VERTEX BALANCED FUND

Year End Report 2005

Just for a minute there I dozed off and dreamt it was beaming with sunshine and the Balanced Fund was up 50% and money was pouring in and…and my phone was ringing off the hook with happy clients querying as to the source of our genius. Suddenly I'm startled back to reality when my phone rings and it's a disgruntled client asking why he's got a distribution of 13% when his fund was up a mere 5% and…and the only thing that's pouring is buckets of rain outside as it has been for almost a month in Vancouver. Ah such are the lows of money management.

A trend follower would notice that this fund has gone from above average from 1998 through 2003 to average in 2004 to below average in 2005 and if one were a trend follower, the only logical course of action would be to sell this pathetic excuse masquerading as a balanced fund and be done with it. Having stated these irrefutable facts I will spend the next few pages presenting arguments for why this course of action would be a mistake. In this undertaking, I'll try to avoid philosophical trickery and surreptitious attacks on the character and competence of the competition however tempting.

<u>Argument #1</u>

Safety and Risk: Few readers ride motorcycles. One of the reasons we stay away from these machines is a high probability of ending up dead. For most of us this high probability of death trumps the thrill of riding fast and free. Your balanced fund does not ride fast and free. The risks of significant loss are too great. The stuff that's gone up most in recent years is likely going to fall the most in future years or at the very least, it will cease going up. With rare exception though, the higher they climb, the harder they fall. It's human nature to underestimate risk when markets are up and overestimate risk after a drop. Conclusion: To avoid financial death – don't sell - **buy** more Balanced Fund!

<u>Argument #2</u>

Commodities: We are somewhere in between the beginning and end of one of the greatest commodity bull runs in history. All that's known for sure is that it began in 1999 and went ballistic in 2005. This served to drive the stampeding masses into purchasing commodity stocks. In order to fund their purchases, traders and speculators had to sell something. Considering no one holds cash or bonds anymore (a peculiar development in its own right considering our aging population), stocks of other companies had to be disposed of. This served either to hold price rises of these stocks in check, or cause a fall. Always looking for a bargain, your penman was willing to take the opposite side of this arrangement and bought stocks deemed inexpensively priced. Conclusion: Balanced Fund is bargain priced – buy more Balanced Fund!

Argument #3

Canada: Canada has become one big commodity trade. Our stock exchange, our currency, our economy is now terminally infected with commodititis. According to government stats, Canada is operating at full capacity. There are, however, only three sectors that are performing: 1. commodities 2. financials (those selling and trading commodity stocks) and commodity income trusts, and 3. construction – this sector benefiting from both low interest rates and the wealth being generated from the latter two sectors which in turn has been generated from commodities. Basically, it's all commodities. With this in mind, your balanced fund has positioned itself as the antithesis of the Canada centric commodity play. With almost 45% of the Vertex Balanced Fund invested outside of Canada, 100% invested in companies with no commodity exposure, this fund is an excellent diversifier from what most of us would be loaded up with in the bulk of our investment portfolios. The time to move more investments into Canada was back when Diane Francis was telling you to get your money out – back when our debt to GDP was a big issue. Now the USA has the debt to GDP issue. The tables have turned – they will turn again. Doing the obvious rarely produces sustained returns. Conclusion: To avoid group think and concentration risk in your portfolio – buy more Balanced Fund!

Argument #4

Currency: Over the past three years, your fund has withstood a tremendous rise in the value of the Canadian dollar over the US dollar. Let me explain. Even while holding between 30% and 45% US dollar exposure when the US dollar has fallen 30% against our dollar, your fund has performed very well. Consider what returns might look like if currency ceases to be a headwind let alone what returns might look like should it become a tailwind. The USA is the largest, most transparent market in the world. It's not going to go away any time soon. There's nothing in Canada that can compete with the GE's, Honeywells, Boeings, Microsofts and the thousands of other global powerhouse companies in the USA. The lower the US dollar goes the more these firms will earn on a translated currency basis. One should have exposure to this market and this currency in a well diversified portfolio especially when everyone worldwide hates it. Conclusion: Buy more Balanced Fund.

Argument #5

Yield: Over time, it has been documented that reinvested dividends and interest is the source of true long-term wealth. Simple compounding generates spectacular returns over a long investment horizon. Your balanced fund has a shockingly high yield. When including all sources of yield; dividends, option writing income, bond interest, and securities lending income, your fund is churning out a yield of over 5% - this despite bond yields being below 5%. To increase your compound return – buy more Balanced Fund.

Argument #6

Do the opposite: This argument might be somewhat in conflict with the last sentence in paragraph #2 but ask your self this question: "Self - how have my friends and neighbors been making money in the last few years?" Chances are it has been from oil stocks, coal stocks, nickel stocks, zinc stocks, gold stocks, and income trusts. Aren't these the same people who were making money in tech stocks in the late nineties? Personally, I don't want to be anywhere near these people or their investments when the inevitable correction happens. There are so many great companies to own that are inexpensive, profitable and won't be affected by the panic selling following every speculative frenzy. It's even more dangerous when everyone believes stocks of companies that have gone up two to five times in a very short span of time represent value because after all, these stocks, "they're not like technology stocks". They're right - Cisco, Microsoft, Intel, Oracle, Dell and many other technology companies have had free cash flow over an entire business cycle. They have very low debt, clean balance sheets and are buying back more stock than they issue. Few commodity companies produce net free cash flow over a cycle. In fact, few commodity companies are producing free cash at the top of the cycle!! Even fewer are buying back stock. In fact the majority are selling shares to the public at a rate that made the technology craze look not so crazy. Sorry folks, stocks are stocks – crazes are crazes. Conclusion: Sell your other stuff before it drops and buy the Vertex Balanced Fund before it goes up again!

Finally, there was a big distribution in the fund due to capital gains realized in 2005. This distribution was automatically reinvested in additional units at the post distribution price. You will notice that your book value has increased and you now hold more units than prior to December 31st. Discipline forces us to sell stocks where price to value has gone beyond that of competing companies or the market. Proceeds were then reinvested in firms where price to value was far below competitors or the market.

PERFORMANCE

	Rate of Return (Class A)					
Net Asset Value	**3 Mos.**	**1 Yr.**	**2 Yrs.***	**3 Yrs.***	**5 Yrs.***	**Since Inception***
$13.4756**	**-0.66%**	**5.19%**	**8.13%**	**12.10%**	**7.45%**	**10.12%**

*Annualized
**Post Distribution

THE PORTFOLIO

The holdings in the Vertex Balanced Fund at January 13th, 2006 were as follows:

Fairfax Financial Holdings	Bank of America	Odyssey Re
CIBC	Enerflex Systems	CTS Corp.
Mattel Inc.	Partner Re	Seamark Asset Mgmt.
BCE Inc.	Kemet Corp.	Laurentian Bank of Cda.
CI Fund Management	Harleysville Group	Sceptre Asset Mgmt.
Angiotech Pharmaceuticals	Montpelier Re	Vishay Intertech Inc.
Saxon Financial Inc.	Merck & Co.	Cisco Systems
XL Capital Ltd.	Level 3 Comm.	

ASSET MIX

Cash	1%	Canadian Equities	35%
Fixed Income	24%	Foreign Equities	40%

Vertex One Asset Management