1920 – 1177 West Hastings Street
Vancouver, British Columbia V6E 2K3
www.vertexone.com
Phone: 604-681-5787
Fax: 604-681-5146

VERTEX FUND

Fourth Quarter Report, 2013

This year Noel Dattrino, who leads our retail sales department, recommended *Christmas Vacation* staring Chevy Chase to us as his favourite Christmas film. Now, everyone has a favourite and of course Jimmy Stewart is tough to beat, but Christmas Vacation was oddly appropriate for this year. The climax of this 80s film is the hundreds of lights used to light-up the roof of the Griswold's house. At the time, this was considered so over the top that it was comical. Today, like most things in life, "over the top" has become the mainstream. Now it's common to see one tree lit up in a home or mall that has more lights than Chevy Chase used in his entire display. Financial markets are over the top as well. Just off the top of our head some examples are:

- The global monetary authorities printing trillions of dollars
- The Chinese Central Committee ordering one billion more babies
- The average CEO pay rising from 20 times the average worker in 1965 to 270 times the average worker in 2013
- Japan deciding it should just print money to rid itself of deflation
- US companies spending $700 billion to buy back stock but only paying out half of that amount in shareholder dividends
- GMP Capital risking more than its entire capital base to do a deal for Barrick Gold
- Bitcoin rising 100 fold to be followed by Peercoin, Litecoin, Novacoin, Feathercoin, Primecoin, and Megacoin just to name a few…

These "over the top" times of course have meant that America is leading the world in equity returns, which in turn has meant that all of Vertex One's funds had double digit returns in 2013. The Vertex Fund was right in line with its long term return posting a 16.30% gain during the past 12 months. As the Vertex Fund grows we are focusing on reducing volatility and we think that on a risk-adjusted basis the fund's returns were the best ever in 2013. In this light of less equity risk, we have also recently launched the Vertex Arbitrage Fund which takes the traditional third that we allocate in the Vertex Fund to merger arbitrage and offers investors full exposure to this low-volatility strategy.

This year we did everything in one-thirds: one third of our exposure was in Merger Arbitrage, one third in Fixed Income and one third in Equities - with an additional third of that hedged with short sales. We also had about one third of our US dollar exposure unhedged just after we told you last quarter that we had given up reducing our dollar hedges. You can call us "Flip Flop" Asset Management from now on if you like...luckily this time though the Canadian dollar finally started to weaken and we expect that to continue in 2014.

Our returns this year were buoyed by our position in Deckers Outdoor, Blackstone and Legg Mason but they were also lessened by us selling our Fannie and Freddie Mac preferred shares which of course rose over 15 times this year after we sold them in 2012. Ugh!! On the fixed income side we reduced our exposure to Royal Bank of Scotland after many years of gains which, amongst other wins this year, resulted in you receiving a capital gain at year-end of slightly over 5% of the NAV. We also tried to book a loss in everything that didn't work out so that we could reduce the taxable gains.

The merger arbitrage side continued to produce solid risk-adjusted returns in the quarter. A significant component of the performance this quarter came from our short position in Cooper Tire. It is not uncommon for us to short takeover targets (in friendly, announced mergers) where we believe the market is mispricing the likelihood of the transaction not being completed. Typically, we might have 1-2 short positions (anticipating deal failure, separate from our short positions to hedge deals we expect to close) in the arbitrage portfolio at any given time (relative to roughly 30 positions in total).

Cooper announced a friendly merger with Apollo Tyres Ltd (an Indian tire manufacture) in June for $35 a share. We initially stayed away from having a long position in the situation because we were cautious on the buyer (this would have been the largest ever US acquisition by an Indian company) and it required an aggressive financing package. As the summer evolved and we did more work, several more events heightened our disdain for the transaction. Cooper badly missed earnings, the United Steelworkers filed grievances as a result of the merger, the Indian rupee weakened substantially, there were rumblings of discontent at Cooper's Chinese joint venture, and Apollo's own share price suffered a dramatic drop. While unsure of the exact turn of events that would lead to the deal collapsing, we felt there were enough strikes against the deal to warrant a short position. The deal collapsed in October when it became apparent that Cooper no longer had control of their Chinese JV and wouldn't agree to a price cut (we're dramatically oversimplifying here). We covered our short position for a profit in October at approximately $25.

While the Cooper deal demonstrates the risks in merger arbitrage, we should note that it was an exceptional situation. In our universe of hundreds of North American merger situations in 2013, only two failed: Cooper Tire and Ebix, Inc. (an aggressive leveraged buyout of a company with a very checkered past, we had no position).

We wish you many happy returns in 2014!

PERFORMANCE (Class A shares as at December 31, 2013)

Net Asset Value	**1 Month**	**3 Month**	**Year to Date**	**1 Year**	**5 Year+**	**10 Year+**	**15 Year+**	**Since Inception+**
$69.7757*	2.49%	6.40%	16.30%	16.30%	21.00%	11.57%	17.37%	16.70%

+annualized returns
*post-distribution

Year-end distributions
Class A: $4.029316 (capital gains)
Class B: $0.487939 (capital gains)
Class F: $3.814033 (capital gains)