

# VERTEX FUND

## First Quarter Report, 2003

### Canada – you rock!

This quarter ended with over 90% of the Fund's assets in Canada – an all time high.

As the US economy weakens, the Federal Reserve has combated this weakness with dramatically lower interest rates while Canada has taken the opposite course of increasing rates. This difference is apparent in today's yield curve with a two-year Canadian Government backed bond paying 2.25% more than its US counterpart. One can now hedge this currency differential for a cost of 1.5% yielding a risk free return of .75%. Although this trade does not appeal to us, as one needs to use a fair amount of leverage to make it worthwhile, it does show the huge buying power potential for Canadian dollars. Canada does not have enough dollars or bonds in circulation to satisfy global demand for this trade. Additionally, the Chinese economy will steam roll ahead with 8% GDP growth in 2003. This will lead to continuing strong demand for Canadian natural resources on its road to industrialization. More demand than supply equals a rising dollar.

Canada's other big advantage is that we are getting American religion when it comes to tax cuts. Alberta is leading the way with British Columbia and Ontario running as fast they can to catch up. Here is a list of the extraordinary changes from Canada's most advanced province, which has also promised to eliminate provincial personal income tax.

#### Corporate Tax Rates –Federal and Alberta Prorated for April 1 average

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Federal %	28	27	25	23	21
Alberta %	<u>16</u>	<u>14</u>	<u>13</u>	<u>12</u>	<u>11</u>
Combined %	44	41	38	35	32

A 27% reduction in taxes will go straight to the bottom line for that Oil and Gas based economy in the Rockies. United States' natural gas production has now declined for six quarters in row while Canada has seen its production of gas exports decline for the first time in 15 years. This is the first time that pipeline capacity is available for Canadian companies to increase production. The problem is that we don't have any excess gas to ship. The Western Canadian sedimentary basin is mature while storage levels in the US are at all time lows - over 40% below levels at this time last year. New wells are being drilled deeper than ever before to squeak out those last fumes. It might be a perfect time to rip out that gas fired water heater and switch to electric. In this environment even oil looks strong over the long term.

Over the quarter, the Fund was down slightly even though fairly strong returns came from merger arbitrage. More deals have attracted us recently and we have doubled our weight to 40%. Our performance was hurt primarily by long positions in Pan American Silver which was an unhedged merger arb position. We have decided to maintain this position because of our bullish stance on precious metals and our negative view of the US dollar. The other long position that hurt us over the quarter was Extencicare. Extencicare is a North American nursing home provider that will do well regardless of the economic environment. It trades at two times cash flow with both insiders and the company treasury buying back stock. In a rare move, the company also purchased its own bonds at a discount. Both these moves enhance shareholder value leading to our view to seeing a significant reward over the long term.

The headlines are screaming about Air Canada's decision to file for creditor protection on April 1, a fitting date for the fools that run this airline. We have maintained our short (even though the borrow has been difficult) since we last mentioned this name nine months ago and will wave goodbye as it slips down the tarmac. Air Canada is doomed for all time and may yet go bankrupt one more time if it escapes out of the current bankruptcy filing. The only profitable business models that now exist belong to WestJet, RyanAir, JetBlue and Southwest Airline. Southwest now has a market capitalization greater than all US airlines combined. If you run an airline any other way you will get bulldozed - or as Warren Buffett said, "If a capitalist had been present when the Kitty Hawk took to the air for the first time, he would have shot it out of the sky."

The Globe and Mail in February ranked the Vertex Fund the number one fund in Canada over five years among the Alternative Investment Category and we look forward to the next five years.

<b>Net Asset Value</b>	<b>Rate of Return</b>					
	<b><u>1 Mo.</u></b>	<b><u>Year to Date</u></b>	<b><u>1 Yr</u></b>	<b><u>2 Yrs*</u></b>	<b><u>3 Yrs*</u></b>	<b><u>5 Yrs*</u></b>
<b>\$23.9173</b>	<b>-2.37%</b>	<b>-0.71%</b>	<b>-8.75%</b>	<b>3.15%</b>	<b>5.65%</b>	<b>17.33%</b>

\*Annualized

We would like to remind you of two accounting notes in the Vertex Fund. The Fund, as a Unit Trust, made its first distribution at year-end of \$2.16, which was re-invested in new units for each unitholder. In addition, when Vertex Fund Limited Partnership units were exchanged for new Vertex Fund units on January 2, 2002, the result was a deemed disposition. Holders of the Vertex Fund L.P. must declare a sale of the units and calculate a capital gain/(loss) for 2002 tax reporting. A letter was sent to you earlier this year stating your Adjusted Cost Base (ACB) for this purpose.