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VERTEX FUND

Third Quarter Report, 2010

QE2 = Ag

Does QE2 (part II of quantitative easing) have a silver lining? It's been two years now since the credit crunch started the ball rolling. With this morbid anniversary still fresh in our minds we had the same nervousness in the markets of May and June this year and just like "Déjà vu", we now have had one of our best months in September just like the months following 2008. In this kind of market, trends remain strong as they have set the tone for the future. All assets are rising. Stocks, bonds and gold (silver) are hitting highs, while interest rates are hitting all time lows. Two year bonds in the U.S. now yield .43% with Canadian bonds sporting a massive 1.4% for the same term. The safest asset classes are having the biggest moves this year, while gold has hit an all time high and silver has hit a shorter term high. I think John Paulson said it best recently:

> "The price of gold has moved in correlation to the monetary base for as long as they have tracked the two data items. As the Fed prints more money, gold should rise. If the Fed were to increase the monetary base by 100% over the next three years, gold should increase by that same amount. Additionally, as inflation accelerates, investors tend to push gold higher than its correlation, like in 1980 when it increased an additional 100% above the correlation. So if gold is at $1,200 now, it should hit $2,400 on the monetary expansion alone, then $4,000 as investors flee inflation"

We're not sure if this forecast will become fact but we think we have a great investment hedge by owning convertible bonds on gold companies. This allows us to clip current coupons that help maintain the current yield of the Vertex Fund at ~6% while getting exposure to a larger rate of return if gold does continue to be the "go to" investment with minimal downside.

The silver lining with quantitative easing (QE2) (which is a great way of making "printing money" sound intellectually correct) is that it acts as a backstop for our investments. As you print cash everything (stocks, bonds and gold) rises in value. This quarter we sold the last of our AIG bonds which were technically owned by the US government, so when they were yielding 40% it seemed like a bit of a gift owning these bonds instead of buying US treasuries yielding 4% as we could get a tenfold return in yield. Now that the bonds have tripled in price and the US government is working on an exit of its investment we think it's a great time to say AI - see YA.

High yield is the best investment in disinflationary times like today but what keeps us up at night is the threat of inflation, so we continue to be big believers in hybrid bonds that will allow for increased coupons as inflation rises along side of interest rates. These bonds trade in increments of a million dollars so a fund of our size is the best way to get exposure to this market with proper diversification. Our favorite hybrid bonds are TD Bank, Great West Life and Wells Fargo.

In looking forward, we also need to reflect on our largest single return since the inception of the Fund which was our $5 million investment in Athabasca Oil which became more than a $100 million profit. We recently invested just over $7 million with the same management team in their brand new company called Canadian International Oil focusing on oil in the Bakken formations. If the past results are an indication of the future it should be a wild ride.

Merger activity was robust in the third quarter, highlighted by two large Canadian deals: Kinross' friendly bid for Red Back Mining and BHP's hostile bid for Potash Corp. We also saw continued activity in the US with Sanofi's proposed acquisition of Genzyme, Aon Corp's purchase of Hewitt Associates, and Intel's acquisition of McAfee. These five deals alone represent $80 billion of equity market value. There was sufficient uncertainty surrounding the Kinross shareholder vote in the Red Back transaction to afford us several opportunities to enter the spread at attractive levels. Additionally, some risk-mitigating activities we undertook in the options markets contributed to our healthy return from this deal.

We have been active in several Australian situations that have offered highly compelling risk/reward opportunities. After being hurt earlier this year by failed deals (partially as a result of the proposed resource super profits tax), arbitrage capital had been fleeing the region. When the acquisition of Centennial Coal was announced in July (where the buyer was fully aware of the super profits tax) it traded at an inordinately attractive spread. After conducting extensive due diligence (late nights in Vancouver, not a trip to Bondi Beach unfortunately) on the likely outcome of the Foreign Investment Review Board's perspective on the transaction, we became comfortable with the risks involved. The transaction was approved in September and is on track to close sooner than expected (despite a prolonged Australian election result).

Also notable in the third quarter was one of the most dramatic bidding wars we have seen in recent memory - Dell and HP's battle over 3Par. After numerous rounds of bidding, HP may have "won the battle" for the company, but by paying a 200%+ premium it remains to be seen if they "won the war". As a result, we have seen some subsequent deals, particularly in the technology sector, trade at unattractive levels as expectations for subsequent bids are unrealistically high. We expect merger activity to continue to be strong as financing remains widely available to acquirers. It is interesting that the high yield bond market is willing to support an LBO-style purchase of Pactiv ($4.4 billion market cap) with virtually no equity cheque. The benchmark deals in the US, Merck KGaA for Millipore and Schlumberger acquiring Smith International, closed in the quarter.

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

PERFORMANCE

The Vertex Fund (Class A) returned 21.65% for the year ended September 30, 2010.

	Rate of Return (Class A)					
Net Asset Value	**1 Mo.**	**3 Mos.**	**Year To Date**	**1 Yr.**	**5 Yrs.***	**Since Inception***
$67.1596	**5.09%**	**8.75%**	**9.12%**	**21.65%**	**9.60%**	**18.99%**

*Annualized

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

Vertex One Asset Management