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VERTEX FUND

Second Quarter Report, 2010

The whole problem with the world is that fools and fanatics are always so certain of themselves, but wiser people so full of doubts."

- Bertrand Russell

After this last quarter of performance it's easy to doubt oneself. After not having a down month in 17 months we had two down months back to back. It is only fair that we take a breather and a few steps back after such a strong march up. But it's also key to remember that when we manage your money, you pay us to panic for you, so you don't have to.

In October 2008 we panicked and eliminated most of our equity exposure and moved into bonds and merger arbitrage. We have continued to maintain our weights in bonds, high yielding stocks and merger arb as we believe over the next two years this will be the best place to earn continued strong returns. Our distrust of the stock market and our negative bias against stocks from the past year and a half continues.

It's ironic that the plume from that big ash hole in Iceland shut down air traffic in Europe like the gods spreading financial mistrust from the epicenter of poor banking in Europe. The silver lining to the cloud is that our portfolio has a large notional exposure to gold and silver through options and warrants with less than 2% underlying exposure to the portfolio. This could represent 20% of our portfolio if precious metals continue to surge as mistrust of the printing presses becomes a mainstream thought. Also, today's money management industry puts massive pressure on portfolio managers to reduce volatility and focus on relative performance. We have always maintained it's better to deliver a lumpy 18% per annum than a smooth and consistent 8% as long as you understand the risk of the portfolio. Everyday we start our day trying to reduce risk in our portfolio but not necessarily volatility. Volatility in the short term is hard on stomachs and nerves but in the long term will deliver better investment returns. Investment policies suffer from a tendency to equate volatility with risk and an indifference to whether assets are cheap or expensive.

This quarter saw, what seems a long time ago now, the European Central bank work out a trillion dollar rescue package for its failing states. We think it took so long for this package to come out as Monsieur Sarkozy must have been restricted to a 35 hour French work week. A severe recession is the only thing that can change the welfare states of Europe. Now a similar package might soon be on the way for various U.S. States that are essentially bankrupt (California and Illinois to name a couple).

We continue to be very skeptical of all government debt and focus only on corporations whose balance sheets we can study and see free cash flow to service the debt versus governments that can't. Barron's said it best recently: "Basically, the Moody's default rate on speculative-grade bonds has receded to just 2.03% over the past three months (was 12% a year ago) and yet the compression in spreads has not fully priced in that development as this is a default rate historically consistent with a spread over Treasuries of 417 bps versus today's actual gap of 710 bps. In fact, when the default rate was at current levels back in June 1997, the spread was at 267 bps (*i.e.*, very expensive at that time, but cheap this time), acknowledging we are in a more tenuous economic environment now. Then again, corporate balance sheet ratios are stronger today." Hence our continued love for fixed income investments.

Merger arbitrage returns were considerably more attractive in the second quarter. Arbitrageurs who were previously overpaying (in our view) for the upside option of competing bids, became more risk-focused and spreads widened out accordingly during the May equity market sell-off. In addition, several large merger situations with exposure to oil and gas exploration and production in the Gulf of Mexico (SII/SLB, ME/APA) came under heavy selling pressure as a result of the uncertainty created by the BP Deepwater Horizon disaster. As a result, we were able to deploy significant amounts of capital at attractive rates of return in our merger arbitrage strategies this quarter. As the quarter drew to a close, the benchmark $25 billion acquisition of XTO Energy by Exxon Mobil was completed. With merger arbitrage capital from this transaction being redeployed into a smaller universe of deals, as well as somewhat less uncertainty emanating from the Gulf of Mexico, merger arbitrage spreads have again tightened to less attractive levels. However, we have recently found some compelling risk/reward opportunities in certain fixed income instruments related to merger situations and we have been increasing our exposure in this area as a result.

As always please call us if you would like more details on the previous analysis.

PERFORMANCE

The Vertex Fund (Class A) returned 34.47% for the year ended June 30, 2010.

	Rate of Return (Class A)					
Net Asset Value	**1 Mo.**	**3 Mos.**	**Year To Date**	**1 Yr.**	**5 Yrs.***	**Since Inception***
$61.7546	**-2.54%**	**-8.87%**	**0.34%**	**34.47%**	**10.21%**	**18.61%**

*Annualized

Past performance is not indicative of future results
All data are based on the Class A unit values

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