of the Fund. When you invest in the Fund, you are buying units of a trust. The trustee holds actual title to the property in the Fund - the cash and portfolio securities - on your behalf.

Citibank Canada is the custodian of the Fund and has physical custody of the securities in the Fund's portfolio.

Citigroup Fund Services Canada is the recordkeeper of the Fund. The recordkeeper provides or arranges for the maintenance of all unitholder records, the processing of purchases and redemption orders, the processing of distributions, and the issuance of investor account statements and annual tax reporting information for the Fund.

There were no transactions with related parties except in the capacities set out above.

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## Financial Highlights

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the year ended December 31, 2009 and prior years as applicable.

### The Fund's Net Assets per Unit <sup>(1)</sup> Series A

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u><sup>(4)</sup>2005</u>
<b>Net assets, beginning of year</b>	\$ 6.34	\$ 11.45	\$ 12.20	\$ 10.34	\$ 10.00
<b>Increase (decrease) from operations</b>					
Total revenue	\$ 0.53	\$ 0.95	\$ 0.67	\$ 0.73	\$ 0.06
Total expenses	(0.11)	(0.06)	(0.16)	(0.05)	(0.01)
Realized gains (losses) for the year	(1.15)	(1.74)	(0.53)	0.18	0
Unrealized gains (losses) for the year	3.40	(3.44)	(0.65)	1.14	0.26
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	\$ 2.67	\$ (4.29)	\$ (0.67)	\$ 2.00	\$ 0.31
<b>Distributions</b>					
From income (excluding dividends)	\$ 0.52	\$ 0.80	\$ 0.43	\$ 0.34	\$ 0.05
From dividends	0	0	0	0	0
From capital gains	0	0	0	0.06	0
Return of capital	0	0	0	0	0
<b>Total annual distributions <sup>(3)</sup></b>	\$ 0.52	\$ 0.80	\$ 0.43	\$ 0.40	\$ 0.05
<b>Net assets at December 31 of year shown</b>	\$ 8.50	\$ 6.34	\$ 11.45	\$ 12.21	\$ 10.34
<b>Net assets at December 31 of year shown in \$US</b>	\$ 8.12	\$ 5.20	\$ 11.58	\$ 10.48	\$ 8.87

### Ratios and Supplemental Data Series A

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Total net asset value (000's) <sup>(5)</sup>	\$ 57,878	\$ 45,347	\$ 76,295	\$ 31,776	\$ 2,933
Number of units outstanding <sup>(5)</sup>	6,801,007	7,153,342	6,660,305	2,602,344	283,682
Management expense ratio <sup>(6)</sup>	1.39%	0.50%	1.34%	0.40%	0.16%
Management expense ratio before waivers or absorptions	1.39%	1.36%	1.34%	1.47%	0.48%
Trading expense ratio <sup>(7)</sup>	0.01%	0.00%	0.02%	0.04%	0%
Portfolio turnover rate <sup>(8)</sup>	61.00%	46.02%	36.52%	5.30%	0%
Net asset value per unit	\$ 8.51	\$ 6.34	\$ 11.46	\$ 12.21	\$ 10.34

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## The Fund's Net Assets per Unit <sup>(1)</sup> Series F

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>(4)2005</u>
<b>Net assets, beginning of year</b>	\$ 6.31	\$ 11.45	\$ 12.21	\$ 10.34	\$ 10.00
<b>Increase (decrease) from operations</b>					
Total revenue	\$ 0.50	\$ 0.95	\$ 0.67	\$ 0.89	\$ 0.06
Total expenses	(0.10)	(0.05)	(0.14)	(0.03)	(0.01)
Realized gains (losses) for the year	(0.85)	(1.71)	(0.52)	0.21	0
Unrealized gains (losses) for the year	3.18	(3.49)	(0.64)	1.05	0.34
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	\$ 2.73	\$ (4.30)	\$ (0.63)	\$ 2.12	\$ 0.39
<b>Distributions</b>					
From income (excluding dividends)	\$ 0.50	\$ 0.82	\$ 0.45	\$ 0.35	\$ 0.05
From dividends	0	0	0	0	0
From capital gains	0	0	0	0.06	0
Return of capital	0	0	0	0	0
<b>Total annual distributions <sup>(3)</sup></b>	\$ 0.50	\$ 0.82	\$ 0.45	\$ 0.41	\$ 0.05
<b>Net assets at December 31 of year shown</b>	\$ 8.49	\$ 6.31	\$ 11.45	\$ 12.22	\$ 10.34
<b>Net assets at December 31 of year shown in \$US</b>	\$ 8.11	\$ 5.18	\$ 11.58	\$ 10.48	\$ 8.87

## Ratios and Supplemental Data Series F

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Total net asset value (000's) <sup>(5)</sup>	\$ 13,236	\$ 7,388	\$ 10,610	\$ 4,595	\$ 23
Number of units outstanding <sup>(5)</sup>	1,556,801	1,170,405	925,972	376,179	2,186
Management expense ratio <sup>(6)</sup>	1.23%	0.45%	1.18%	0.24%	0.12%
Management expense ratio before waivers or absorptions	1.23%	1.19%	1.18%	1.31%	0.43%
Trading expense ratio <sup>(7)</sup>	0.01%	0.00%	0.02%	0.04%	0%
Portfolio turnover rate <sup>(8)</sup>	61.00%	46.02%	36.52%	5.30%	0%
Net asset value per unit	\$ 8.50	\$ 6.31	\$ 11.46	\$ 12.22	\$ 10.34

<sup>(1)</sup> This information is derived from the Fund's audited annual financial statements. The net assets per unit presented in the financial statements differs from the net asset value calculated for fund pricing purposes. An explanation of these differences can be found in the notes to the financial statements.

<sup>(2)</sup> Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period.

<sup>(3)</sup> Distributions were reinvested in additional units of the Fund or paid in cash upon request.

<sup>(4)</sup> Series A numbers for 2005 are for the period from September 16 to December 31. Series F numbers for 2005 are for the period from September 30 to December 31.

<sup>(5)</sup> This information is provided as at December 31 of the year end shown and is rounded to the nearest thousand.

<sup>(6)</sup> Management expense ratio is based on total expenses (excluding commissions and other portfolio transaction costs) for the stated period and is expressed as an annualized percentage of weekly average net asset value during the period. The 2005 management expense ratio is for the period from September 16 to December 31 for Series A and September 30 to December 31 for Series F.

<sup>(7)</sup> The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of weekly average net asset value during the period.

<sup>(8)</sup> The Fund's portfolio turnover rate indicates how actively the Fund's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

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## Management Fees

The Manager manages the Fund. The Manager is entitled to an investment management fee calculated as a percentage of the market value of the net assets equal to 0.0958% per month for Series A units and 0.083% per month for Series F units. The Manager pays 15 basis points per year trailer fees to dealers out of management fees for Series A units. There is no trailer fee paid out for Series F units.

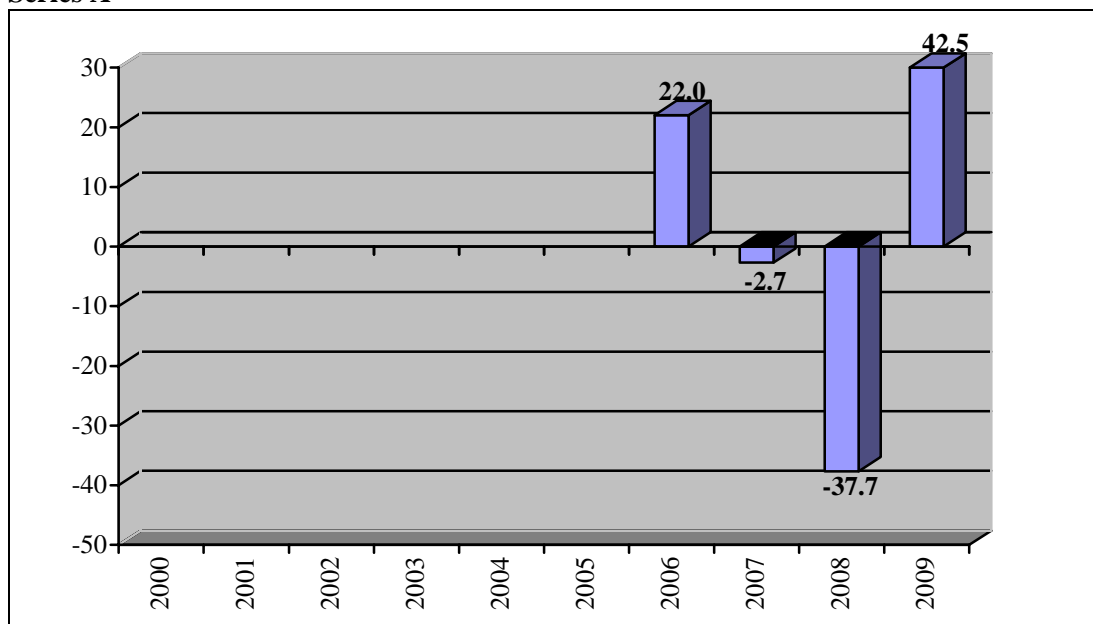
## Past Performance

The following charts and tables show the Fund's past performance. Rates of return are historical total returns including changes in unit prices and assume the reinvestment of all distributions. These returns do not take into account any sales charges, redemption fees, other optional expenses or income taxes that you have to pay and which could reduce these returns. The Fund's past performance does not necessarily indicate future performance.

## Year-by-Year Returns

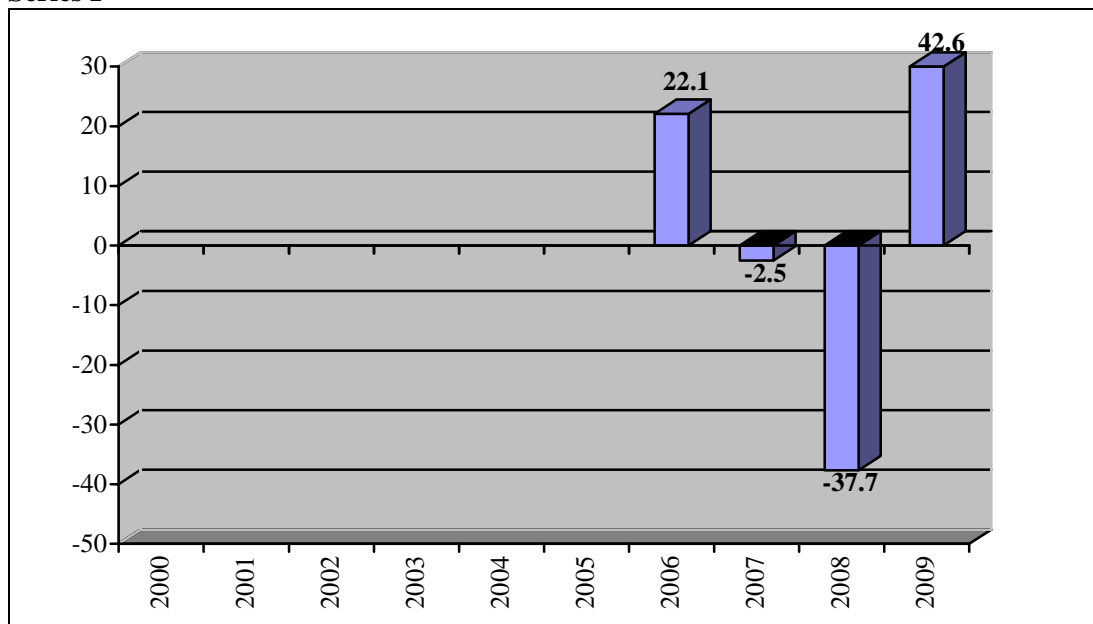
The bar charts show the annual performance for Series A and Series F units of the Fund for each of the years shown. Each chart shows, in percentage terms, how an investment on January 1 would have increased or decreased by December 31 for each of the years, and how the performance varied from year to year.

### Series A



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## Series F



## Annual Compound Returns

The following tables <sup>(1)</sup> show the annual compound total return for Series A and Series F units of Chou Bond Fund. Below each return are benchmarks for comparison.

### Series A

December 31, 2009	Past Year	Past 3 Years	Since Inception
Bond Fund	42.5%	-4.8%	2.1%
Citigroup WGBI All Maturities (\$CAN)	-11.5%	4.5%	3.5%
Barclays U.S. Corporate High Yield Index (\$CAN)	34.4%	2.4%	3.8%

### Series F

December 31, 2009	Past Year	Past 3 Years	Since Inception
Bond Fund	42.6%	-4.7%	2.2%
Citigroup WGBI All Maturities (\$CAN)	-11.5%	4.5%	4.2%
Barclays U.S. Corporate High Yield Index (\$CAN)	34.4%	2.4%	4.4%

<sup>(1)</sup> Tables assume the reinvestment of all income.

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## Summary of Investment Portfolio as at December 31, 2009

### Portfolio Allocation

Foreign Corporate debts	56.9%
Corporate debts	10.3%
Income trusts	0.9%
Common shares	0.9%
Net Cash & Equivalents	<u>31.0%</u>
Total Portfolio	100.0%

### Total Holdings

(excluding cash equivalents)

International Coal Group Inc. debts	9.3%
Goldman Sachs Capital Inc. debts	8.0%
Level 3 Communications Inc. debts	5.6%
Primus Telecommunications Group Inc. shares & debts	5.5%
Abitibi-Consolidated Inc. debts	5.4%
James River Coal Company debts	4.5%
Overstock.com Inc. debts	4.3%
Wells Fargo Capital XIII debts	4.2%
Mannkind Corporation debts	4.0%
Pinnacle Airline Corporation debts	3.2%
ExpressJet Holdings Inc. debts	2.8%
French Lick Resorts & Casino debts	2.5%
SFK Pulp Fund debts & trust units	2.4%
Texas Competitive Electric debts	2.3%
CanWest MediaWorks LP debts	1.5%
Taiga Building Products Ltd. debts	1.2%
AmeriCredit Corporation debts	0.7%
Tembec Industries Inc. debts	0.6%
Clarke Inc. debts	0.4%
Global Crossing (UK) Ltd. finance debts	0.3%
The McClatchy Company debts	0.2%
Rainmaker Entertainment Inc.*	<u>0.1%</u>
Total Holdings	69.0%

\*Rainmaker Income Fund changed its name to Rainmaker Entertainment Inc. and became a corporation.

The Summary of Investment Portfolio will change due to ongoing portfolio transactions of the Fund. The next quarterly update as at March 31, 2010 will be in the Quarterly Portfolio Disclosure which will be posted on our website, [www.choufunds.com](http://www.choufunds.com), on or before May 31, 2010.

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