

VERTEX FUND

First Quarter Report, 2014

Does a Bimbo buy bread?
The answer is "Yes".

Our favourite merger headline this decade has been the acquisition of Canada Bread by **Grupo Bimbo** that was announced in February. In this time of international border tension we could use a little humour for cross border acquisitions, whether they are on friendly or unfriendly terms.



During the first quarter of this year, the Vertex Fund had its best outperformance against the American market in quite some time, with an increase of roughly 6 percent versus flat performance from the indices. This was due to the portfolio having little American equity exposure; with most of our performance coming from our over-weighted position in European banks and unhedged US dollar exposure.

Over the past three years, Fairfax Financial has lost over three billion dollars hedging against the supposed collapse in China. However, we now think some small cracks in Asia are showing with the first Chinese bank defaulting and the first high-yield note defaulting within the last 30 days. The correlation between an Asian slowdown and the North American economy may be higher than most have thought, so we have been more reticent to have equity exposure. Our net equity exposure over the last quarter has never been lower and we have had a maximum exposure to our outright short position.

On the long front, we have built a sizeable position in the old GMAC, now known as Ally Financial. Our favourite theme, since the financial crisis of 2008, is to invest in bankrupt companies as they exhibit little downside after bankruptcy! Ally has already kicked the can down the road and will soon come back as a public company with the US Government selling its interest in an IPO. We plan to benefit in two ways with our ownership in the bonds and the equity. Firstly, we think with its improved financial condition, the bonds will be re-rated and carry a lower interest rate, causing a capital appreciation and an option to get called, as the company re-finances its high coupons with lower coupons. Secondly, we own equity in Ally at around \$8400 a share, which will soon split at a ratio of 310-to-one. We hope this IPO goes better than Facebook and more like Twitter.

Our arbitrage strategies continued to chug along in the first quarter, with no major surprises. At the risk of repeating ourselves, we continue to be frustrated by a level of M&A activity that stubbornly remains below our expectations. Thankfully, there are signs that activity is picking

up; this quarter was the most active for M&A since the third quarter of 2008 (thanks largely to the \$40B acquisition of Time Warner Cable by Comcast).

One area we have touched on in the past is the inefficiency that sometimes arises when a portion of a merger's consideration comes in the form of a "spinco". These small spin-off companies are often sold by merger arbitrageurs into a grey market with a lack of real buyers. Unlike our arbitrage brethren that are simply looking to sell spinco's in order to lock in a spread, we often find these securities to be trading very cheaply and will buy them. A great example is Knight Therapeutics, the spinco from the acquisition of Paladin Labs by Endo International. This security was trading at roughly \$2.25 in the grey market in January and February, but opened at \$4.00 on the day it was first exchange listed in early March (it is now trading north of \$6.00 after some positive news and a couple of financings). This example illustrates the fertile ground that M&A provides for event-driven ideas beyond our more typical arbitrage strategies.

PERFORMANCE (Class A shares as at March 31, 2014)

Net Asset Value	1 Month	3 Month	Year to Date	1 Year	5 Year⁺	10 Year⁺	15 Year⁺	Since Inception⁺
\$74.0042	0.62%	6.06%	6.06%	16.59%	20.50%	11.49%	16.93%	16.84%

⁺annualized returns

This statistical information is intended to provide you with information about the Vertex Fund. Advertised performance is based on Class A shares. Important information about the Fund is contained in the Offering Memorandum which should be read carefully before investing. You can obtain an offering memorandum from Vertex One Asset Management Inc. The Offering Memorandum for Vertex One Asset Management Inc.'s Investment Funds does not constitute an offer or solicitation to anyone in any jurisdiction in which such an offer or solicitation is not authorized or to any person to whom it is unlawful to make such an offer or solicitation. The indicated rates of return are the historical annual compounded total returns for the period indicated, including changes in security value and the reinvestment of all distributions and do not take into account income taxes payable that would have reduced returns. The funds are not guaranteed; their values change frequently and past performance may not be repeated.