

VERTEX FUND

Third Quarter Report, 2014

Lord grant that Marshal Wade

May by thy mighty aid

Victory bring.

May he sedition hush

And like a torrent rush,

Rebellious Scots to crush.

God save the King.

- Lyrics to "God Save the Queen (King)"

This quarter it was all about Scotland (ignoring the other regions looking for independence, from Catalonia to Ukraine). The Royal Bank of Scotland (RBS) had been our largest debt holdings over the past three years because we saw the largest potential for a recovery to par. As most of RBS capital structure now trades through par, we have sold 90 percent of our holdings and thought we had moved on. But when one door closes another opens. There is very limited risk when you buy something that has already gone bankrupt and the 2008 financial crisis afforded us a lot of opportunities to implement this theory. Scotland continues to surprise us with opportunity.

The Scottish independence vote caused the pound to sell off and the common shares of RBS to follow suit, as opinion polls were split down the middle for independence. But like Quebec, they have now stated their "declaration of dependence" and much like Quebec, the undecided are the ones who swayed the vote. If you weren't a separatist going into the voting poll you weren't going to turn into one as you marked your ballot. With fears that RBS would have to relocate to London, we recalled that when the Bank of Montreal ran to Toronto during the referendum, over the medium term, the valuation never differentiated from its Canadian peers. RBS today trades below 0.6 of book value and we believe it will trade near book value. We have also added exposure to Barclay's under the same investment theme.

British banks are now our largest equity weight in the portfolio and as markets sold off in their usual autumn (read "fall") decline, we have taken advantage of these bargains to add equity exposure. We also added exposure to the US currency and removed our gold hedges in light of new quantitative easing measures in Europe and China, which should bode well for European banks. As Canada is following a lower Loonie policy, we will stay unhedged until at least 85 cents (USD to CAD).

Also, during the last quarter we witnessed "Arbageddon" with the collapse of the non-definitive Walgreen, Sprint and Time Warner Inc deals. We avoided most of the carnage, with the exception of Time Warner where we took a small loss. Otherwise, definitive M&A deal flow continues to be excellent. Whereas the first half of the year was dominated by large deals, we are now seeing more mid-cap transactions (roughly \$2-10 billion in equity capitalization) that allow us to build out a highly diversified portfolio of arbitrage situations. Additionally, the

issuance of subscription receipts in Canada continues at a strong pace, providing another low-risk arbitrage strategy.

Tax inversions, the process by which US companies seek to re-domicile outside of the US by acquiring a smaller foreign company, were very topical. The IRS taxes American companies on their worldwide income, not just income earned in the US (the same applies for US citizens). Because US corporate tax rates are among the highest in the developed world, there is a strong incentive for many US companies to re-domicile in foreign jurisdictions possessing territorial tax systems (paying taxes only in the countries in which income is earned). The pace of tax inversions has been accelerating in recent years, which has not gone unnoticed in Washington. In early August, the Obama administration tasked the Treasury/IRS with toughening the rules around inversions. This was a surprising move given their previous stance of being unable to act without congressional approval of changes to the tax code, something that is highly unlikely in the current political environment.

In terms of the arbitrage portfolio, the two spreads that are most relevant to inversion risk are Covidien being acquired by Medtronic and Shire being acquired by AbbVie. Tim Hortons by Burger King is a different type of transaction that is not subject to the same risks (although we find it amusing to see Canada being portrayed as a tax haven). While there are clearly tax benefits that arise from these deals, there are also sound strategic rationales and synergies. Furthermore, terminating these deals will result in significant costs (primarily in the form of break fees) for the acquirers. The Covidien and Shire spreads widened considerably on the surprise August announcement, hurting the fund's performance. On September 22nd, after much uncertainty, the Treasury released their proposed rule changes. The changes were within our expectations and the arbitrage spreads have narrowed slightly on the belief that the changes will not be enough to derail the transactions.

PERFORMANCE (Class A returns as at September 30, 2014)

Net Asset Value	1 Month	3 Month	Year to Date	1 Year	5 Year⁺	10 Year⁺	15 Year⁺	Since Inception⁺
\$72.4507	-2.72%	-3.31%	3.83%	10.48%	10.27%	10.73%	15.12%	16.15%

Net of all fees and includes reinvested distributions.

⁺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.