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# VERTEX ENHANCED INCOME FUND

Second Quarter Report, 2011

***"School's out for summer"*** - Alice Cooper

Remember that feeling in the spring when it started to get really hot in the school and you couldn't wait to get to summer? Well, it sure seemed like the capital markets felt that way as everyone was headed for the exits this spring.

The quarter was dominated by the equity markets with the S&P/TSX Composite Index down 5.78% with resources leading the slide. The fund did what it was supposed to do, it is a long-only fund and right now we have it set up to have a beta of 0.25 to 0.35 in negative markets. The fund was very consistent throughout the quarter and despite the loss is still up 3.09% year-to-date, outperforming its benchmark by 1.97%.

For the first time in 12 months, high yield bonds saw net outflows as investors moved to a "risk off" trade out of risky assets. This was more of a general move than high yield specific, as commodities and equities also took it on the chin, while treasuries seemed to be the only asset class that benefited. We will see if the "risk on" trade comes back over the summer or whether this is the start of a larger move. A very similar situation last spring led to a strong market in the second half of the year. With a long-only fund, negative returns are tough to avoid when the macro environment is negative, but we can control the beta of the fund. As a result, we were pleased this quarter that the fund, in much the same market conditions as Q2 2010, was down 1.59% compared to down 3.54% Q2'10.

The funds main bond theme remains cash flow businesses. MBAs will tell you that on the first day of accounting class they learn that "Cash Flow is King", and there is a good reason for it. Warren Buffet built his empire on the concept of investing in steady cash flow businesses. Las Vegas bonds always trade with high yields indicating a perception of high risk; meanwhile, gambling is a cash flow business that is amazingly consistent (based on the law of large numbers). So, we see the actual risk as low and owning the debt of casinos is a great way to take advantage of the old proverb "the house always wins". This is why we love these bonds and have positions in no less than five Las Vegas casino operators.

Another cash flow theme is cash stores. Here's a stat that few probably know: nearly 2% of the customers at cheque cashing stores make over $100,000 per year. Another business based on the law of large numbers, they can accurately predict losses due to non-payment and therefore have very consistent earnings. It just so happens that there was a flood of them to issue new bonds this year and we participated in four of them. Considering that they were paying 20% for their funding costs, the 10.50-10.75% coupons are a win-win for bondholders and the companies themselves. Most states and provinces now have stable legislation in place for cash lending operations and we continue to look for more investments in the space.

In most Ontario towns, the big vacation month was always July, the plants shut-down and everyone left the cities and towns in groves to head for the lakes. So, while we'll be here working hard to get back last quarter's losses, we hope you enjoy the water! Let's hope for some good weather…

**PERFORMANCE** (Class F)

| Net Asset Value | 1 Month | 3 Month | Year-to-Date | 1 Year | Total Cumulative |
|---|---|---|---|---|---|
| $11.6685+ | -1.97% | -1.59% | 3.09% | 17.33% | 28.30% |

Income Distribution: $0.059067

+Post Distribution

This statistical information is intended to provide you with information about the Vertex Enhanced Income Fund. Important information about the Fund is contained in the Simplified Prospectus which should be read carefully before investing. You can obtain an offering memorandum from Vertex One Asset Management Inc. The Simplified Prospectus 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 funds are not guaranteed; their values change frequently and past performance may not be repeated.