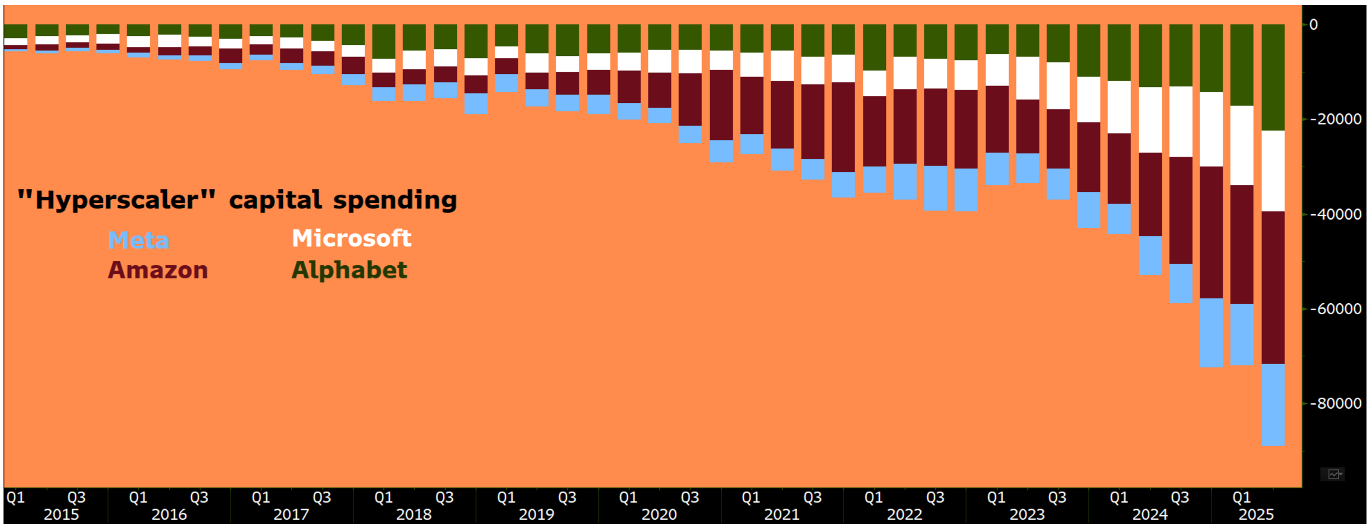
August 11, 2025

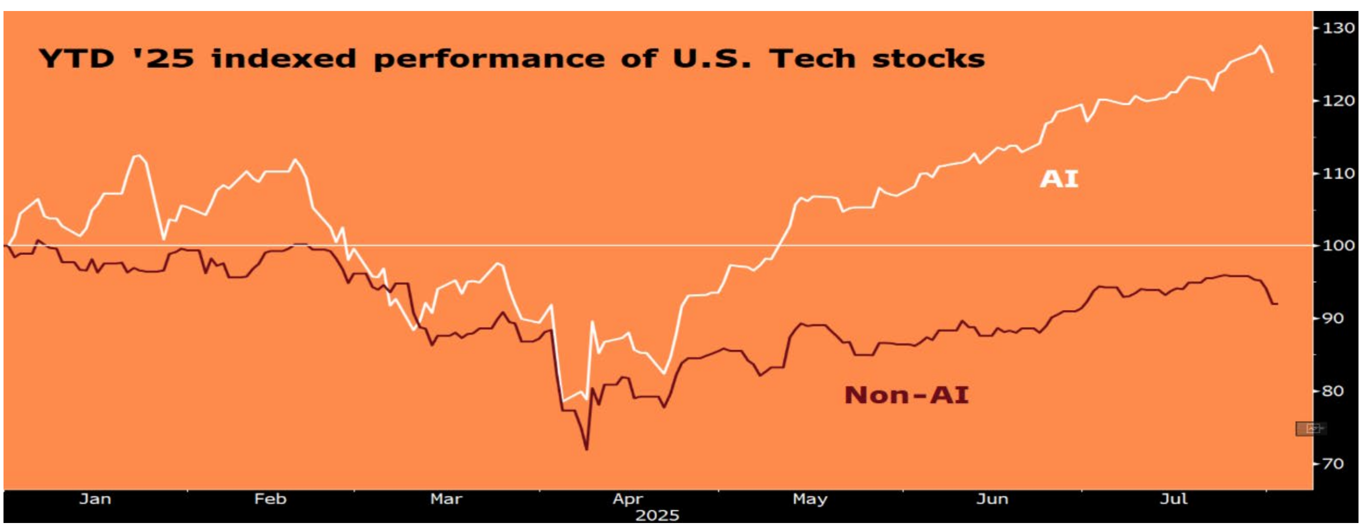
July 2025 Commentary

Please remind me what DeepSeek was all about. Wasn't it supposed to upend the proverbial apple cart and cause the hyperscalers to take a hatchet to their forward capital spending programs? That was January 2025, while the far-right side of the bar graph below displays the capital spending in billions of US$ of the hyperscalers for the recently reported quarter. AI-driven capital spending has returned with a vengeance as Meta, Microsoft, Amazon, and Alphabet spent $155B during the first half of 2025. According to Britain's The Guardian newspaper, this sum is greater than what the U.S. government has spent on education, training, employment and social services fiscal year-to-date.



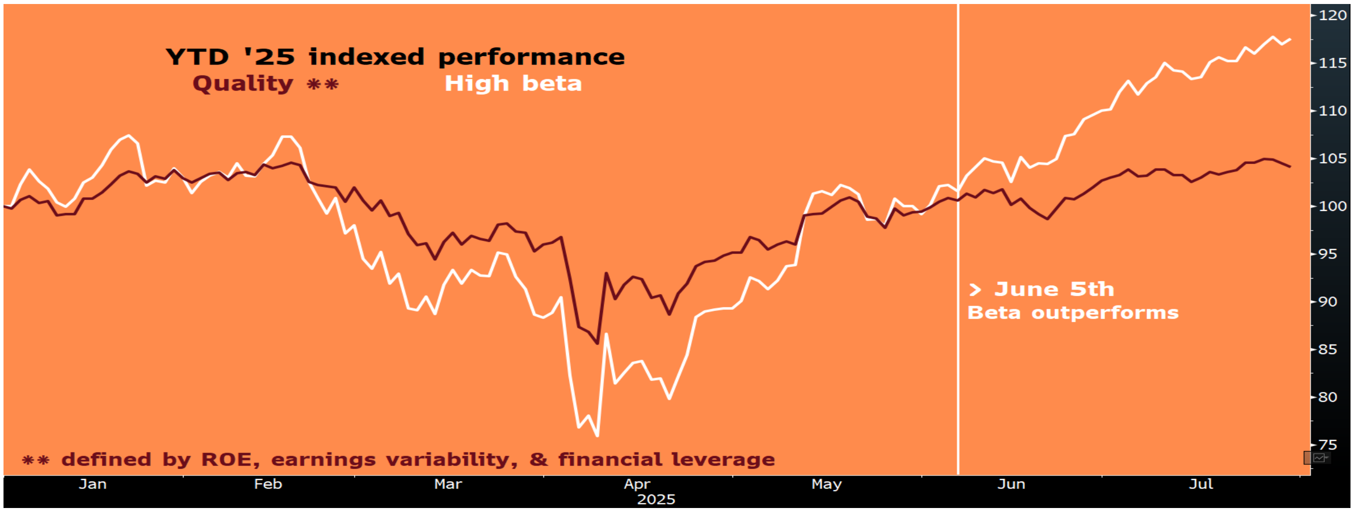
Source: Bloomberg

According to The Wall Street Journal, these four companies will spend more than $400B on capex during their next fiscal year. This full-on AI frenzy explains why AI-based tech stocks have significantly outperformed non-AI tech stocks from the April 2025 bottom in equities as shown in the year-to-date indexed graph below. Interestingly, within one to two months, DeepSeek is expected to release the 2.0 version of its large language model with a focus on video and graphics. We wonder if 'lightning will strike twice'!



Source: Bloomberg

Needless to say, our positions in the Technology sector contributed positively to the good month delivered by each of our funds. Beyond this Technology exposure, attribution, which included a solid contribution from the fixed income sleeve of our "sophisticated balanced fund" (Multi Strategy LP) was led by positions in Industrials (Comfort Systems USA Inc. - FIX.US), Consumer Non-Cyclicals (Gildan Activewear Inc. - GIL.CA) and Energy (Spartan Delta Corp. - SDE.CA). Losses arose from our positions in Hedges, REITs and Materials. As discussed in past commentaries, given our dual mandate to protect capital and deliver a competitive risk-adjusted net return, it has been annoying to continue to roll protection during a period of time when investors appear to have thrown caution to the wind.



Source: Bloomberg

Yet, as the predecessors to our alternative mutual funds, the original Limited Partnership versions of our funds enter their 14th year of operation. Our clients know that we will always stick to our disciplines of holding protection, a short book, no privates, and modest, if any, exposure to small caps. Consequently, the "chase to beta (white line)" over "quality (red line)" shown on the right side of the white vertical bar in the YTD, indexed graph above is frustrating, but we suspect transient. Price gains in the equal-weighted S&P 500 (red line) in the below graph were a respectable, but less exciting +5.8% through July 31, while the similar index for the Russell 2000 (white line) were flat for the YTD.

Source: Bloomberg

As of month-end, the Class F Lead Series of our Multi Strategy LP had gained +5.25% net of fees YTD, including a +2.23% advance during July. The Class F Lead Series of our Long Short LP earned +1.43% net of fees last month, such that it closed out July up 3.22% net YTD.

The beta-adjusted net equity exposure of our Multi Strategy LP and Long Short LP respectively were -9%/-13% lower from their mid-month peak on July 15th. The former closed the month with delta-adjusted gross exposure of 213% and net exposure of 81%, split between fixed income (46%) and Equities at (35%). Similar numbers for the Long Short LP showed delta-adjusted gross exposure of 134% and net long exposure of 31%.

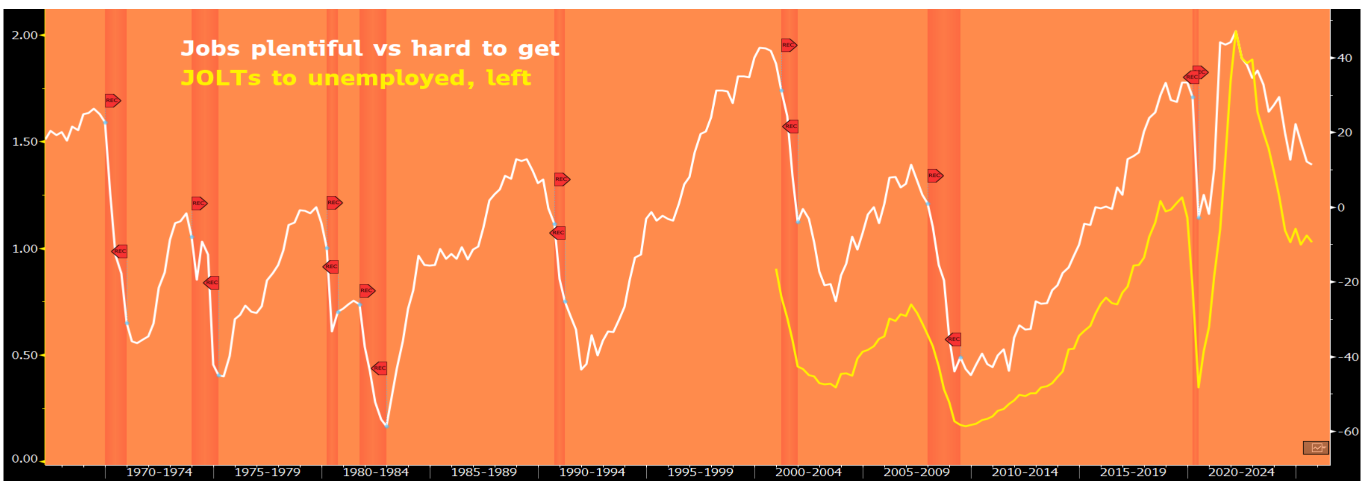
This purposeful degrossing was aligned with our strategy to reduce equity exposure into the seasonally tougher August/September period. These lower exposure levels are largely explained by higher deltas on our systematic SPY hedges, a return to our negative delta IWM strategy, reduced exposure to performing ideas and increased ETF short exposure.

Further, we cut our financials exposure materially, exiting JPMorgan Chase & Co. (JPM.US), Ares Management Corp. (ARES.US), KKR & Co. Inc. (KKR.US), and reduced our weighting in Brookfield Business Partners L.P. (BBU-U.CA). We also initiated a short position in a U.S. regional banking ETF (KRE.US). We do not believe that Financials are well positioned for the pending reduction in policy rates and the inevitable decline in reserve required to fund the federal deficit, as this pair should pressure deposits and net interest margins.

As of July 31, 2025	YTD	1-mo	3-mo	6-mo	1-year	3-year	5-year	10-year	Inception
					----------------	Annualized	----------------		
Forge First Long Short LP (Class F Lead Series)	3.22%	1.43%	7.74%	3.47%	7.86%	7.24%	9.97%	7.95%	12.89%
Forge First Multi Strategy LP (Class F Lead Series)	5.25%	2.23%	10.76%	5.28%	10.85%	11.11%	11.85%	7.64%	11.07%
S&P/TSX Composite Total Return Index	12.03%	1.69%	10.47%	8.26%	21.37%	14.98%	14.40%	9.83%	10.03%
S&P 500 Total Return Index (C$)	4.50%	3.91%	14.52%	1.59%	16.67%	20.18%	16.62%	14.35%	17.44%

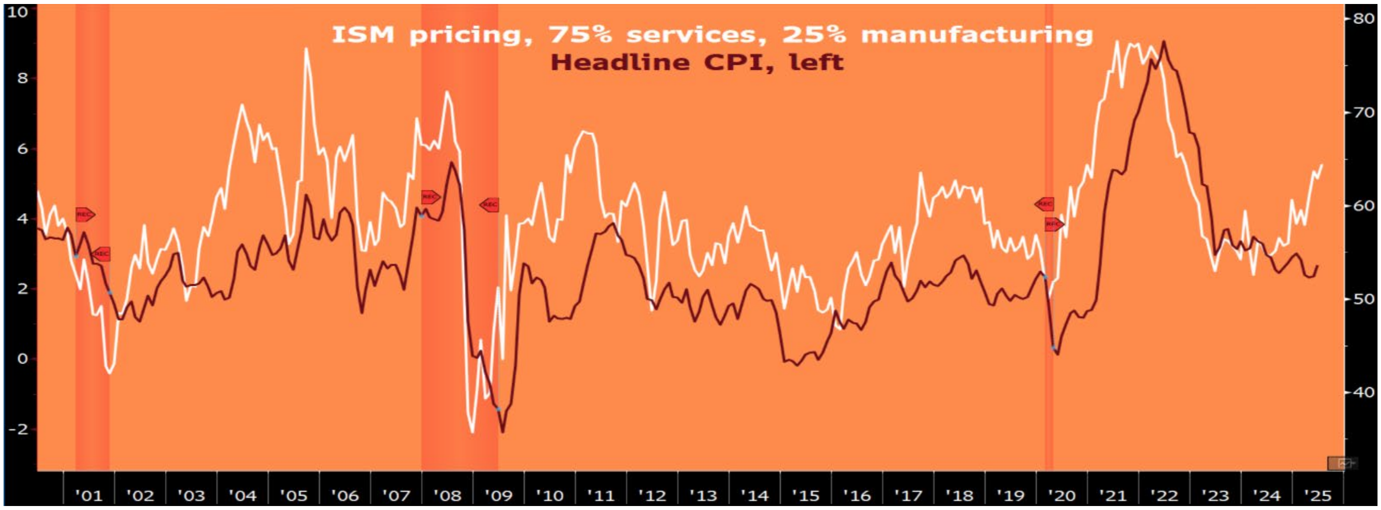
Note: Returns for the Forge First funds are based on the August 2012 Class F Lead Series and are net of all fees and expenses. In a year, up to 12 series can be created within a Class of units. Unitholders are advised to refer to their monthly statement for the net return of their respective Class and Series. All returns are in local currencies.

Whether the restart of rate cuts by the FOMC will occur at its meeting in September is a function of the trajectory for economic growth, the health of the labour market and the outlook for inflation. The meagre +1.2% real final demand (free of indirect effects of trade and inventory distortions) print for the H1 of 2025 and the sizeable negative revisions seen in the U.S. jobs report for July make it clear that the U.S. economy is slowing. Both serve to validate a rate cut in September. Yet the 60-year graph below suggests the labour market is merely continuing to normalize, as opposed to currently being in bad shape. In addition, net immigration trends could retard the slowdown in wage rates typically accompanying a slowing job market.



Source: Bloomberg

In assessing inflation, we must consider service industry pricing and the outlook of tariffs. The following 25-year graph compares the ISM Pricing Index (white line, right axis), weighted between services and manufacturing, against Headline CPI (red line, left axis). The recent marked decoupling of a previously strongly correlated pair of statistics supports a view of higher inflation. While the start of April marked the first pronouncement of tariffs, due to a host of reasons, the number of companies increasing prices in an attempt to cover tariffs has only recently begun to climb. Consequently, we expect to see a rising number of tariff-driven price hikes during the remainder of the year relative to what we've seen during the past few months.



Source: Bloomberg

Additionally, a key reason for President Trump to boost tariffs to levels last seen almost 100 years ago was to repatriate manufacturing jobs to America. Unfortunately, many of the highest tariffs announced to date will serve to drive up the cost of imported industrial inputs for U.S. manufacturers, causing them to be less competitive, unless massive subsidization follows.

Between the impact of tariffs and the current trend in service industry-based pricing, it does appear that one of the Fed's favourite inflation metrics, Core PCE, is likely to exit 2025 at 3% or higher. Arguably up until the July jobs-shocker, which could shift his thinking, little wonder why Chair Powell has been willing to watch and wait.

The Fed has been between a 'rock and a hard place', navigating two competing narratives, one where 1) tariffs and softening consumer demand derail the soft landing, against the scenario in which 2) gargantuan AI investment and resilient high-income spending keeps the economy running at a pace that arguably lessens the need for rate cuts, notwithstanding the strains evident within the lower quintiles of the population.

Fortunately, or unfortunately as the case may be, as seems to have been the case since 2008, stimulus surrounds us. Treasury Secretary Bessent's "stealth QE" of financing at the short end will cut the supply of duration with one intent being to reduce the term premium out the curve. Then of course, there are stablecoins. To us it's unclear how these products can be the source of US$2T plus of funding for the Treasury when the purchaser of the asset gets no yield, but the issuer does? Yet, this author will admit to not understanding the soundness of the mania in marijuana stocks during 2017-2018 given that marijuana was just a crop! Then let's not forget the fiscal stimulus arising from Trump's "OBBB". While unlikely to have a large impact, it is thought this legislation will further increase Washington's deficit next year.

Similar to any investor, we've had our share of hits and misses this year, but there's little doubt that aside from April's swoon, our disciplined use of protective hedges has been a cost to the funds this year. Yet beyond their use being a discipline, the unpredictability emanating from the White House, other macro uncertainties and the valuation of stocks have explained why we've held that protection. We expect that stocks will pull back here and at this juncture, we expect to be buyers on pullbacks.

Please let us know if you have any questions and thank you for your business.

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