

June 2024 Commentary

Post the strong bounce back of equities during May, the combination of deteriorating market breadth and weakening economic statistics in June suggest stocks may enter a choppy period during the summer. Regardless as to whether that implies sideways or negative price performance, strong messaging that the Fed put remains in place, plus the expectation of one last barnburner quarter of earnings from mega cap tech should prevent stocks from experiencing a significant downdraft in the near term.

For June 2024, the S&P 500 U\$ generated a price gain of +3.47% versus a +0.99% advance in the S&P 493 and negative performance for the equal weighted index. The M7 accounted for 79% of the SPX's total return. The greater than 400 bps divergence between the equal and market weighted SPX was the third largest performance spread since 1989, only 'bettered' by tape action during the 'tech bubble' and COVID. As these two indices have exhibited a 90% correlation during the past five years, we found the degree of divergence to be eye-popping. For the second quarter as a whole, the S&P 500 U\$ posted a price gain of +3.92% (+4.28% total return), however, the S&P 493 declined -1.47% and, unlike Q1, breadth was markedly negative as 304 issues declined in price compared to 199 advancing stocks.



Source: Bloomberg

Meanwhile, inside the yellow oval on the far-right hand side of the 20-year graph above, you can see that the Citigroup economic surprise index for the U.S. (red line) has gone decidedly negative. The similar line denoting inflation surprises (white line) has also gone negative, though granted it's much tougher to view on the graph. There's little question the U.S. economy is slowing. Just during the last week of June, we witnessed lousy housing data and tepid orders for durable goods, while companies from Nike Inc. to Walgreens to Southwest Airlines to General Mills all took a hatchet to their operating expectations for the second half of calendar 2024.

Shifting to our funds, each of our two funds posted strong performance for the month. The Series F of our Long Short Alternative Fund gained +3.29% net, boosting its year-to-date net return to +7.06%. The trailing 12-month net return sits at +15.00%. The winningest sectors were Financials, Technology, Consumer Non-Cyclicals, Industrials, Energy, and Market Hedges, while modest losses were experienced from positions in Communications, Real Estate and Materials. Given the net common equity exposure range remained low, at between 17% and 25%, the vast majority of returns were driven by alpha not beta.

The delta-adjusted gross and net exposure of this fund exited June at +145% and 41%. Besides roughly 17.5% net long exposure to two high-yielding, leveraged loan ETFs, the Financials sector, at 10.18%, is the only sector with net long exposure in excess of 10%. Six sectors have net long exposures of between 4% and 5%, including Technology (see comments on the Conservative Alternative Fund below), Consumer Cyclical, Real Estate, Industrials, and Utilities. The fund is currently net short the Materials sector.



Source: Bloomberg

The yellow oval on the right side of the above graph confirms the recent pain of holding systemic protection against market declines due to falling realized volatility (white line). Falling single stock correlation has also reduced the utility of index protection. However, our disciplined approach to managing capital ensures the use of index puts and put spreads will always constitute a one layer of insurance for our portfolios. In addition, given the dynamics discussed here, we have shifted a portion of our typical index protection into a broadened sleeve of single stock short positions.

As of June 30, 2024	YTD	1-mo	3-mo	6-mo	1-year	2-year*	3-year*	5-year*	Since Inception*
Forge First Long Short Alternative Fund Series A	6.59%	3.21%	2.94%	6.59%	14.36%	4.19%	2.60%	7.81%	7.03%
Forge First Long Short Alternative Fund Series F	7.06%	3.29%	3.17%	7.06%	15.00%	5.05%	3.47%	8.74%	7.95%
Forge First Conservative Alternative Fund Series A	6.29%	2.11%	2.44%	6.29%	10.93%	6.05%	4.08%	7.65%	7.26%
Forge First Conservative Alternative Fund Series AT**	6.29%	2.11%	2.44%	6.29%	10.92%	6.03%	4.01%	N/A	4.22%
Forge First Conservative Alternative Fund Series F	6.79%	2.18%	2.68%	6.79%	11.96%	7.02%	5.04%	8.63%	8.23%
Forge First Conservative Alternative Fund Series FT**	6.79%	2.18%	2.68%	6.79%	11.96%	7.03%	5.02%	N/A	5.21%
S&P/TSX Composite Total Return Index	6.05%	-1.42%	-0.53%	6.05%	12.13%	11.27%	5.98%	9.28%	8.61%
S&P 500 Total Return Index (C\$)	19.38%	3.83%	5.35%	19.38%	28.76%	25.80%	13.64%	16.05%	14.82%

*Annualized | Inception date: April 24, 2019 | **Inception date: June 10, 2021

Shifting to our low volatility, multi-asset Conservative Alternative Fund, the Series F advanced +2.18% net for the month of June, increasing its year-to-date net gain to +6.79% and trailing 12-month net performance to +11.96%. Positions in Technology, Industrials, Financials, Consumer Non-Cyclicals, and Energy captured the majority of the returns with modest losses in Hedges and Consumer Cyclical stocks. Similar to the Long Short Alternative Fund, given the rough net common equity average exposure of 14% during the month, the majority of profits in the Conservative Fund were also generated from alpha not beta. The fund markedly reduced its net exposure to Technology stocks towards the end of the month.

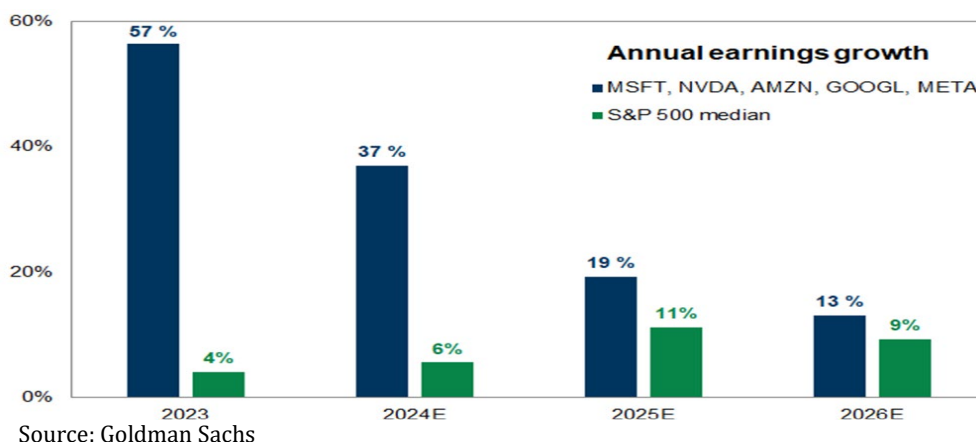
In light of the strong performance during the past two months of our high conviction ideas in the Tech sector, our portfolio management process dictated a reduction in sector exposure to approximately +3% net long in Conservative and +4% in Long Short. These nets were achieved by reducing exposure to Broadcom Inc. (AVGO.US), Taiwan Semiconductor Manufacturing Co. (TSM.US), and our already modest exposure to NVIDIA Corp. (NVDA.US). While we view the Tech sector as too frothy in the short term, we remain attracted to the “AI arms race”, hence while we added a put spread on a Semiconductor ETF, we also sold out-of-the-money puts on Broadcom and Taiwan Semiconductor Manufacturing Co. Lumine Group Inc. (LMN.CA) remains the largest Tech position in the Conservative Alternative Fund, followed by Apple Inc. (AAPL.US) with Apple being the largest Tech weight in the Long Short Alternative Fund.

Other moves in the equity sleeve of the Conservative Alternative Fund offset the reduction of exposure to Technology stocks such that the net exposure to common equities closed the month at +14% net long (+22.9% net long exposure in underlying securities less - 8.9% of short exposure via listed options) versus +10% a month ago. At a roughly 10% net long exposure, Industrials is now the equity sector with the largest net long position. Within Industrials, shares of AtkinsRealis Group Inc. (ATRL.CA) represent the largest position.

Beyond common stocks, the fund also exited June with a +19% net long exposure to fixed income securities, including a position in the straight debt of AtkinsRealis (7% June 2026) such that in total, the delta-adjusted gross and net exposure of the Conservative Alternative Fund at the end of the month was 129% and 33% respectively,

As implied by the opening paragraph to this note and the positioning adjustments in the funds, while we foresee some near-term turbulence in markets fuelled by some froth in Technology, ongoing negative earnings revisions in the small and mid-cap space, and our expectation of rangebound yields, we don’t believe it is time to hit the ‘sell button’ for good. Yet given that momentum has been the best performing factor in markets, and its strong linkage to Tech stocks, for us it is a ‘pause that refreshes’ and we will use expected weakness to add exposure to higher conviction, GARP and value-oriented securities.

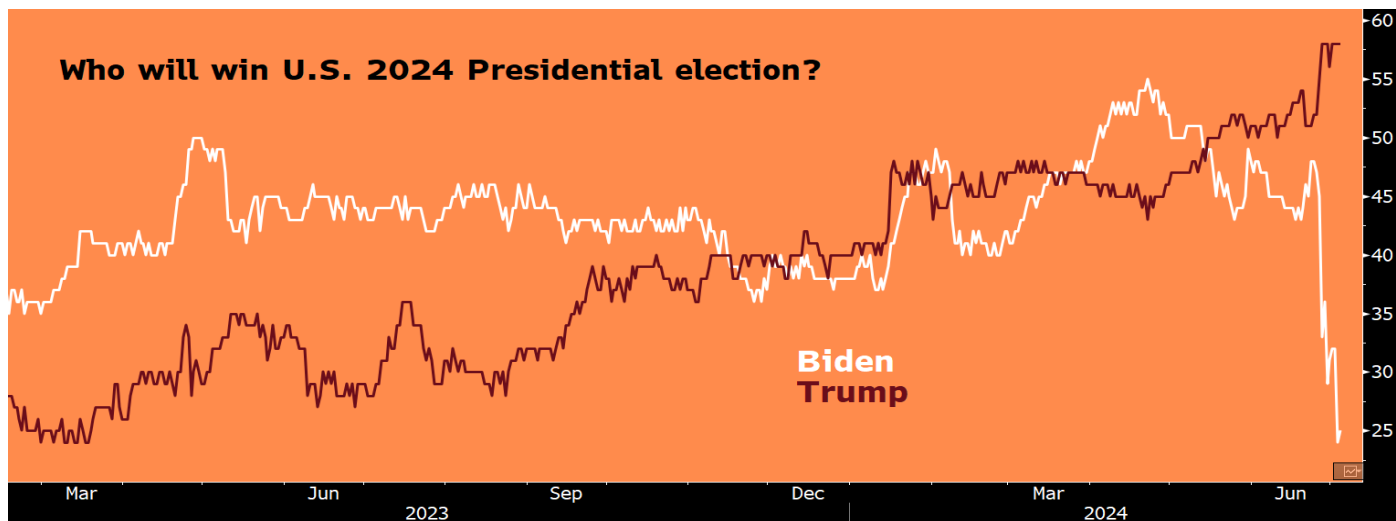
It will be fascinating to watch how markets react to the late July earnings releases of the macro cap tech sector. While the graph below, courtesy of Goldman Sachs, suggests the EPS growth premium of these companies is expected to erode markedly lower during 2025, that process is expected to begin post the upcoming Q2 results. If this turns out to be the case, will this cause the valuation expansion of the giants to stall or even decline? Further, according to S&P Global, the S&P 495 (the SPX less the M7 excluding Tesla Inc. and Apple Inc.) is forecast to exhibit negative EPS growth of 5% for 2024.



As per one of our predictions for 2024 in our December 2023 monthly commentary that the Fed would begin to cut rates during the second half of 2024, the directions of both the employment and inflation data appear to be supportive of cuts finally starting to happen. However, the Fed’s still not entirely out of the woods yet on inflation.

Shelter still accounts for 45% of core CPI and data suggests official CPI data is still understating the actual rental costs as measured by the Zillow rent index (up 31.5% since February 2020 versus a 22.9% same period rise in CPI shelter). Hence, shelter costs are falling but the landing is still in the future. While this fact is at least a nuisance for the Fed, on the positive side of the ledger, core goods pricing is now running at a negative 1.7% to at least partially offset the reality that core services are still running at hotter than desired levels.

Beyond inflation and earnings, investors are approaching the point in time when the U.S. Presidential election would normally hit their radar. Yet this time it appears the late June debate may have hijacked the suspense. Obviously, a lot may happen between now and early November, but the graph below suggests President Trump will win. If that’s the case our team believes the key issues for investors to consider will be tariffs, regulation, and the future make-up of the Supreme Court.



Source: Bloomberg

Thank you for your business and interest in our funds. For more information, please visit our website at www.forgefirst.com, or call us at 416-687-6771 should you have any questions.

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