# VERTEX BALANCED FUND

## Fourth Quarter Report, 2000

It is the beginning of a New Year and time to reflect upon what happened in Two Thousand. Last year was like any other. The greedy got separated from their money just like they have for centuries so it would be a waste of your time to bla bla bla on in a play by play fashion about that. Reflecting done, let's spend some time on what is happening right now.

The fed just, and I mean literally just, lowered rates by half a point and stocks, especially the tech stocks, have shot up. In fact the NASDAQ index closed up 14% today. That's right. Today. That should just about do it for NASDAQ this year. The NASDAQ is heavily weighted in companies where interest rate cuts won't make much of a difference. These firms have technically worked on a barter system for years, trading expensive stock for companies, goods, services and people. They have low or no debt, and very little in the way of PPE (property, plant and equipment). Assets are instead in PPI (people, patents and ideas). Where tech companies do have debt, it trades as junk with yields so high as to make the fed funds rate irrelevant and Cheech and Chong look sober. The companies benefiting most from rate cuts are financials, where the spreads between money lent and money borrowed widen, increasing profits. This is offset somewhat by delinquent loans as the economy slows and people decide not to make good on their promise to pay back the bank and make good the promise made to friends about screwing the big bad bank anyway.

Where rate cuts help the most though is at the consumer level. Mortgage rates, personal loans and so on. Even with cheaper money, people are not going to buy a whole lot more technology this year. The world has been on a bit of a technology binge and has got a slight case of indigestion. When you've got enough, enough is enough. Thus prices for many technology companies are still way too high in relation to their lack of earnings and interest relief isn't going to help.

Readers having come this far deserve some real insight. OK fasten your seatbelt. The Fed rate cut was not made to save the NASDAQ but to save the economy. After two years of fighting the NASDAQ the fed realized that they had only crippled the beast but killed an economy in the process. Now this is where it gets really interesting. Remember bonds? Acting like a wise professor, the bond market had correctly predicted the outcome of Greenspan vs. the NASDAQ a year ago and had taken long-term interest rates from close to 7% to just over 5% resulting in double-digit returns. Meanwhile, the equity market still had the gas pedal to the floor even after it went off a cliff and any of you familiar with physics will note that depressing a brake pedal once airborne has a certain element of futility. Now the fed is behind the wheel and having released the brake is pressing on the gas pedal. Unfortunately, the rod behind the pedal might have turned to rope and those of you familiar with rope will note the futility of pushing on it.

That said, there are three possible scenarios we are willing to consider, the first is of a soft landing, the cliff is not too high and the landing is in water. The second, a harder landing, picture a larger cliff over water or a smaller cliff with no water. Both have roughly equal impact using Newtonian physics. Without getting into great detail, under the first scenario bonds should rock, under the second they'll go platinum. Our spider senses are tingling and telling us the bond market is where the juiciest insects are hanging out. On the equity front, there have been a lot of casualties and many of the wounded over the last few years are showing signs of life. Take for example Mattel, 3M, Ingesoll Rand, Caterpillar, Cummins Engines. Even forest products look interesting after being starved of capital for three long years. These companies have grown at the rate of cool molasses but investors are beginning to realize that molasses is pretty tasty. I will conjecture that most companies growing faster have unsustainable business practices, or are cooking the books.

Oh, the other scenario? The repeat of last year's "tech stocks at any price" show? There is not that much money around and I have too much respect for humanity to believe we'll revisit those shenanigans again so soon.

Finally, the investment plan for 010101 (it's the year of "binary code" in the Chinese calendar) is to own a few more bonds than last year. For the equity markets to rally significantly lower rates are necessary. Oil and gas prices are still very high. High energy costs replicate high taxes and interest rates. It is necessary for rates to come down and bonds will be the first beneficiaries. Some of the companies mentioned above may make it into the portfolio this year if they can prove themselves more worthy of ownership than those already in your fund.

**The Portfolio**

The top 10 holdings at December 31st were as follows:

| | |
|---|---|
| C. I. Fund Management | Avista Corp. |
| Fairfax Financial Holdings | Investors Group |
| United Technologies Corp. | Talisman Energy |
| Sun Life Financial Services | CIBC |
| Olin Corp. | Royal Bank of Canada |

**Asset Mix**

| | |
|---|---|
| Cash | 0% |
| Fixed Income | 40% |
| Canadian Equities | 37% |
| Foreign Equities | 23% |

**Performance**

We are pleased to report that the Vertex Balanced Fund returned 26.22% for the year ended December 31, 2000.

| | Net Asset Value | Rate of Return | | | | |
|---|---|---|---|---|---|---|
| | | 1 Mo. | 3 Mos. | 6 Mos. | 1 Year | 2 Years |
| **Dec. 31, 2000** | **$13.16*** | **5.48%** | **5.68%** | **10.93%** | **26.22%** | **20.34%** |

* Post Distribution