

## **VERTEX ENHANCED INCOME FUND**

Fourth Quarter Report 2017

The Vertex Enhanced Income Fund returned 1.63% for the month of December; the fund returned -1% in the 4th quarter of 2017, but was up overall with 3.91% for the year (F Class).

**"A person will experience three bull markets in their lifetime. In the first one you do not have enough money to do much with it. In the third one you are too old to take the risk of investing in stocks. So, you had better use the second bull market to accumulate wealth."**

We couldn't find who penned the above quote, but it speaks loudly to the current market. There's no shortage of people telling you the bull market has run its course, gone on too long, or is just destined to fail. But, bull markets don't end because they've been around too long, they end because there's a problem – and that problem, more often than not, is because there's a cog in the machine, a slowdown in the velocity of money. We're not saying that the bull can last forever; we're saying that we don't see a catalyst that will bring the market down in the short term.

There are people talking about the housing bubble and the bitcoin bubble and the (fill in your own blank here) bubble, but until anything causes a slowdown or stoppage in the flow (or velocity of money), the bull market will remain intact. New rules for housing in Canada come into effect on January 1, 2018 and we'll be watching intently. As every bear market is different than the last, we'd be surprised to see something happen that causes the bull to end its reign.

Bitcoin, as every supporter will tell you, is different. While we agree that it's different, we don't agree that it's a different market and needs to be valued differently. To us, that sounds too much like the 2000 tech bubble language, which makes us nervous. We do see, however, the value in blockchain changing our future, we're just not so sure it's bitcoin or any of the dozens of alternatives now created. Is Bitcoin internet 1.0? Will it be good enough to survive as infrastructure can be built around it? Is Ethereum the answer? Is the rally in blockchain currencies real?

All great questions and we continue to search for answers. With a new blockchain company popping up every day, how do we take advantage of it? Anyone who has tried to execute a blockchain transaction over the last few months knows that the transactions are far from instantaneous. The infrastructure needed to build out blockchain will be immense. For an income product, we stick to the infrastructure names: Microsoft and Oracle. There might be an Amazon out there, but how do we find it amongst all the sector noise? We stick to what we know.

Maybe 2018 is the year people start talking about the oil bubble – now that oil is bumping up on \$60. We can hope for nothing more as bull markets are built on a wall of worry. We're still closely watching the Saudi Amarco IPO and wouldn't be surprised to see the IPO date slide into 2019. It's hard to analyze the Amarco IPO's impact on the market; we continue to keep a close eye for potential problems. We do know the Saudi's want to dress Amarco up to be "the Belle of the Ball" and this means PROFITS from a higher oil price. Most importantly, your fund does not own "the market" – we like to populate the portfolio with undervalued equities with less correlation to the market. We've found these equities largely in the unloved commodities.

The equity portfolio returned 150 bps for the quarter, largely on the back of our copper producers, (Freeport-McMoRan and BHP Billiton) and the offshore drillers (Diamond Offshore and Noble Corp). Our equity weight is close to the 25% upper limit (24.65%). We will continue to keep it at the high-end for diversification and enhanced return.

The bond portfolio returned negative (65 bps) for the quarter. A few of our restructurings proved challenging and we wrote down the value of a few of our private securities:

- We were wrong with our assumptions on a restructuring of one of our securities and sold the security down.
- We continue to hold another restructuring security as we think the first offer from the company undercuts the value of the positive cash flow – plenty of growth opportunities in the pipeline.
- We wrote down the value of one of our private notes; we continue to negotiate with the company and like how current management has cleaned up the structure, while moving forward with positive steps to accrete value to stakeholders.

Our weight in bonds is 64.25%, with 9.5% of that total being convertible bonds where correlation leans toward equity. Our duration is extremely short, therefore we are well protected should interest rates rise significantly. Although we couldn't have predicted the high yield and commodity rout in 2015, the fund generated a return of 9.5% annualized for the past two years and 5.8% annualized since inception.

Your Enhanced Income Fund remains an excellent diversifier away from traditional bond funds and equities. The most important factor in portfolio construction and risk reduction is how different assets work together to reduce risk, as it's hard to predict which economic factors will drive returns in the short term. Our portfolio management process within the fund itself takes this approach as sometimes our best ideas fail, while others perform incredibly well. Knowing we don't know is everything in investing.

We wish the best for our shared success in 2018!

## PERFORMANCE (Class F returns as at December 29, 2017)

Net Asset Value	1 Month	3 Month	Year-to-Date	1 Year	3 Year*	5 Year*	Since Inception*
\$ 9.4399 <sup>+</sup>	1.63%	-1.00%	3.91%	3.91%	1.85%	3.62%	5.76%

Net of all fees and includes reinvested distributions. <sup>+</sup>Post Distribution <sup>\*</sup>Annualized. 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.