

VERTEX BALANCED FUND

Third Quarter Report 1998

This is only the second quarter for the Vertex Balanced Fund and a most interesting quarter to say the least. The TSE 300 Index fell 23.5% and the Dow Jones Industrial Average fell 9% when measured in Canadian dollar terms. Bonds performed best with a return of 2.5%. Finally, after many years of stellar equity returns we are once again reminded of the benefits that come from owning bonds and why maintaining balance is so important.

The Current Scene

Walking down any main street in Canada you will notice that the banks, that proudly displayed their mutual fund returns, have now removed all advertising relating to these funds and replaced it with GIC rate charts. Newspaper headlines focus on Russia, Asia, Latin America and "The Global Crisis". You may recall in our last report we talked about the euphoria that had become so pervasive in the minds of investors. Well, euphoria is out and depression is in. Investment sentiment has clearly shifted. Companies that have shown strong earnings recently have continued to suffer poor stock prices. No one knows whether the economies of America and Western Europe will fall into a recession and if they do, to what magnitude and how long it might last. In Canada, with a sell-off of 32% from its high, the market has already predicted a recession. Getting back to Russia, Asia, et al, if you think back only 10 years, these economies were insignificant and maybe they are less significant than we think today. For example, America does more trade with Canada than the whole of Latin America combined. Japan, which until recently acted like an ostrich with its head in the sand, is showing signs of dealing with their troubled banks. Thus, contrary to the media, our view is that the world is not going to blow up and opportunities to greatly enhance the return of your fund are starting to present themselves. We are very excited about the future.

The Portfolio

Our first job as investment managers is to find excellent companies that have consistent earnings and strong financial positions. The fund now holds 13 of these companies representing 25% of the portfolio total. Although there is less risk in stocks than at the beginning of the quarter, bonds still look very attractive on a risk adjusted basis. In line with this view, 60% of the total portfolio is invested in long dated Government guaranteed bonds with the balance in money market instruments. Over the next few months we foresee increasing investments in companies with high dividends and low debt at low price to value ratios. For example, CIBC was added to the fund during the quarter. CIBC now has a dividend yield over 4% and on a tax-adjusted basis provides a return higher than current five-year term deposits. The objective of concentrating on these types of companies is to get paid while owning them in the event that the market continues to misbehave.

Performance

The fund produced a return of -8.54% for the quarter. It is always unpleasant to write those negative numbers. Fortunately, it is seldom that markets behave as in the past quarter and your fund performed strongly relative to other Canadian balanced funds.

Fund Unit Value

The fund opened on April 3rd of this year with a value of \$10.00 per unit. Monthly unit values can be found in most papers under the mutual fund heading "other funds" and also on our web page at www.vertexone.com

<u>1998</u>	<u>Net Asset Value</u>	<u>Monthly Return</u>
April 3	\$10.00	
April 22	\$9.92	-0.79%
April 30	\$9.78	-1.43%
May 31	\$9.94	1.64%
June 30	\$10.22	2.79%
July 31	\$10.12	.90%
Aug 31	\$8.94	-11.70%
Sept 30	\$9.34	4.51%
Return since inception		-6.56%