

DEANS KNIGHT

INCOME CORPORATION

INTERIM MANAGEMENT REPORT

OF FUND PERFORMANCE

For the period from

January 1, 2014 to June 30, 2014

This interim 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 financial statements of the Company for the six month period ending June 30, 2014 (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, investment strategy, behaviour of financial markets, the availability and use of the tax attributes of the Company, the resolution and disposition of the CRA Matter (as defined herein) including the extent of the Potential Tax Liability (as defined herein), the anticipated receipt of the 2013 Tax Refund (as defined herein) and reflects the Company's expectations regarding the results of operations and performance 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, the liquidity and potential proceeds to be realized from the Remaining Investments (as defined herein), 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 that, prior to April 30, 2014, was focused on investing in corporate debt securities. The Company's assets are 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, foundations, endowments and pension funds.

Since making a special cash distribution ("**Cash Distribution**") on April 30, 2014, the Company has ceased all investing and portfolio activities, such that the Company's business now consists of: (i) attending to, and if necessary, litigating, the Canada Revenue Agency ("**CRA**") audit and, if applicable, the related tax appeal; (ii) divesting of the securities held in the Company's portfolio that were not liquidated prior to the Cash Distribution (the "**Remaining Investments**"); and, (iii) attending to any additional distributions to shareholders of any surplus cash and the eventual wind-up and termination of the Company thereafter.

Risk

The overall risks of the Company are as described in its annual information form of the Company dated March 6, 2014 (the "**AIF**").

Prior to the reorganization and change in the Company's business that occurred in 2008, as discussed in Note 1 of the Financial Statements, the Company had generated significant tax losses and other tax attributes as a result of its prior business activities. In its tax filings since the reorganization, the Company has taken the position that these losses and other tax attributes could be used to offset profits generated by the Company, thereby reducing its taxes payable.

On July 16, 2014, the Company received Notices of Reassessment ("**NORAs**") from the CRA for the taxation years 2009 to 2012, inclusive. In the NORAs, the CRA denied the use of certain tax attributes by the Company on the basis that an acquisition of control of the Company occurred and on the basis of the General Anti-Avoidance Rule in the *Income Tax Act* (Canada) (the "**CRA Matter**").

The NORAs indicate the Company's tax liability for the 2009 to 2012 taxation years to be approximately \$22.7 million or \$2.15 per Share ("**Disputed Amount**"), including arrears interest and penalties. If the CRA's position were to be followed by the Company in future years, the overall tax liability will continue to fluctuate depending on the profitability of the Company. Given the Company's financial results for 2013, the Company estimates it is entitled to a refund of \$1.1 million ("**2013 Tax Refund**") following the CRA's position. As such, the Company estimates its overall potential net tax liability to be approximately \$21.6 million, or \$2.05 per Share ("**Potential Tax Liability**").

Should the Company be successful in defending its tax filing position, the Disputed Amount will be refunded to the Company with interest. However, if the Company is unsuccessful, the recorded amount of the tax assets, if any, as well as such amounts claimed to date would be recorded as a charge to income.

On April 15, 2014, the Voting Shares (as defined herein) were delisted from trading on the Toronto Stock Exchange. As a result, the Company's shares are no longer traded in a public market, there is no active market through which the shares may be sold and there is no guarantee that an active trading market will develop. The lack of a market for the Company's shares may affect the price of the shares in any secondary market that may develop; however, there can be no assurance that an active trading market or secondary market will develop, or if developed, that such a market will be sustained at the price level of the net asset value per share.

Given the majority of the Company's business is now limited to attending to the CRA Matter, the resolution and disposition of this matter which is uncertain at this time, an investment in the Company may be considered to be speculative. Therefore, an investment in the Company is only suitable for investors who are looking for potential capital appreciation and are willing to tolerate volatility in the value of their investment.

Results of Operations

On April 30, 2014, the Company executed on its plan to distribute a substantial portion of its assets to holders of voting common shares ("**Voting Shares**") and non-voting common shares ("**Non-Voting Shares**" and together with the Voting Shares, the "**Common Shares**") of the Company through the payment of the Cash Distribution in the aggregate amount of \$102.7 million (\$9.75 per Common Share). The Cash Distribution was considered a return of capital to holders of Common Shares for income tax purposes.

Given the Cash Distribution, the net assets of the Company at June 30, 2014 (\$27,518,217 or \$2.61 per Common Share) were significantly lower than at December 31, 2013 (\$130,367,007 or \$12.37 per Common Share). The net assets of the Company consisted of the following components:

	June 30, 2014		
	\$	Per Common Share ⁽¹⁾	%
Remaining Investments ⁽²⁾	3,511,452	0.33	12.8
Cash and short-term deposits	1,274,500	0.12	4.6
Accrued income	54,004	0.01	0.2
Prepaid tax payment ⁽³⁾	22,690,000	2.15	82.4
Prepaid assets less accrued liabilities	(11,739)	0.00	(0.0)
	<u>27,518,217</u>	<u>2.61</u>	<u>100.0</u>

(1) Based on 10,537,263 Common Shares, including 10,191,592 Voting Shares and 345,671 Non-Voting Shares, as outlined in the notes to the Financial Statements.

(2) The details of the Remaining Investments are outlined in the Summary of Investment Portfolio below.

(3) The prepaid tax payment excludes the expected 2013 Tax Refund. The result of receiving this anticipated refund will be an increase in cash and short-term deposits and a decrease to the prepaid tax payment. Refer to the Taxation note to the Financial Statements for more detail.

December 31, 2013

	\$	Per Common Share ⁽¹⁾	%
Investments ⁽²⁾	65,659,396	6.23	50.4
Cash and short-term deposits	64,573,401	6.13	49.5
Accrued income	786,745	0.07	0.6
Prepaid expenses	41,370	0.00	0.0
Future income tax asset ⁽³⁾	180,000	0.02	0.2
Accounts payable and accrued liabilities	(873,905)	(0.08)	(0.7)
	<u>130,367,007</u>	<u>12.37</u>	<u>100.0</u>

(1) Based on 10,537,263 Common Shares, including 10,191,592 Voting Shares and 345,671 Non-Voting 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's net investment income, being interest for distribution purposes and royalty income less expenses, for the six month period to June 30, 2014 was approximately \$0.371 million (\$0.04 per share) versus \$4.077 million (\$0.39 per share). The decrease is the result of the Company liquidating the majority of its income generating investments in anticipation of paying the Cash Distribution. In addition, the Company also incurred \$3.897 million of realized capital losses in the period from the sale of all the liquid investments held in the portfolio, the exchange of debt securities for common shares of Mirabela Nickel, and the settlement of foreign currency contracts. Conversely, the sales resulted in the majority of the change in unrealized appreciation on investments of \$3.596 million.

Going forward, investment income is anticipated to be generated from the Company's investments in Skylink Aviation Inc. and the royalty stream it is entitled to from Rapid Eye Canada Inc. For the six months ended June 30, 2014, these investments generated \$243,647 of investment income.

In late June 2014, there were positive developments regarding the Company's investment in Mirabela Nickel Limited ("**Mirabela**"). As previously disclosed, in late 2013 Mirabela began a process to recapitalize, as it fell victim to a two year slump in the nickel market. Deans Knight worked for over 6 months as part of a debtholder group to restructure the nickel company. As a result, in late June, the Company was able to exchange the debt it held for shares in the restructured business along with a subordinated note with minimal value. The new shares were re-listed on the Australian Stock Exchange on June 30, 2014 and closed at a price of AUS\$0.04 per share. At AUS\$0.04 per share, the total value of the shares was approximately equal to the fair value ascribed to debt investment immediately before the exchange. The ultimate recovery on the initial debt investment will be determined by the value of the Mirabela shares.

There were no other significant developments to report relating to the Company's other Remaining Investments. The Company will continue to look for opportunities to sell the Remaining Investments as prudently as possible. Otherwise, the Company's business will be limited solely to attending to the CRA Matter and, if applicable, the related tax appeal, and attending to any additional distributions to shareholders of any surplus cash and the eventual wind-up of the Company.

CRA Matter

The Company, in consultation with its legal advisors, remains of the view that its tax filing position is appropriate, and intends to vigorously defend its position. As such, on July 24, 2014, the Company filed Notices of Objection to the NORAs. If the CRA does not reverse its ruling within 90 days from the date the Notices of Objection were filed, the Company intends to appeal to the Tax Court of Canada to defend its tax filing position.

The NORAs indicate the Disputed Amount to be approximately \$22.7 million or \$2.15 per Common Share, based on the aggregate reassessment amounts for the 2009 through 2012 taxation years, including arrears interest and penalties.

The Company has estimated the Potential Tax Liability to be approximately \$21.6 million, or \$2.05 per Share, being the Disputed Amount, totaling approximately \$22.7 million, less the 2013 Tax Refund of approximately \$1.1 million.

The Company has prepaid the Disputed Amount to the CRA to minimize any further interest from accruing. Should the Company be successful in defending its tax filing position, the Disputed Amount will be refunded with interest. However, should the Company be denied the deductions in full, the recorded amount of the tax assets, if any, as well as such amounts claimed to date would be recorded as a charge to income.

Recent Developments

Cash Distribution and Extension of Termination Date

On April 4, 2014, shareholders voted in favour of the special resolution authorizing: (i) the reduction in the stated capital of the Voting Shares; (ii) an extension of the termination date of the Company until such time as is reasonably practicable following the conclusion of the CRA Matter (as defined herein) or such other date as the Company deems appropriate on not less than 30 days' notice to shareholders; and (iii) the removal of the restrictions on business that the Company can carry on.

With these shareholder approvals, on April 30, 2014, the Company executed on its plan to distribute a substantial portion of its assets to shareholders through the payment of the Cash Distribution in the amount of \$9.75 per Common Share. Further, the Company is now limiting its business solely to attending to the CRA Matter, liquidating the Remaining Investments in a prudent manner with a view to distributing the proceeds of such Remaining Investments to shareholders as soon as reasonably practicable.

International Financial Reporting Standards

This reporting period represents the Company's first set of financial statements reported under IFRS. The statements include corresponding comparative financial information for 2013, including an opening statement of net assets as at January 1, 2013.

The Company's transition to IFRS is as outlined in the notes to the Financial Statements. More specifically, Note 11 of the Financial Statements outlines the Company's transition to IFRS and the related impact on the Company's equity and comprehensive income. This change has resulted in certain comparative figures in this management report of fund performance being updated to reflect the changes to the Company's financial statements.

Related Party Transactions

The officers and 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 administration, financial reporting and other ancillary services required by a public company, as well as investment management services related to the Remaining Investments, all as more particularly set forth in the Services Agreement between the Company and Deans Knight dated May 20, 2014 and available for review on SEDAR at www.sedar.com. Deans Knight is paid a nominal fee of \$10 per month, starting May 1, 2014, for the services it provides to the Company under the Services Agreement. Prior to that, and for the period January 1, 2014 to April 30, 2014, Deans Knight was paid a management fee computed 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 six month period ending June 30, 2014, management fees totaled \$554,701 (2013 - \$1,089,013). At June 30, 2014, \$20 (December 31, 2013- \$512,138) was owed to Deans Knight, which was unsecured and included in accounts payable and accrued liabilities in the statement of financial position, and is payable immediately.

A former director of the Company, who was no longer a director in 2014, is a partner at a law firm that provides legal services to the Company. During the six month period ending June 30, 2013, the Company incurred \$175,830 in legal services and disbursements received from this related party. At December 31, 2013, all amounts owing had been paid.

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⁾

	Six months ended June 30, 2014	Year ended December 31,				Period March 17 to December 31, 2009
		2013	2012	2011	2010	
	\$	\$	\$	\$	\$	\$
Net assets, beginning of year ⁽²⁾	12.37	13.58	13.43	13.60	12.21	9.12
Increase from operations						
Total revenue	0.11	0.96	1.10	1.10	0.94	0.62
Total expenses	(0.08)	(0.29)	(0.26)	(0.26)	(0.24)	(0.20)
Realized (losses) gains	(0.37)	(0.50)	0.44	0.36	1.82	1.25
Unrealized gains (losses)	0.34	(0.47)	(0.19)	(0.52)	(0.27)	1.21
Future income taxes	(0.01)	(0.21)	(0.24)	(0.15)	(0.16)	0.62
Total increase from operations ⁽²⁾	(0.01)	(0.51)	0.85	0.53	2.09	3.50
Return of Capital	(9.75)	-	-	-	-	-
Dividends ⁽²⁾⁽³⁾	-	(0.70)	(0.70)	(0.70)	(0.70)	(0.41)
Net assets, end of year ⁽⁴⁾	2.61	12.37	13.58	13.43	13.60	12.21

- (1) The information is derived from the Company's audited annual and unaudited interim 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, beginning of the period for 2009 reflect the net assets in the Company at March 17, 2009, after giving effect to the conversion of the convertible debenture and interest owing thereon and the issuance of common shares on the Company's initial public offering less total share issue expenses.
- (3) Net assets and dividends are based on the actual number of shares outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of shares outstanding over the period.
- (4) Dividends were paid in cash.

Ratios and Supplemental Data ⁽¹⁾

	Six months ended June 30, 2014	Year Ended December 31,				Period March 17 to December 31, 2009
		2013	2012	2011	2010	
Net asset value (000's)	\$27,518	\$130,367	\$143,065	\$142,178	\$143,880	\$128,930
Number of common shares outstanding (000's)	10,537	10,537	10,537	10,537	10,537	10,537
Management expense ratio ⁽²⁾	0.71%	2.21%	1.96%	1.90%	1.91%	5.51%
Portfolio turnover rate ⁽³⁾	-92.11%	25.23%	14.79%	79.90%	86.60%	36.69%
Trading expense ratio ⁽⁴⁾	0.02%	0.00%	0.01%	0.00%	0.01%	0.01%
Net asset value per common share	\$2.61	12.37	\$13.58	\$13.49	\$13.65	\$12.23
Closing market price – common share ⁽⁵⁾	n/a	10.01	\$12.69	\$11.84	\$12.54	\$11.40

(1) Management expense ratio is annualized and based on total expenses for the period and is expressed as a percentage of weekly average net asset values over the period. For 2009, this ratio is calculated from the date the Company began operating its business as an investment corporation, on March 17, 2009, to December 31, 2009.

(2) The Management expense ratio for 2009 includes offering costs for the IPO of \$6,268,800 less the offsetting related future tax benefit of \$1,692,500.

(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.

(5) Voting Shares were delisted from the TSX on April 15, 2014

Management Fees

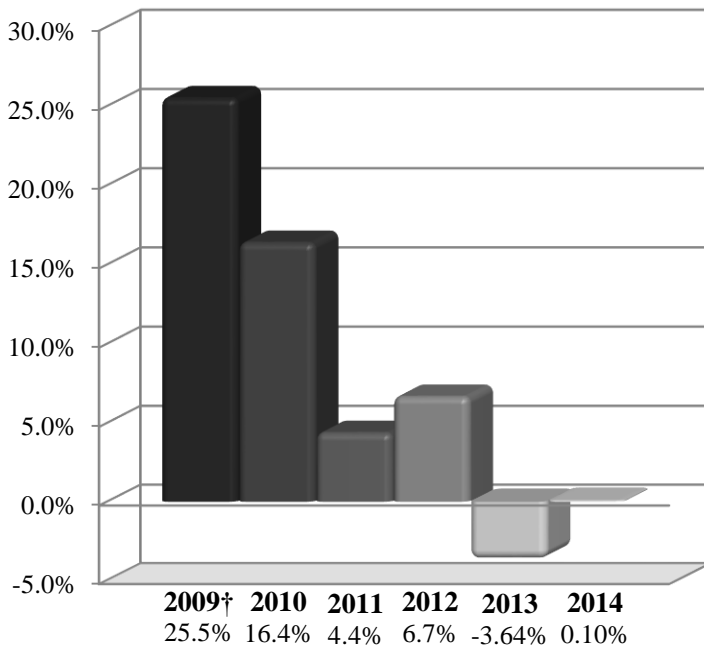
Deans Knight provides administration, financial reporting and other ancillary services required by a publicly listed company, as well as investment management services related to the Remaining Investments, all as more particularly set forth in the Services Agreement between the Company and Deans Knight dated May 20, 2014 and available for review on SEDAR at www.sedar.com. Deans Knight is paid a nominal fee of \$10 per month, starting May 1, 2014, for the services it provides to the Company under the Services Agreement. Prior to that, and for the period January 1, 2014 to April 30, 2014, Deans Knight was paid a management fee computed 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, 2012, 2013 and how much an investment made for the six-month period ending June 30, 2014. Given the Company has ceased all investing activities, other than liquidating the Remaining Investments, the return provided below for the six months ended June 30, 2014 of 0.10% is not necessarily indicative of what the return would have been for the period if the Company had continued to actively manage the investment portfolio.



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

Summary of Investment Portfolio

The following is a summary of the Company's investment portfolio as at June 30, 2014. This is a summary only and will change as the Company divests the Remaining Investments. A quarterly update is available at www.dkincomecorp.com.

Investments			% of Net Asset Value	Portfolio Composition	% of Net Asset Value
RAPIDEYE CANADA	0.020%	1-Jan-21	4.3		
SKYLINK AVIATION INC	10.000%	8-Mar-15	3.7	Fixed Income	
MIRABELA NICKEL LTD	0.000%	N/A	3.0	Canadian denominated in CAD	1.3
SKYLINK AVIATION INC	0.120%	10-May-18	1.3	Canadian denominated in USD	4.2
MIRABELA NICKEL LTD	1.000%	30-Jun-44	0.5	United States denominated in USD	-
CONIFEX TIMBER INC	0.000%	31-Dec-14	0.0	Other Foreign denominated in EUR	4.3
					9.8
				Equity and Warrants	3.0
				Investment Portfolio	12.8
				Cash & Short-term Deposits	4.6
				Other Net Assets	82.6
					100.0
				Sector Breakdown	
				Energy	-
				Materials & Metals	3.5
				Consumer Discretionary	-
				Forestry	-
				Financial Services	-
				Technology	4.3
				Services	5.0
				Investment Portfolio	12.8
				Cash & Short-term Deposits	4.6
				Other Net Assets	82.6
					100.0