Press Release

For Immediate Release, March 11, 2013

Deans Knight Income Corporation

Releases Annual Management Report of Fund Performance and Financial Statements for the year ended December 31, 2012

Vancouver, B.C. - Deans Knight Income Corporation (the "Company") (TSX: DNC) is pleased to release its annual Management Report of Fund Performance and Financial Statements for the year ended December 31, 2012.

These documents can be found on SEDAR at www.sedar.com or the Company's website: www.dkincomecorp.com.

Forward-Looking Statements

This press release contains forward-looking statements. More particularly, this press release contains forward-looking statements concerning the Company's corporate objectives, the investment of the Company's proceeds from the sale of investments previously made, availability of tax losses and deductions, the anticipated total return to the Company's shareholders and the Company's intention to pay out earned income in the form of monthly dividends. Although the Company believes that the expectations reflected in these forward-looking statements are reasonable, undue reliance should not be placed on them because the Company can give no assurance that they will prove to be correct since forward-looking statements address future events and conditions and by their very nature, involve inherent risks and uncertainties. The forward-looking statements contained in this press release are made as of the date hereof and the Company 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 so required by applicable securities laws.

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DEANS KNIGHT
INCOME CORPORATION

ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE FOR 2012

This annual management report of fund performance (the "**Report**") contains financial highlights of Deans Knight Income Corporation (the "**Company**"). This Report should be read in conjunction with the annual financial statements of the Company for the year ended December 31, 2012 (the "**Financial Statements**"), which, if not included with this Report, can be obtained at your request, at no cost by emailing info@dkincomecorp.com, visiting our website at www.dkincomecorp.com for contact details or on SEDAR at www.sedar.com. Readers may also contact us to request a free copy of the Company's proxy voting policies and procedures, proxy voting disclosure record or quarterly portfolio disclosure.

A NOTE ON FORWARD-LOOKING STATEMENTS

This Report contains certain forward-looking statements. In particular, this Report contains forward-looking statements in respect of the Company's targeted dividend payout, investment strategy, behaviour of financial markets and reflects the Company's expectations regarding the growth, results of operations, performance and business prospects and opportunities of the Company and its investments. In some cases, forward-looking statements can be identified by terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "predict", "potential", "continue" or the negative of these terms or other comparable terminology. Such forward-looking statements reflect the Company's current beliefs and are based on information currently available to the Company. With respect to such forward-looking statements, the Company has made assumptions regarding, among other things, what type of debt securities will be included in its investment portfolio, currency, exchange and interest rates. A number of factors could cause actual events or results to differ materially from the results discussed in the forward-looking statements. In evaluating these statements, prospective investors should specifically consider various factors, including global equity and capital markets, business competition, technological change, changes in government regulations, unexpected judicial or regulatory proceedings, and catastrophic events and the risks outlined under "Risk Factors" in the AIF (as defined herein), which may cause actual results to differ materially from any forward-looking statement. Although the forward-looking statements contained in this Report are based upon what the Company believes to be reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward-looking statements. Forward-looking statements are made as of the date of this Report and, other than as required by applicable law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.

This Report also contains certain financial and operational information obtained from public sources in respect of certain companies included in the Company's investment portfolio. While management believes this data to be reliable, such information is subject to variations and may not be able to be verified due to limits on the availability and reliability of data inputs, the nature of the data gathering process and other limitations and uncertainties inherent in such information. Accordingly, the accuracy, currency and completeness of this information cannot be guaranteed. The Company has not independently verified any of the data from third party sources referred to in this Report or ascertained the underlying assumptions relied upon by such sources.

Investment Objectives and Strategies

The Company is a closed-end, non-redeemable investment company focused on investing in corporate debt securities. The Company's assets are actively managed by Deans Knight Capital Management Ltd. ("**Deans Knight**"), a respected British Columbia-based investment firm focused on managing high income and growth mandates for high net worth individuals. Deans Knight, formed in 1992, has an experienced management team and a long history of successful investing in corporate debt securities.

The Company's investment objectives are to: (i) maximize the total return for shareholders, consisting of dividend income and capital appreciation; and (ii) provide shareholders with monthly dividends, which to date have been set at $0.0583 per common share per month. The Company intends to continue to achieve these objectives by investing primarily in corporate debt securities rated BBB or below by Standard & Poor's Rating Services ("**S&P**") or an equivalent rating by another nationally recognized statistical rating organization. The Company may also invest in investment grade debt securities rated above BBB and non-rated debt securities from time to time. Examples of investments made during the period are detailed below in the Results from Operations.

The Company believes there are attractive investment opportunities today in owning corporate debt of businesses with tangible assets, strong cash flows and reasonable leverage.

When evaluating securities to purchase for the Company, Deans Knight focuses on the following:

- amount of security or collateral within a business to support the value of the securities;
- the position of the debt in the capital structure;
- covenants;
- liquidity;
- the business' ability to reduce or refinance the debt; and
- the overall term of the debt and yield to bondholders.

Deans Knight uses the above credit-based analysis to identify corporate debt for inclusion in the Company's investment portfolio with attractive valuations in order to maintain its targeted dividend payment.

Risk

The overall risks of the Company are as described in its annual information form of the Company dated March 11, 2013 (the "**AIF**").

Prior to the reorganization and change in business as discussed in Note 1 of the Financial Statements, the Company generated significant tax losses and other tax attributes as a result of its prior businesses and research activities. The Company has recorded, as a tax asset, the full amount of the potential tax benefit of such items to the extent of its projected taxable income. There is uncertainty as to whether the tax authorities will allow the Company to deduct some or all of the tax losses and other attributes. Should the Company be denied the deductions in full, the recorded amount of the tax assets as well as such amounts claimed to date would be recorded as a charge to income. The total tax assets recognized and tax losses and other attributes claimed to date, which are subject to uncertainty, amount to $21,154,044 (2011 - $21,024,806), representing $2.01 per common share at December 31, 2012 (2011 - $2.00).

There were no significant changes during the year ending December 31, 2012 that affected the overall risk of investing in the Company. Given the type of investments made by the Company, an investment in the Company may be considered to be speculative. An investment in the Company is generally suitable for investors who are looking to receive income, yet are willing to tolerate volatility in the value of their investment.

Results of Operations

The net assets of the Company at December 31, 2012 were $142,275,000 or $13.50 per common share (2011 - $141,539,920 or $13.43 per common share). The net assets of the Company consisted of the following components:

	December 31, 2012		
	$	**Per common share[(1)]**	**%**
Investments[(2)]	118,788,753	11.27	83.5
Cash and short-term deposits	20,091,125	1.91	14.1
Accrued income	1,662,373	0.16	1.2
Prepaid expenses	56,460	0.00	0.0
Future income tax asset[(3)]	2,390,000	0.23	1.7
Accounts payable and accrued liabilities	(713,711)	(0.07)	(0.5)
	142,275,000	13.50	100.0

(1) Based on 10,537,263 common shares, including 10,191,592 voting common shares and 345,671 non-voting common shares, as outlined in the notes to the Financial Statements.
(2) The details of the investments are outlined in the Summary of Investment Portfolio below.
(3) Refer to the Taxation note to the Financial Statements for more detail.

	December 31, 2011		
	$	**Per common share(1)**	**%**
Investments(2)	129,918,543	12.33	91.8
Cash and short-term deposits	4,997,715	0.47	3.5
Accrued income	2,339,751	0.22	1.7
Prepaid expenses	73,151	0.01	0.0
Future income tax asset(3)	4,920,000	0.47	3.5
Accounts payable and accrued liabilities	(709,240)	(0.07)	(0.5)
	141,539,920	13.43	100.0

(1) Based on 10,537,263 common shares, including 10,191,592 voting common shares and 345,671 non-voting common shares, as outlined in the notes to the Financial Statements.
(2) The details of the investments are outlined in the Summary of Investment Portfolio below.
(3) Refer to the Taxation note to the Financial Statements for more detail.

The Company began operating as an Investment Company in March 2009 to take advantage of attractive pricing in the high yield market with the objectives of: (i) maximizing the total return for Shareholders, consisting of dividend income and capital appreciation; and (ii) providing Shareholders with monthly dividends targeted to payout a minimum of 75% of net earnings annually. During 2012, the Company made monthly dividend payments totalling $7,371,869, or $0.70 per common share (2011 - $7,371,869, or $0.70 per common share). This represented approximately 83.9% of net investment income (2011 – 83.4%).

Since commencement of its investment business, the Company has made monthly dividend payments totalling $26,415,864, or $2.51 per common share. This represents approximately 90.3% of net investment income earned since March 17, 2009. On January 4, 2013, the Company announced it will maintain monthly cash dividends at $0.0583 per common share for each of the first three months of 2013.

The net assets of the Company grew in 2012 from $13.43 per common share to $13.50. The net asset value was actually down 3.4% for the first 6 months of the year but was up 4.0% in the second half contributing to the $0.07 increase in our net assets per common share. Since inception, the Company's net assets per common share have appreciated from the issue price of $10 by 35%. Over half of the capital appreciation came in the first twelve months following the issue as the economy showed signs of life from the 2008/09 credit crunch. Since that time, we have added additional value as spreads continued to narrow and from a handful of creatively structured private debt financings. The private debt financings are typically short term in nature; pay a high coupon; in some cases are fully secured; and, provide the aforementioned capital growth through "equity kickers" in the form of warrants or convertible debt.

As an example, in April 2012, Deans Knight structured a secured debt financing with Petroamerica Oil Corp. for $35 million, of which $4.0 million was subscribed to by the Company. The debentures mature on April 19, 2015 and bear interest of 11.5%. In addition to the coupon, the Company received a commitment fee of 1.5% and warrants to purchase 100 common shares per $100 of debt at an exercise price of $0.20 per share, which mature on April 19, 2015. Petroamerica is an oil producer with assets in Colombia. They started 2012 producing 200 barrels of oil equivalent per day ("boepd") with proceeds from the debt financing to be used to develop and appraise their assets. They drilled 5 wells on their Las Maracas property which, at year end, were producing 4,000 boepd net to Petroamerica. In addition to the Las Maracas asset, Petroamerica announced a new discovery at La Casona in November 2012 with one well testing at 480 boepd net to Petroamerica. With this success, Petroamerica's stock was trading at $0.35 per share at December 31, 2012, almost double the exercise price. Deans Knight Capital Management, the Company, and related parties did not receive compensation for structuring the debt financing.

Recent Developments

Comparison of net asset value and net assets

National Instrument 81-106 ("NI 81-106") permits investment companies to have two different net asset values: (i) one for financial statements, which will be prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") including Section 3855 (and referred to as "net assets") and (ii) another for all other purposes, including unit pricing for investor transactions (referred to as "net asset value"). The main difference in calculating net assets and net asset value is that GAAP requires bid price to be used in valuing securities traded in an active market where quoted prices are readily and regularly available, rather than the use of a price between the bid and the ask price currently used for determining net asset value. This difference results in an insignificant difference of approximately $0.08 per common share at December 31, 2012 (2011 - $0.06 per common share), as outlined in the notes to the Financial Statements.

International Financial Reporting Standards

The Company will be required to adopt international financial reporting standards ("IFRS"). The Canadian Accounting Standards Board (AcSB) previously announced January 1, 2011 as the date international financial reporting standards (IFRS) would replace current Canadian standards and interpretations as GAAP for publicly accountable enterprises, which include investment companies.

In December 2011, the AcSB issued a decision to defer adoption of IFRS for investment companies currently applying Accounting Guideline 18 - Investment Companies until years beginning on or after January 1, 2014.

Under the above noted decision, the Company's first set of financial statements to be reported on under IFRS would be for the semi-annual period ending June 30, 2014. These statements would include corresponding comparative financial information for 2013, including an opening statement of net assets as at January 1, 2013. However, the Company has a termination date of April 30, 2014, and as such will not be required to issue statements reported on under IFRS. The Company will continue to monitor any further AcSB decisions that may affect the Company's requirement to adopt IFRS.

Harmonized Sales Tax

The Company is subject to non-recoverable Harmonized Sales Tax on its expenses. The BC Government has announced that the Harmonized Sales Tax will be replaced by the Federal Goods and Services Tax and a Provincial Sales Tax in April 2013; however, this is not expected to have a significant impact on net assets per common share.

Related Party Transactions

The officers, and certain directors, of the Company are also employees of Deans Knight, the Company's investment advisor. These officers, and directors, are not paid by the Company. Deans Knight provides investment management services to the Company, as well as administration, financial reporting and other ancillary services required by a publicly listed company. Management fees, for the services outlined above, are computed and paid quarterly, at an annual rate of 1.5% of the net asset value plus applicable taxes, and adjusted for certain non-investment related assets.

For the year ended December 31, 2012, management fees totaled $2,311,284 (2011 - $2,283,158). At December 31, 2012, $589,251 (December 2011- $575,224) was owed to Deans Knight, which was included in accounts payable and accrued liabilities in the statement of net assets, and is payable immediately. In calculating the management fee, the net asset value was reduced by the value of the future income tax asset included in the statement of net assets.

A director of the Company is a partner at a law firm that provides legal services to the Company. During the year ended December 31, 2012, the Company incurred $14,014 (2011 - $42,750) in legal services and disbursements received from this related party. At December 31, 2012, accounts payable and accrued liabilities include $226 (2011 - $4,185) due to the law firm for legal fees and disbursements.

Financial Highlights

The following tables show selected key financial information about the Company and are intended to help you understand the Company's financial performance since it began operating its new business of investing in corporate debt in March 2009.

The Company's Net Assets per Common Share [(1)]

	2012 $	2011 $	2010 $	Period March 17 to December 31, 2009 $
Net assets, beginning of year [(2)]	13.43	13.60	12.21	9.12
Increase from operations				
Total revenue	1.10	1.10	0.94	0.62
Total expenses	(0.26)	(0.26)	(0.24)	(0.20)
Realized gains	0.44	0.36	1.82	1.25
Unrealized losses	(0.27)	(0.52)	(0.27)	1.21
Future income taxes	(0.24)	(0.15)	(0.16)	0.62
Total increase from operations [(2)]	0.77	0.53	2.09	3.50
Dividends [(2)(3)]	(0.70)	(0.70)	(0.70)	(0.41)
Net assets, end of year [(4)]	13.50	13.43	13.60	12.21

(1) The information is derived from the Company's audited annual financial statements. Common shares outstanding are 10,537,263, including 10,191,592 voting common shares and 345,671 non-voting common shares.
(2) Net assets and dividends are based on the actual number of common shares outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of common shares outstanding over the year.
(3) Dividends were paid in cash.
(4) The net assets per common share presented in the financial statements differs from the net asset value per common share calculated for fund pricing purposes due to the provisions of CICA Handbook Section 3855. An explanation of the differences can be found in the notes to the financial statements.

Ratios and Supplemental Data [(1)]

	2012	2011	2010	Period March 17 to December 31, 2009
Net asset value (000's)	$143,065	$142,178	$143,880	$128,930
Number of common shares outstanding (000's)	10,537	10,537	10,537	10,537
Management expense ratio [(2)]	1.96%	1.90%	1.91%	5.51%
Portfolio turnover rate [(3)]	14.79%	79.90%	86.60%	36.69%
Trading expense ratio [(4)]	0.01%	0.00%	0.01%	0.01%
Net asset value per common share	$13.58	$13.49	$13.65	$12.23
Closing market price – common share	$12.69	$11.84	$12.54	$11.40

(1) This information is provided as at December 31 of the years shown.
(2) Management expense ratio is based on total expenses for the period and is expressed as an percentage of weekly average net asset values over the year.
(3) The Company's portfolio turnover rate indicates how actively the Company manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Company buying and selling all of the securities in its portfolio once in the course of the year. The higher a portfolio turnover-rate in a year, the greater the trading costs payable by the Company in the year. There is not necessarily a relationship between a high turnover rate and the performance of the investment portfolio.
(4) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net asset value during the period. This expense is $11,318 for 2012 (2011- $nil), as the purchasing and selling of bonds do not generally attract a commission from the buying or selling party.

Management Fees

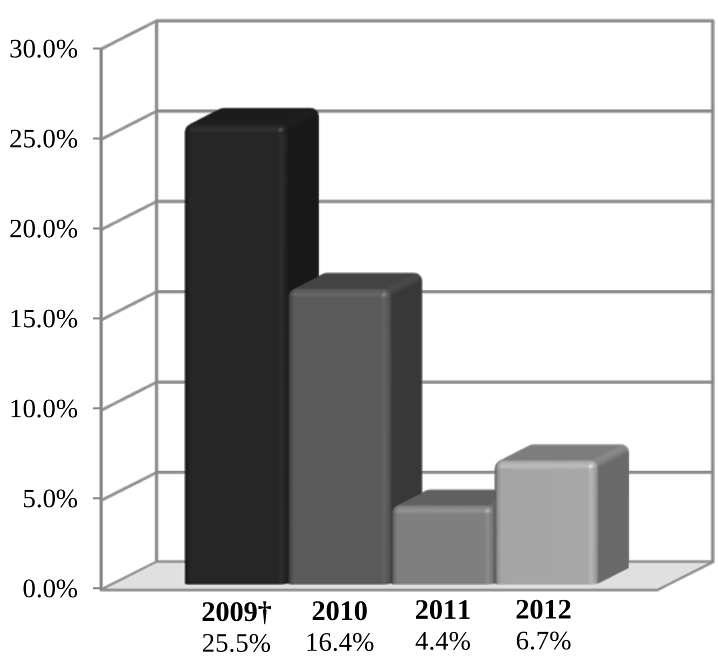
Deans Knight provides investment management services to the Company, as well as administration, financial reporting and other ancillary services required by a publicly listed company. Management fees are computed and paid quarterly, at an annual rate of 1.5% of the net asset value plus applicable taxes, and adjusted for certain non-investment related assets.

Past Performance

This section shows the Company's past performance, since it began operating its business as an investment fund. The past performance information includes changes in net asset value and assumes the reinvestment of all dividends paid to common shareholders. It is important to note that the past performance will not necessarily indicate what performance in the future will be.

Year-by-year Returns

The accompanying bar chart shows the Company's performance for the years shown and illustrates how the Company's performance has changed from year to year. The bar chart shows, in percentage terms, how much an investment made from when the Company began its operation as an investment fund on March 17, 2009 to December 31, 2009, and how much an investment made for the years ending December 31, 2010, 2011 and 2012.



† March 17, 2009 (Inception) to Dec. 31, 2009

Annual Compound Returns

The table below summarizes the Company's annual compound total returns for the periods ended December 31 as indicated. As a basis for comparison, we have provided the performance of the Merrill Lynch Canada High Yield Bond Index ("Index"). The Index is a broad based index that tracks the performance of the Canadian high-yield bond market. As the criteria for determining the constituents of the Company's investment portfolio and the Index differ, it is not expected that the Company's performance will mirror that of the Index. Further, the return of the Index is calculated without the deduction of management fees and fund expenses whereas the performance of the Company is calculated after deducting fees and expenses.

Annual Compound Returns	**Company**	**Index**
1 Year	6.70%	15.10%
2 Years	5.60%	9.10%
3 Years	9.10%	10.60%
Since Inception	14.00%	19.90%

Summary of Investment Portfolio

The following is a summary of the Company's investment portfolio as at December 31, 2012. This is a summary only and will change due to ongoing portfolio transactions of the Company. A quarterly update is available at www.dkincomecorp.com.

Top 25 Investments			% of Net Asset Value
PARAMOUNT RESOURCES	8.250%	13-Dec-17	6.7
WHITECAP RESOURCES	N/A	N/A	6.1
MIRABELA NICKEL LTD	8.750%	15-Apr-18	6.0
STONE ENERGY CORP	8.625%	1-Feb-17	5.8
NORTH AMERICA ENERGY	9.125%	7-Apr-17	5.4
SOUTHERN PACIFIC RES	10.500%	1-Jan-16	4.2
CALFRAC HOLDINGS LP	7.500%	1-Dec-20	4.1
NORTHLAND RESOURCES	13.000%	6-Mar-17	3.4
PERPETUAL ENERGY INC	8.750%	15-Mar-18	3.4
TEMBEC INDUSTRIES	11.250%	15-Dec-18	3.2
CCS INC	11.000%	15-Nov-15	3.1
PETROAMERICA OIL	11.500%	19-Apr-15	2.8
SHERRITT INTL CORP	8.000%	15-Nov-18	2.8
CARA OPERATIONS LTD	9.125%	1-Dec-15	2.5
GARDA WORLD SECURITY	9.750%	15-Mar-17	2.4
BEAZER HOMES USA	9.125%	15-Jun-18	2.4
CONIFEX TIMBER INC	12.000%	31-Dec-13	2.1
GATEWAY CASINOS	8.875%	15-Nov-17	2.0
BLACK PRESS GROUP	10.000%	4-Feb-14	1.9
PACIFIC RUBIALES	7.250%	12-Dec-21	1.8
SURE ENERGY	6.250%	21-Jan-14	1.8
WESTERN ENERGY SVS	7.785%	30-Jan-19	1.6
NIKO RESOURCES LTD.	7.000%	13-Dec-17	1.5
99 CENTS ONLY STORES	11.000%	15-Dec-19	1.5
SHERRITT INTL CORP	7.500%	24-Sep-20	1.4

Portfolio Composition	% of Net Asset Value
Fixed Income	
Canadian denominated in CAD	39.9
Canadian denominated in USD	18.2
United States denominated in USD	14.6
Other Foreign denominated in USD	3.4
Other Foreign denominated in EUR	0.9
	77.0
Convertible Debentures	
Other Foreign denominated in AUD	-
	77.0
Equity and Warrants	6.6
Investment Portfolio	83.6
Cash & Short-term Deposits	14.1
Other Net Assets	2.3
	100.0
Sector Breakdown	
Energy	49.9
Materials & Metals	13.7
Consumer Discretionary	8.4
Forestry	6.2
Industrial/Manufacturing	4.3
Technology	0.9
Services	0.2
Investment Portfolio	83.6
Cash & Short-term Deposits	14.1
Other Net Assets	2.3
	100.0

Deans Knight Income Corporation

Financial Statements
December 31, 2012

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March 11, 2013

Independent Auditor's Report

To the Shareholders of Deans Knight Income Corporation

We have audited the accompanying financial statements of Deans Knight Income Corporation which comprise the statements of net assets as at December 31, 2012 and 2011, the statements of operations, changes in net assets and cash flows for the years then ended, the statement of investments as at December 31, 2012, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Deans Knight Income Corporation as at December 31, 2012 and 2011 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Deans Knight Income Corporation

Statements of Net Assets

As at December 31, 2012 and 2011

	2012 $	2011 $
Assets		
Investments - at fair value (cost - $117,207,284 ; 2011 - $125,475,983)	118,788,753	129,918,543
Cash and cash equivalents	20,091,125	4,997,715
Accrued interest receivable	1,662,373	2,339,751
Prepaid expenses	56,460	73,151
Future income tax benefits (note 7)	2,390,000	4,920,000
	142,988,711	142,249,160
Liabilities		
Accounts payable and accrued liabilities (note 5)	713,711	709,240
Net assets	142,275,000	141,539,920
Shareholders' equity		
Common shares (note 3)	99,366,429	99,366,429
Contributed surplus (note 3)	9,904,504	9,904,504
Retained earnings (note 4)	33,004,067	32,268,987
	142,275,000	141,539,920
Number of common shares outstanding (note 3)	10,537,263	10,537,263
Net assets per common share (notes 7 and 10)	13.50	13.43

Contingencies (notes 1 and 7)
Commitments (notes 1 and 9)
Subsequent events (note 11)

Approved by the Board of Directors

(signed) Wayne Deans Director (signed) Craig Langdon Director

The accompanying notes are an integral part of these financial statements.

Deans Knight Income Corporation

Statements of Operations

For the years ended December 31, 2012 and 2011

	2012 $	2011 $
Investment income		
Interest and other	11,547,744	11,607,293
Expenses		
Management fees (note 5)	2,311,289	2,283,158
Directors' fees and expenses	148,727	157,681
Public company reporting costs	127,384	141,111
Audit, accounting and tax fees	82,024	87,003
Custodial fees	50,651	51,354
Legal fees (note 5)	14,014	37,336
Independent Review Committee fees	12,180	12,000
Transaction costs	11,318	-
	2,757,587	2,769,643
Net investment income	8,790,157	8,837,650
Realized and unrealized gains (losses) on investments		
Net realized gain on investments sold (note 6)	2,548,818	4,695,889
Net realized gain (loss) on settlement of foreign currency contracts (note 6)	2,159,065	(892,178)
Change in unrealized appreciation on investments	(2,564,496)	(5,832,280)
Unrealized (depreciation) appreciation on foreign currency contracts	(296,595)	389,347
Net gain (loss) on investments	1,846,792	(1,639,222)
Increase in net assets from operations before tax	10,636,949	7,198,428
Provision for future income tax (note 7)	(2,530,000)	(1,630,000)
Increase in net assets from operations	8,106,949	5,568,428
Increase in net assets from operations per weighted average common share (note 2)	0.77	0.53

The accompanying notes are an integral part of these financial statements.

Deans Knight Income Corporation

Statements of Changes in Net Assets

For the years ended December 31, 2012 and 2011

	2012 $	2011 $
Increase in net assets from operations	8,106,949	5,568,428
Dividends to common shareholders (notes 4 and 9)	(7,371,869)	(7,371,869)
Increase (decrease) in net assets during the year	735,080	(1,803,441)
Net assets – Beginning of year	141,539,920	143,343,361
Net assets – End of year	142,275,000	141,539,920

The accompanying notes are an integral part of these financial statements.

Deans Knight Income Corporation

Statements of Cash Flows

For the years ended December 31, 2012 and 2011

	2012 $	2011 $
Cash flows from operating activities		
Increase in net assets from operations	8,106,949	5,568,428
Items not affecting cash		
Net realized gain on investments sold	(2,548,818)	(4,695,889)
Net realized (gain) loss on settlement of foreign currency contracts	(2,159,065)	892,178
Change in unrealized appreciation on investments	2,564,496	5,832,280
Unrealized depreciation (appreciation) on foreign currency contracts	296,595	(389,347)
Future income tax provision	2,530,000	1,630,000
	8,790,157	8,837,650
Cost of investments purchased (note 6)	(18,898,699)	(62,743,948)
Proceeds from investments sold (note 6)	31,875,281	59,635,633
Net change in non-cash balances related to operations		
Accrued interest receivable	677,378	(530,995)
Prepaid expenses	16,691	16,511
Accounts payable and accrued liabilities	4,471	16,766
	22,465,279	5,231,617
Cash flows from financing activities		
Dividends paid to common shareholders (notes 4 and 9)	(7,371,869)	(7,371,869)
Net increase (decrease) in cash and cash equivalents during the year	15,093,410	(2,140,252)
Cash and cash equivalents – Beginning of year	4,997,715	7,137,967
Cash and cash equivalents – End of year	20,091,125	4,997,715
Cash and cash equivalents comprise		
Cash	9,110,875	2,402,631
Short-term deposits	10,980,250	2,595,084
	20,091,125	4,997,715

Deans Knight Income Corporation

Statement of Investments

As at December 31, 2012

	Par value [1] $	Average cost [2] $	Fair value [2] $	Percentage of total fair value [3] %
Fixed income - Canadian				
Denominated in Canadian dollars				
Athabasca Oil Corp 7.5% 11-19-2017	1,500,000	1,500,000	1,500,000	1.3
Black Press Group 10.00% 02-04-2014 [4]	2,750,000	2,750,000	2,746,563	2.3
Cara Operations Ltd. 9.13% 12-01-2015	3,500,000	3,500,000	3,622,500	3.0
Conifex Timber Inc. 12.00% 12-31-2013 [4]	3,000,000	3,000,000	3,000,000	2.5
Garda World Security 9.75% 03-15-2017	3,250,000	3,237,105	3,380,000	2.8
Gateway Casinos 8.88% 11-15-2017	2,750,000	2,816,875	2,894,375	2.4
North American Energy Partners Inc. 9.13% 04-07-2017	8,750,000	8,793,125	7,743,750	6.5
Paramount Resources Ltd. 8.25% 12-13-2017	9,250,000	9,250,000	9,596,875	8.1
Perpetual Energy Inc. 8.75% 03-15-2018	5,000,000	5,000,000	4,775,000	4.0
Petroamerica Oil Corp. 11.50% 04-19-2015 [4]	4,000,000	4,000,000	4,000,000	3.4
Sherritt International Corp. 7.75% 10-15-2015	196,000	152,233	208,740	0.2
Sherritt International Corp. 8.00% 11-15-2018	3,750,000	3,750,000	3,937,500	3.3
Sherritt International Corp. 7.50% 09-24-2020	2,000,000	2,000,000	2,045,000	1.7
Skylink Aviation Inc. 12.25% 03-15-2016	5,450,000	5,357,250	1,635,000	1.3
Sure Energy Inc. 6.25% 01-21-2014 [4]	2,500,000	2,500,000	2,500,000	2.1
Western Energy Services Corp. 7.88% 01-30-2019	2,250,000	2,250,000	2,317,500	2.0
		59,856,588	55,902,803	46.9
Denominated in United States dollars				
CCS Inc. 11.00% 11-15-2015	4,500,000	2,252,568	4,465,856	3.8
Mirabela Nickel Ltd. 8.75% 04-15-2018	10,050,000	9,138,320	8,498,933	7.2
Pacific Rubiales Energy Corp. 7.25% 12-12-2021	2,300,000	2,365,780	2,628,650	2.2
Southern Pacific Resources Libor+8.5% 01-01-2016	5,880,000	5,808,758	5,908,513	5.0
Tembec Industries 11.25% 12-15-2018	4,250,000	4,494,779	4,503,166	3.8
		24,060,205	26,005,118	22.0
Total Canadian fixed income		83,916,793	81,907,921	68.9

[1] Par values are presented in their source currency
[2] All amounts are shown in Canadian dollars
[3] Percentages are shown as a percentage of total investments
[4] These investments represent loans receivable

Deans Knight Income Corporation

Statement of Investments...*continued*

As at December 31, 2012

	Par value [1] $	Average cost [2] $	Fair value [2] $	Percentage of total fair value [3] %
Fixed income – United States				
Denominated in United States dollars				
99 Cents Only Stores 11.00% 12-15-2019	1,850,000	1,926,584	2,079,838	1.8
Abitibibowater Inc. 10.25% 10-15-2018	1,185,000	1,221,735	1,349,905	1.1
Beazer Homes USA, Inc. 9.13% 06-15-2018	3,250,000	3,327,056	3,370,846	2.8
Calfrac Holdings LP 7.5% 12-01-2020	6,000,000	6,130,329	5,894,783	5.0
Stone Energy Corp. 8.63% 02-01-2017	7,750,000	7,813,451	8,211,656	6.9
Total United States fixed income		20,419,155	20,907,028	17.6
Fixed income - International				
Denominated in United States dollars				
Northland Resources 13.0% 03-16-2017	4,750.000	4,678,275	4,820,291	4.1
Total fixed income		109,014,223	107,635,240	90.6
Convertible debentures - Canada				
Denominated in Canadian dollars				
Niko Resources Ltd. 7.00% 12-13-2017	2,000,000	2,000,000	2,200,000	1.9
Equities – Canada				
Conifex Timber Inc.- purchase warrants $9.38 strike, 12-31-2014	81,250	-	16,102	0.0
Petroamerica Oil Corp. - purchase warrants $0.20 strike, 04-19-2015	400	-	661,311	0.6
Sure Energy Inc.- purchase warrants $1.80 strike, 12-21-2013	625,000	-	-	0.0
Whitecap Resources Inc.- common shares	1,005,367	6,193,061	8,696,425	7.3
Total equities		6,193,061	9,373,838	7.9
Royalties – Canada				
Denominated in Euro				
RapidEye Canada Royalty		-	1,238,770	1.0
Provision for investments		-	(1,362,500)	(1.1)
Investments subtotal		117,207,284	119,085,348	100.3
Foreign Currency Contracts (note 8)				
Denominated in United States dollars				
Payable 01-08-2013 at 0.99310	25,000,000	-	(47,949)	(0.1)
Payable 01-08-2013 at 0.99356	3,000,000	-	(4,356)	(0.0)
Payable 02-12-2013 at 0.98698	28,000,000	-	(244,290)	(0.2)
Total foreign currency contracts		-	(296,595)	(0.3)
		117,207,284	118,788,753	100.0

[1] Par values are presented in their source currency

[2] All amounts are shown in Canadian dollars

[3] Percentages are shown as a percentage of total investments

[4] These investments represent loans receivable

The accompanying notes are an integral part of these financial statements.

1 Nature of operations and basis of presentation

Deans Knight Income Corporation (the "Company") is a corporation continued under the laws of Canada on April 11, 2001. The Company is a closed-end, non-redeemable investment company. It invests, primarily, in corporate debt rated BBB or below by recognized credit rating organizations.

Prior to its reorganization in May 2008, the Company was a life sciences company involved in the research, development and commercialization of innovative products for the prevention and treatment of life-threatening diseases. Forbes Medi-Tech Inc ("Forbes"), who now carries on the prior business of the Company, has provided an indemnity to the Company with respect to liabilities relating to the Company's assets transferred to Forbes and the Company's prior business. In addition, Forbes obtained, on behalf of the Company, product liability insurance for certain claims that may arise in the future in connection with the Company's prior business. To date, no such claims or potential claims have arisen. There can be no assurance that the above noted guarantee will be sufficient to cover any future claims. In March 2009, the Company completed an initial public offering, whereby it raised gross proceeds of $100,368,900 and began operating its new business as an investment company.

As per the Company's Articles of Incorporation, the common shares of the Company are to be redeemed on, or around, April 30, 2014, for a cash amount equal to 100% of the net asset value per common share.

The accompanying financial statements are prepared in accordance with Part V of the Canadian Institute of Chartered Accountants Handbook, Pre-changeover Accounting Standards (GAAP). All amounts are presented in Canadian dollars, unless otherwise noted.

2 Summary of significant accounting policies

The following is a summary of significant accounting policies followed by the Company:

Financial instruments

Investments

Investments are held for trading and are recorded at fair values determined as follows:

Fixed income investments

Fixed income investments traded on a public securities exchange or traded on an over-the-counter market are valued at the closing bid price. Where no closing bid price is available, the last sale or close price is used where, in management's opinion, this provides the best estimate of fair value.

Unlisted or non-exchange traded investments, or investments where a last bid, sale or close price is unavailable, or investments for which market quotations are, in the Company's opinion, inaccurate, unreliable, or not reflective of all available material information, are valued at their fair value as determined by the Company using appropriate and accepted industry valuation techniques including valuation models. The fair value determined using valuation models requires the use of inputs and assumptions based on observable market data including volatility and other applicable rates or prices. In certain circumstances, the fair value may be determined using valuation techniques that are not supported by observable market data.

The resulting values for investments not traded in an active market may differ from values that would be determined had a ready market existed, and the difference could be significant.

Foreign currency contracts

Foreign currency contracts are recorded at fair value. The proceeds (payments) on contracts settled during the year are included in the net realized gain (loss) on settlement of foreign currency contracts (note 6). The Company's policy is to hedge 95% - 105% of the fair value of foreign denominated investments with foreign exchange forward sell contracts.

Public company equities

Publicly traded equities are recorded at bid prices as quoted on recognized stock exchanges.

The amounts at which the Company's publicly-traded investments could be disposed of currently may differ from carrying value based on market quotes, as the value at which significant ownership positions are sold is often different than the quoted market price due to a variety of factors such as premiums paid for large blocks or discounts due to illiquidity.

Warrants

Warrants are recorded at their estimated fair value using appropriate and accepted industry valuation techniques.

The impact of changes in fair value of investments is recorded in the statement of operations.

Cash and cash equivalents

Cash and cash equivalents are accounted for at amortized cost. They consist of cash and deposits with maturities, at the time of purchase, of three months or less and are held with a Canadian chartered bank.

Accrued interest receivable

Accrued interest is designated as loans and receivables and is accounted for at amortized cost. Due to the immediate and short-term nature, carrying value approximates fair value.

Financial liabilities

Financial liabilities, consisting of accounts payable and accrued liabilities, are designated as other financial liabilities and are accounted for at amortized cost. Due to the immediate and short-term nature, the carrying value approximates fair value.

Investment transactions

Investment transactions are recorded on the trade date. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an investment, which include fees and commissions paid to agents, advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. These costs are expensed and are included in the statement of operations.

Income recognition

Income from investments is recognized on an accrual basis. Interest income is accrued based on the number of days the investment is held during the year. Royalty income is recognized on an accrual basis as earned. Gains or losses on the sale of investments, including foreign exchange gain or loss on such investments, are calculated on an average cost basis.

Foreign currency contracts

Foreign currency contracts (note 8) entered into by the Company are valued at an amount that is equal to the gain or loss that would be realized if the position were to be closed out, which is equivalent to the difference between the deliverable asset and the value of the asset to be received. Changes in the value of a forward contract or the assets deliverable under such a contract are included as unrealized appreciation/depreciation on foreign currency contracts in the statement of operations.

Foreign exchange

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rate applicable on the valuation date. Purchases and sales of investments, investment income and expenses are calculated at the exchange rates prevailing on the dates of the transactions.

Income taxes

The Company follows the asset and liability method of accounting for income taxes. Future income tax assets and liabilities are measured using rates expected to apply to the taxable income in the years in which the temporary differences are expected to be settled. The Company accounts for uncertain tax positions using the contingent liability model, whereby a provision is established only where it is likely that a payment will be required to be made.

A valuation allowance is recognized to the extent that it is more likely than not future income tax assets will not be realized. Management has estimated the income tax provision and future income tax balances taking into account its expectation of future taxable income and an interpretation of the various income tax laws and regulations. It is possible, due to the complexity inherent in estimating income taxes, that the tax provision and future tax balances could change (note 7), and the change could be significant.

Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses. Actual results could differ from those reported and such differences could be material. Significant areas involving the use of estimates include determining the estimated fair value of investments and future income tax assets.

Net assets per common share

The net assets per common share are computed by dividing the net assets of the Company by the total number of common shares outstanding on the statements of net assets date.

Increase in net assets from operations per weighted average common share

The increase in net assets from operations per common share represents the increase in net assets from operations divided by the weighted average number of common shares outstanding during the year.

The weighted average number of shares outstanding during the year ended December 31, 2012 was 10,537,263 (2011 - 10,537,263). This weighted average includes both the voting common shares and non-voting common shares of the Company.

3 Capital stock

The Company is authorized to issue an unlimited number of voting common shares without par value, and an unlimited number of non-voting common shares without par value.

There were no changes in the number of voting and non-voting common shares for the years ended December 31, 2011 and 2012.

The total shares outstanding at December 31 are summarized as follows:

		2012		**2011**
	Number of Shares	**Amount $**	**Number of Shares**	**Amount $**
Voting common shares	10,191,592	96,273,343	10,191,592	96,273,343
Non-voting common shares	345,671	3,093,086	345,671	3,093,086
Total common shares outstanding	10,537,263	99,366,429	10,537,263	99,366,429

Contributed surplus

Contributed surplus consists of:

	2012 $	**2011** $
Surplus related to stock compensation, warrants and options associated with common shares	8,030,295	8,030,295
Surplus relating to warrants associated with previously issued preferred shares	1,874,209	1,874,209
	9,904,504	9,904,504

4 Retained earnings

The changes in retained earnings for the year were as follows:

	2012 $	**2011** $
Retained earnings – opening balance	32,268,987	34,072,428
Increase in net assets from operations	8,106,949	5,568,428
Dividends paid from net investment income	(7,371,869)	(7,371,869)
Retained earnings – closing balance	33,004,067	32,268,987

5 Related party transactions and balances

Management fees are paid quarterly to Deans Knight Capital Management Ltd. (the Investment Advisor), a corporation with certain common directors and officers of the Company, for services received in connection with the management of the investment portfolio and financial accounts, among other services provided. Management fees are computed quarterly at an annual rate of 1.5% of net asset value, adjusted for certain non-investment related assets. For the year ended December 31, 2012, management fees (including applicable taxes) totalled $2,311,289 (2011- $2,283,158). At December 31, 2012, $589,251 (2011 - $575,224) was owed to the Investment Advisor, which was included in accounts payable and accrued liabilities in the statement of net assets, and is payable immediately.

A director of the Company is a partner at a law firm that provides legal services to the Company. During the year ended December 31, 2012, the Company incurred $14,014 (2011 - $ 42,750) in legal services and disbursements received from this related party. At December 31, 2012, accounts payable and accrued liabilities include $226 (2011 - $4,185) due to the law firm for legal fees and disbursements.

6 Net realized gains on investments sold and foreign currency contracts

The net realized gain on investments sold and foreign currency contracts for the year ended December 31 was as follows:

	2012 **$**	**2011** **$**
Proceeds from sale of investments	31,875,281	59,635,633
Investments at cost – Beginning of year	125,475,983	118,563,957
Add: Cost of investments purchased	18,898,699	62,743,948
	144,374,682	181,307,905
Less: Investments at cost – End of year	(117,207,284)	(125,475,983)
Cost of investments sold	27,167,398	55,831,922
Net realized gain on investments sold	4,707,883	3,803,711

Net realized gain on investments sold and foreign currency contracts consists of:

	2012 **$**	**2011** **$**
Realized gain on investments sold	2,548,818	4,695,889
Realized gain (loss) on settlement of foreign currency contracts	2,159,065	(892,178)
	4,707,883	3,803,711

7 Taxation

Uncertainty of deductibility of tax losses

Prior to the reorganization and change in business as discussed in note 1, the Company had generated significant tax losses and other tax attributes as a result of its prior businesses and research activities. The Company has recorded, as a tax asset, the full amount of the potential tax benefit of such items to the extent of its projected taxable income. There is no guarantee that the tax authorities will allow the Company to deduct some, or all, of the tax losses and other attributes. Should the Company be denied the deductions, the recognized amount of the tax assets, as well as such amounts claimed to date, would be recorded as a charge to income. The total tax assets recognized and tax losses and other attributes claimed to December 31, 2012, which are subject to uncertainty, amount to $21,154,044 (2011 - $21,024,806), representing $2.01 per common share at December 31, 2012 (2011 - $2.00 per common share).

Future tax asset

Canadian GAAP requires a valuation allowance to be recognized against any future tax asset to the extent that it is more likely than not that the future income tax asset will not be realized. This is also the Company's stated accounting policy.

As the Company's investments in debt securities are generating interest income, but are not expected to generate sufficient taxable income in order to fully utilize the available tax credits during the years of operations through to April 30, 2014, the Company has recorded a valuation allowance. The difference between the total value of these tax benefits less the valuation allowance, being $2,390,000 (2011 - $4,920,000), is the amount of the future income tax asset that has been recorded by the Company in the statement of net assets. The valuation allowance is reviewed, based on updated projections of taxable income, and adjusted accordingly by a credit or charge to the statement of operations.

The tax effects of temporary differences and tax credits that give rise to significant components of the future income tax assets, at the statutory enacted rates when such benefits are expected to be realized, are as follows:

	2012 $	2011 $
Future tax assets		
Research and development expenditures	4,533,250	6,879,250
Investment tax credits	5,322,750	5,322,750
Share issuance costs	313,440	626,880
Total gross future tax assets	10,169,440	12,828,880
Valuation allowance	(7,779,440)	(7,908,880)
Net future tax asset	2,390,000	4,920,000

Future tax assets expected to be realized in:

	2012 $	2011 $
Less than 12 months	1,930,000	2,180,000
Greater than 12 months	460,000	2,740,000
Net future tax asset	2,390,000	4,920,000

The tax balances and income tax expense recognized by the Company are based on management's interpretation of the tax laws. Due to the complexity inherent in tax interpretations, regulations and legislation, there are significant estimates required to compute income tax balances. It is possible that some or all of the Company's significant components of the future income tax assets may not be deductible for tax purposes and, accordingly, the amount of future income taxes and provision for income taxes recorded in the financial statements could change by a material amount.

In determining the amount of future income tax assets recognized, management assessed the projected taxable income of the Company. Inherent in all forward looking information is uncertainty and actual amounts could differ from these estimates and the difference could be material. In developing the projection, management has assumed full payment of all contractual interest, that investments maturing prior to April 30, 2014 will be redeemed for par value, and that investments maturing after April 30, 2014 will be sold at their current value.

Tax pools available to offset future tax expense and payable

The operations of the Company and related tax interpretations, regulations and legislation are continually changing. As a result, significant estimates are required to compute income tax balances. As at December 31, 2012, the Company has accumulated scientific research and experimental development expenditures in the amount of $18,133,000 available for carry-forward indefinitely. The Company also has accumulated approximately $7,097,000 of unclaimed federal investment tax credits, which expire as follows:

	Investment tax credits $
Year of expiry	
2018	265,000
2019	990,000
2020	1,872,000
2021	2,483,000
2022	298,000
2023	187,000
2024	496,000
2025	506,000
	7,097,000

Reconciliation of income tax expense

The reconciliation of income tax computed at the statutory tax rate to income tax expense, using a 25.0% statutory tax rate (2011 - 26.5%), is:

	2012 $	2011 $
Increase in net assets from operations before tax	10,636,949	7,198,428
Statutory tax rate	25.0%	26.5%
Income tax expense at statutory rates	2,659,238	1,907,583
Use of scientific research and experimental development expenditures	(2,345,798)	(1,575,337)
Reduction of future tax asset	2,530,000	1,630,000
Current tax deductions for offering costs	(313,440)	(332,246)
Provision for future income tax	2,530,000	1,630,000

8 Financial instruments

Fair value measurement

Financial instruments are classified in a hierarchy that prioritizes the inputs to fair value measurement. Each level is based on the transparency of the inputs used to measure the fair values of assets and liabilities. The three levels of the fair value hierarchy are:

Level 1 – inputs that reflect unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – inputs that reflect other than quoted prices that are observable for the assets or liabilities either directly or indirectly;

Level 3 – inputs that are not based on observable market data.

The following tables illustrate the classification of the Company's financial instruments within the fair value hierarchy:

	Financial assets at fair value – 2012			
	Level 1 $	**Level 2 $**	**Level 3 $**	**Total $**
Corporate debt	-	93,669,383	13,965,857	107,635,240
Convertible debentures	-	2,200,000	-	2,200,000
Equity	8,696,425	-	677,413	9,373,838
Royalty	-	-	1,238,770	1,238,770
Other	-	(1,362,500)	-	(1,362,500)
Foreign currency contracts	-	(296,595)	-	(296,595)
	8,696,425	94,210,288	15,882,040	118,788,753

	Financial assets at fair value – 2011			
	Level 1 $	**Level 2 $**	**Level 3 $**	**Total $**
Corporate debt	-	94,406,534	22,965,956	117,372,490
Convertible debentures	-	-	1,554,218	1,554,218
Equity	10,397,044	-	205,444	10,602,488
Foreign currency contracts	-	389,347	-	389,347
	10,397,044	94,795,881	24,725,618	129,918,543

All investments remained at their respective levels within the fair value hierarchy during the year.

The following table reconciles the Company's Level 3 fair value measurements:

	Fair value measurements of Level 3 inputs				
	Corporate debt $	**Convertible debentures $**	**Equities $**	**Royalty $**	**Total $**
Balance – December 31, 2010	14,475,875	3,617,677	400,000	-	18,493,552
Purchases	14,812,500	-	-	-	14,812,500
Sales	(7,031,250)	(2,148,120)	-	-	(9,179,370)
Unrealized appreciation (depreciation) included in net gain on investments	708,831	84,661	(194,556)	-	598,936
Balance – December 31, 2011	22,965,956	1,554,218	205,444	-	24,725,618
Purchases	4,000,000		-	-	4,000,000
Sales	(13,081,762)	(1,558,378)	-	-	(14,640,140)
Unrealized appreciation (depreciation) included in net gain on investments	81,663	4,160	471,969	1,238,770	1,796,562
Balance – December 31, 2012	13,965,857	-	677,413	1,238,770	15,882,040

Level 3 fair value measurements have predominantly been valued by considering data inputs such as the last price the security was traded at, most recent bid/ask information, prices of similar securities with available prices, and comparison of yields of comparable investments. Accordingly, in the absence of any reasonably possible alternative assumptions, and except as noted below, it is not practicable to provide a sensitivity analysis.

For certain Level 3 investments measured on a discounted cash flow basis the value is imputed through forecasted cash flows and discount rates. The following summarizes the affect a change in assumptions would have on total net assets at December 31, 2012:

	Increase by 5%	Decrease by 5%
Cash flow growth rate	198,972	(189,288)
Discount rate	(219,021)	279,418

Management of financial risks

In the normal course of business, the Company is exposed to various financial risks, including credit risk, liquidity risk and market risk (consisting of interest rate risk, currency risk and other price risk). The Company's overall risk management program seeks to minimize potentially adverse effects of these risks on the Company's financial performance by employing a professional, experienced portfolio advisor, monitoring daily the Company's positions and market events, diversifying the investment portfolio within the constraints of the investment guidelines and periodically using derivatives to hedge certain risk exposures. Further, the Company monitors the portfolio to ensure compliance with its investment strategy, investment guidelines and securities regulations.

Fair value risk

The Company's investments are exposed to market price risk and this risk affects the fair value of the investments. All investments have an inherent risk of loss of capital. The maximum risk resulting from investments is determined by their fair value. The Company seeks to manage valuation risks by careful selection of fixed income investments prior to making an investment and by regular ongoing monitoring of the investment performance of the individual investee companies. Due to the predominantly fixed income nature of the investment portfolio, the Company has minimal direct price risk. A 10% change in the value of the Company's equity investments (excluding warrants) would have a $869,643 impact on net assets, on an after tax basis.

Credit risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company.

All transactions executed by the Company in listed securities are settled/paid for upon delivery using approved brokers. The risk of this settlement not occurring is considered minimal, as delivery of securities sold is only made once the broker has received payment. Payment is made on a purchase once the securities have been received by the broker. The trade will fail if either party fails to meet its obligation. Since the Company invests in high-yield debt instruments and derivatives, this represents the main concentration of credit risk. The fair value of debt securities includes consideration of the creditworthiness of the debt issuer. The maximum credit exposure of these assets is represented by their carrying amounts. This maximum exposure may be offset to varying degrees in each investment, based on the collateral held, if any. Collateral may include such things as a general security agreement over all assets, or specific security over specific assets. It may also entitle the debt holder to take over the overall business through restructuring of the investment.

The Company's credit risk exposure by credit ratings on its investments is listed as follows:

	As a % of net assets	
	2012	**2011**
Credit rating		
BB+	4.4	-
BB	1.8	1.7
BB-	0.9	-
B+	8.3	-
B	6.0	37.3
B-	10.6	-
CCC+	30.3	-
CCC	3.1	23.0
CCC-	2.4	-
Not rated*	15.7	29.3
	83.5	91.3

* Unrated debt securities consist primarily of loans receivable.

Credit ratings are obtained from various credit rating agencies and sources. Where one or more rating is obtained for a security, the lowest rating has been used.

The Company's credit risk exposure by sector on its investments is as follows:

	As a % of net assets	
	2012	**2011**
Sector		
Consumer goods	8.4	7.5
Energy	49.8	50.4
Financial services	-	2.9
Forestry	6.2	6.9
Industrial/manufacturing	4.3	3.5
Materials and metals	13.7	12.2
Services	0.2	4.2
Technology	0.9	3.7
	83.5	91.3

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or fair values of financial instruments.

The Company invests primarily in interest-bearing financial instruments. As such, the Company is exposed to the risk that the value of such financial instruments will fluctuate due to changes in the prevailing levels of market interest rates. The table below summarizes the Company's exposure to interest rate risk by term to maturity:

	Fair value	
	2012 **$**	**2011** **$**
Maturity		
Less than 1 year	-	1,943,565
1 – 3 years	20,543,660	20,139,165
3 – 5 years	46,527,959	27,120,250
Greater than 5 years	42,639,891	70,113,075
	109,711,510	119,316,055

As at December 31, 2012, if the prevailing interest rates had been raised or lowered by 1%, assuming a parallel shift in the yield curve, with all other factors remaining constant, net assets could possibly have decreased or increased, respectively, by approximately $4,000,000, or approximately 2.8% of net assets (December 31, 2011 - $5,000,000, or approximately 3.5% of net assets).

Liquidity risk

As the Company is a publicly traded, closed-end investment company with a fixed number of common shares outstanding, unlike an open-ended mutual fund, it is not exposed to the liquidity risk associated with daily cash redemptions of securities.

Investments in fixed income investments may not be able to be liquidated quickly at an amount close to their fair value to respond to specific events such as deterioration in the creditworthiness of any particular issuer. Fixed income investments purchased by the Company may be subject to resale restrictions such as hold periods. The resulting values for fixed income investments may differ from values that would be realized had a ready market existed.

The Company actively reviews its investment portfolio, and the fixed income market, to assess liquidity risk on its holdings.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Company invests a portion of its assets in securities that are denominated in a currency other than the Canadian dollar, which represents the functional currency of the Company. Consequently, the Company is exposed to currency risk as the value of the portfolio securities denominated in currencies other than the Canadian dollar will vary due to changes in foreign currency exchange rates.

The Company enters into foreign currency contracts with financial institutions to hedge the value of foreign currency denominated investments. The fair value of these contracts is reflected in investments. Gains or losses arising from these contracts offset the gains or losses from translation of the underlying investments. The unrealized gains or losses are reflected in unrealized appreciation/depreciation on foreign currency contracts on the statement of operations. The potential impact to net assets of a 5% change in foreign currency rates against the Canadian dollar, assuming all other variables remain constant, would be $16,000 (2011 - $160,000).

9 Capital management

The capital of the Company is divided into voting and non-voting common shares, each having an unlimited authorized amount. The number of voting and non-voting shares outstanding and changes thereto, are outlined in note 3.

The Company manages its capital in accordance with the Company's investment objectives. The Company's investment objectives are to: (i) maximize the total return for common shareholders, consisting of dividend income and capital appreciation; and (ii) provide shareholders with monthly dividends targeted to payout a minimum of 75% of net investment income annually. Net investment income, in reference to the Company's dividend payments to shareholders, excludes any realized and unrealized capital gains and losses from debt securities in the portfolio and any income or loss not derived from debt securities in the portfolio. The Company commenced its dividend payments on June 30, 2009, making monthly payments of $0.0583 per voting and non-voting common share, or $614,322. During the year ended December 31, 2012, the Company made dividend payments of $7,371,869 (December 31, 2011 - $7,371,869).

The Company is committed to continue paying a monthly dividend of $0.0583 per voting and non-voting common share for the three months ending March 31, 2013, totalling $1,842,966 (note 11).

10 Comparison of net asset value per share and net assets per share

In accordance with Section 3.6(1) of National Instrument 81-106, the Company's net asset value per share, the net assets per share calculated in accordance with Canadian GAAP for financial reporting purposes, and an explanation of the differences between such amounts, are required disclosures in the notes to the financial statements. For investments that are traded in an active market, Canadian GAAP requires that bid prices be used in the fair value of instruments, rather than the use of the last traded price, as currently used for the purpose of determining net asset value. This change accounts for the difference between the net asset value and the net assets.

	2012 $	2011 $
Net asset value per share	13.58	13.49
Canadian GAAP adjustments	(0.08)	(0.06)
Net assets per share	13.50	13.43

11 Subsequent events

On January 4, 2013, the Company announced a monthly dividend of $614,322, or $0.0583 per common share, payable on each of January 31, 2013, February 28, 2013 and March 29, 2013.