FORGE FIRST
ASSET MANAGEMENT INC

March 5, 2021

February 2021 Commentary

Another action-packed month in markets saw bond yields spike, oil soar and all North American indices deliver solid returns despite the sea of red during the last week of February. Once again, the funds at Forge First profitably navigated these stormy waters.

As shown in the table below, the Long Short Alternative Fund, Series 'F' advanced +5.15% net of fees, pushing its 1-year net return to +24.22%. This monthly outperformance versus the major North American equity indices was attributable to two factors. First, the fund was underweight long duration, richly valued securities that stand to suffer the most from a rising interest rate environment. In contrast, the fund remains positioned to benefit from the "reflation" and "re-opening" themes that favour more cyclical, value-oriented securities.

Positive performance was generated from each of the sectors in which the fund is invested, with holdings in the energy and consumer sectors leading the charge. Our hedge book, including ETFs and index puts, cost the fund money during the month. One positive exception to this expense was attributable to our short basket of alternative power providers. At month-end, the gross and net exposures of the Long Short Alternative Fund were 127% and 40% respectively compared to 135% and 51% at the end of January.

	YTD	1 mo	3 mo	6 mo	1 year	Since Inception*
Forge First Long Short Alternative Fund Series A	5.29%	5.08%	8.12%	13.73%	23.10%	24.56%
Forge First Long Short Alternative Fund Series F	5.43%	5.15%	8.35%	14.22%	24.22%	26.67%
Forge First Conservative Alternative Fund Series A	4.69%	3.87%	8.47%	15.51%	22.21%	23.26%
Forge First Conservative Alternative Fund Series F	4.84%	3.94%	8.71%	16.03%	23.26%	25.32%
TSX Total Return	4.03%	4.36%	5.82%	11.02%	14.74%	14.95%
S&P 500 Total Return (US$)	1.72%	2.76%	5.63%	9.74%	31.29%	34.49%

***Inception**: April 24, 2019

Shifting to our lower volatility portfolio, the Conservative Alternative Fund, Series 'F' gained +3.94% net of fees, boosting its 1-year net return to +23.26%. Gross and net exposure closed the month at 123% and 51%. This net exposure includes a 39% net long position in the equity or capital growth sleeve, and a 14% net long exposure to credit and preferreds, which combined with a 7% holding in SPACs, adds up to a 21% net long position in the alternatives sleeve. The 3rd sleeve of this alternative mutual fund, asset protection, represented a -8% delta-adjusted net short position via listed options.

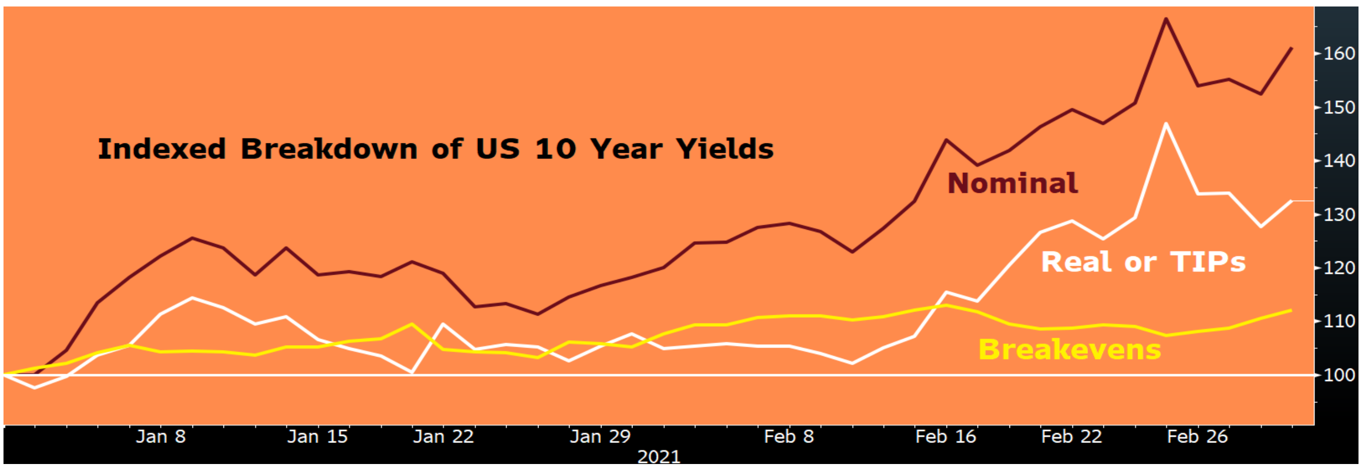
February performance was driven by positive contributions from the capital growth and alternative strategy sleeves, while the asset protection sleeve was a small net detractor. Positive attribution in the capital growth sleeve was fairly balanced across sectors and driven by high conviction equity positions. The alternative strategies sleeve had a very strong month, driven by positive returns from long positions in rate-reset preferred shares, corporate debt, convertible bonds, and short positions in long-dated government bond funds.

As discussed in our last commentary, the fund had increased its allocation to rate-reset preferred shares. These securities offer a combination of attractive running yields, and significant upside potential in the event that government bond yields rise. In Canada, the majority of these shares are priced off of the Government of Canada 5-Year Note. As rates rise, the future implied dividend on the rate-reset preferred shares rises. The Government of Canada 5-Year Note saw its yield rise from 42 basis points at the start of the month to 87 basis points at month-end, driving strong performance in preferred shares.

Also, in response to quickly rising long-term bond yields, the fund used short-dated option strategies to significantly increase the size of the asset protection sleeve of the portfolio. This action served to reduce the net equity exposure of the fund to its lowest year-to-date level and protect investors from the broad-based equity softness seen during the last week of February. A portion of this incremental protection was reduced at month-end.

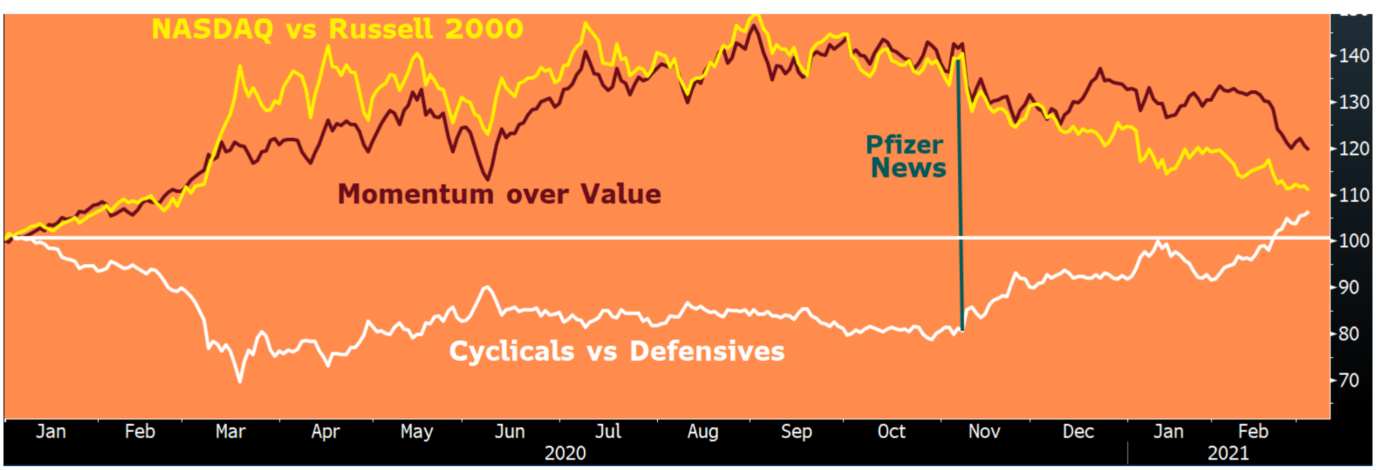
Consequently, our Conservative Alternative Fund was shielded from much of the pressure affecting other multi asset portfolios during late February, including balanced funds that resulted from an increase in volatility and the heightened correlation between equities and bonds.

The mini-turmoil that began to impact markets during the 2nd week of February was catalyzed by the combination of an increasingly positive vaccine roll-out in the U.S. and the growing confidence that Biden's next round of fiscal stimulus would proceed. These beliefs triggered a rise in the difference between nominal (or headline) yields and breakeven yields or 'real' yields. The graph below displays the year-to-date indexed changes in each of those three yields. The greater than 30% rise in real yields (white line) was the key to market action during the last half of February.



Source: Bloomberg

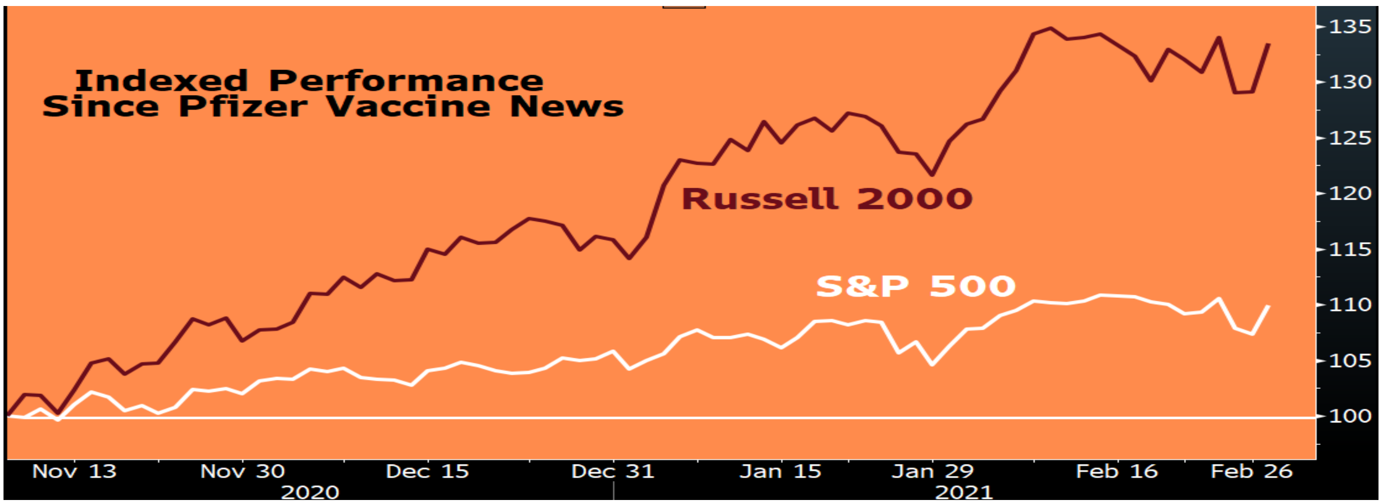
This increase in real yields drove investors away from momentum stocks towards value-based equities. The pain this rotation causes momentum-driven investors has been especially apparent in 'bubble-like' sectors that would include securities characterized as 'stay-at-home', non-profitable tech companies, alternative energy, and expensive software stocks. The catalyst for this shift is triggered when the market begins to discount the removal of monetary policy accommodation, as higher discount rates must be used to present value each company's future income streams. Naturally, the greatest impact is seen in equities in the most richly-valued sectors. Conversely, companies that benefit from improved growth, the prospect for higher inflation and rising interest rates, see the price of their shares rise.



Source: Bloomberg

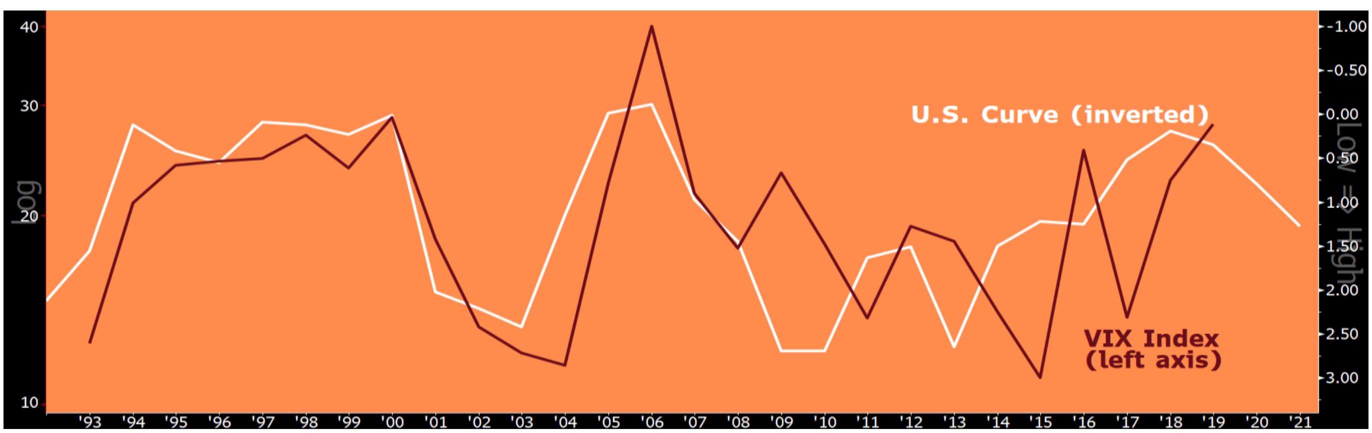
1 DISCLAIMER: This material has been published by Forge First Asset Management Inc. It is provided as a general source of information; it is subject to change without notification and should not be construed as investment advice. This material should not be relied upon for any investment decision and is not a recommendation, solicitation or offering of any security in any jurisdiction. The information contained in this material has been obtained from sources believed reliable. Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The indicated rates of return are the historical annual compounded total returns including changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any security holder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. The 2020 and 2021 results are unaudited, net of all fees and expenses, and are based on our best estimates at the time of this report. Index statistics use total return indices. The statements contained herein that are not historical facts are forward-looking statements, which are based on current expectations and estimates about particular markets. These statements are not guarantees of future performance and involve certain risks, uncertainties, and assumptions which are difficult to predict. Therefore, actual outcomes and returns may differ materially from what is expressed in such forward-looking statements. The information contained herein is subject to updating and further verification and may be amended at any time without notice and we are under no obligation to update this information at any particular time. The composition of the Funds' portfolio could differ significantly from an index due to the investment strategy employed, and includes differences such as use of equal weight positions, use of short positions and varying fund net exposure. Source for all index data: Bloomberg.

The indexed, relative strength graph above that begins during January 2020 indicates this rotation began concurrent with the release by Pfizer Inc. (PFE.US) of the results for its COVID-19 vaccine in early November. Since that time, cyclicals have trounced defensive stocks (white), value-based equities have outperformed momentum stocks (red), and the more sector-balanced, smaller cap Russell 2000 has trumped the tech-heavy NASDAQ (yellow). In fact, the duration of these rotations has been long enough to cause momentum indicators themselves to rotate towards a more cyclical composition beginning in March, first with the materials and consumer discretionary sectors, followed by energy up shortly thereafter.



Source: Bloomberg

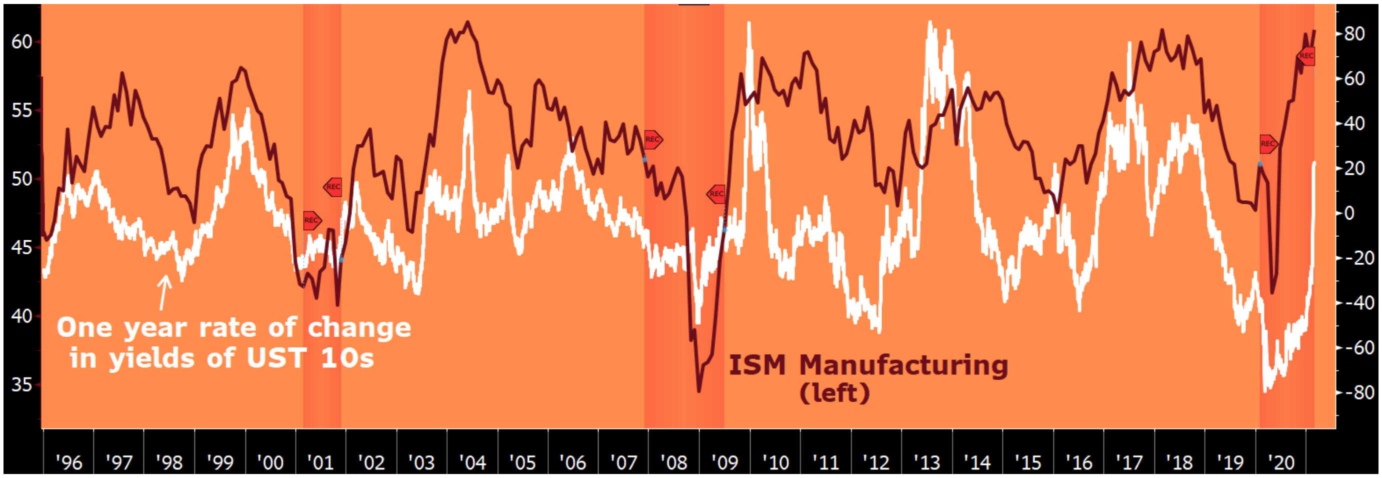
Given that growth is more heavily weighted than value in the S&P 500, this factor rotation is pushing the volatility between stocks lower, serving to keep the SPX range bound compared to the Russell 2000 as can be seen in the above graph. Unless real rates fully reverse their recent upward move, we would expect this rotation to continue. Such a scenario would imply a great market for stock pickers, on both the long and the short side. It could also be expected to drive realized volatility lower, even if the current elevated demand for put options keeps the VIX Index higher than might otherwise be the case. Also worth noting on the volatility front, the 28-year graph below suggests the VIX (red line) follows the inverted 10-2 yield curve (white line) with a two-year lag.



Source: Bloomberg

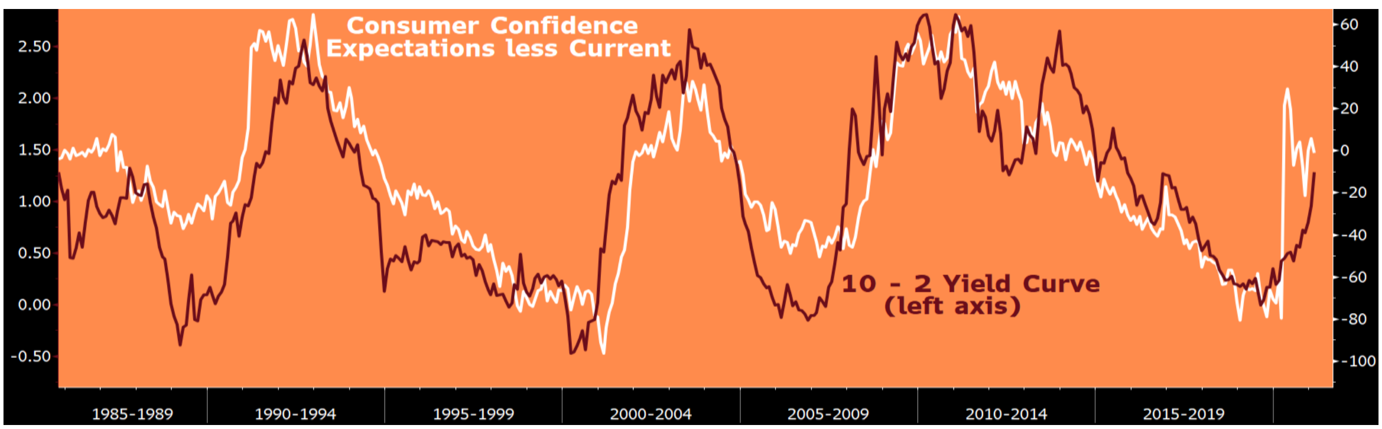
Looking ahead, all signs remain supportive of our medium-term constructive attitude towards equities. First, monetary and fiscal stimulus remain on full throttle. Second, the pace of vaccinations in the U.S. market is accelerating, accompanied by improving relevant related metrics. Third, as evidenced by last week's ISM manufacturing data, the recent rise in interest rates is symbolic of an improving economy.

FORGEFIRST
ASSET MANAGEMENT INC



Source: Bloomberg

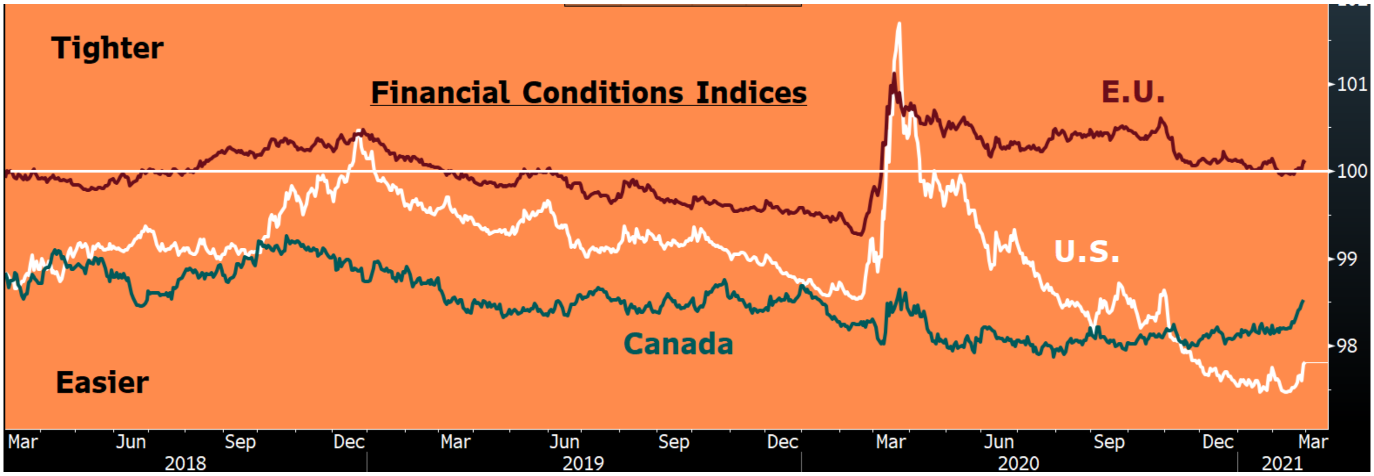
The 25-year graph above compares the year-over-year rate of change in 10-year U.S. Treasury bonds (white line on right axis) against the ISM manufacturing (red line on left axis). The shaded orange vertical bars denote recessions. On the right side, you can see that the improvement in the ISM fully supports the rate of change in interest rates. A similar argument can be made with the 35-year graph below.



Source: Bloomberg

The above graph compares the 'Expectations less Current Conditions' of Consumer Confidence data from the U.S. Conference Board (white line on right axis) against the 10-2 U.S. yield curve. Once again, this recent shift in interest rates is supported by the trend in economic growth, as opposed to the type of move higher in rates that punishes equities; ones driven by a change in direction by monetary authorities.

We've never fancied ourselves as interest rate strategists predicting specific levels across the curve. However, we have consistently suggested that for the foreseeable future, as in 2021-2022, consumer inflation is unlikely to force U.S. 10-year yields anywhere close to the 3% level that they traded at as recently as late 2018. This view is partially attributable to a belief that post the recovery from COVID-19, debt levels and structural changes to the economy will cause trend growth to recede back towards the anemic pre-COVID-19 levels. However, while we wouldn't be surprised to see a near-term pullback in rates, over the next six to nine months, we would expect rates to grind higher, and the Fed won't care!



Source: Bloomberg

That's because, as can be seen in the above 3-year graph highlighting financial conditions indices in Canada (dark cyan), the E.U. (red), and the U.S. (white), notwithstanding the recent rise in interest rates, financial conditions in the U.S. remain very easy. Credit spreads remaining near record tights is a key driver of this situation. Consequently, when Warren Buffett was quoted in his latest annual letter to shareholders that bond investors faced a "bleak future" and that "bonds are not the place to be these days", we took notice.

With this in mind, our Conservative Alternative Fund remains short government bonds. In addition, rate reset preferreds held in the fund have shifted to offerings with lower resets (200 bps + 5 year Canadas versus 400+bps) as the price of these securities are more sensitive to rising rates. It's this tactical ability of our Conservative Alternative Fund that enables this fund to constitute a great bond replacement product with an equity kicker to boot!

Speaking of tactical adjustments, our Long Short Alternative Fund has nudged up its net long exposure to energy (11.1% at time of writing). We believe the oil market is currently under-supplied by at least 2M barrels/day. Further, by this Summer, we don't believe supply will be able to keep pace with demand because, while OPEC's spare capacity resides with three countries, it's our belief that the KSA (the Saudis) remains quite content to maintain production below capacity. Due to their lack of investments, other members, including Venezuela and Nigeria, will continue to produce below capacity while declines in countries such as the U.S. won't easily be arrested despite the short cycle nature of U.S. shale.

Risks to our constructive view on oil are twofold. First, as China loaded up on cheap oil during 2020, authorities may moderate state-sponsored purchases in 2021. The second risk is of a U.S. deal with Iran. However, with a Presidential election this June, we don't think Iranian authorities will make any concessions, in turn eliminating any likelihood of near-term developments on this file.

Being 'buy and hold' investors focused on the generation of free cash flow, our largest energy position remains Canadian Natural Resources Ltd. (CNQ.CA), a company whose shares still trade at a free cash yield of in excess of 20% at strip pricing. Our other energy producer holdings, all of which will be familiar to regular readers of our commentaries, include MEG Energy Corp. (MEG.CA), Tourmaline Oil Corp. (TOU.CA) and Parex Resources Inc. (PXT.CA).

Notwithstanding our constructive stance towards markets and enthusiasm towards our high convictions investment ideas, as always the position-sizing within our funds remains pragmatic and our portfolios feature a healthy helping of right-sized short positions and listed put options. While this note has reiterated our rationale for markets to grind higher, beyond the near-term, as the global economy improves, it's only a matter of time until the expiry of the 'free pass' granted by the Fed. When that happens, while corporate earnings will continue to improve, apace with the economy, valuations are likely to contract. Such a scenario implies rising dispersion amongst the price performance of equities, a situation ripe for active managers of liquid portfolios, especially managers with a successful track record of utilizing shorts and listed options. To that end, we'd remind readers that our alternative mutual funds are rated as having medium risk and feature daily liquidity.

Thank you for the 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.

Thank you,

Andrew McCreath	Daniel Lloyd	Keenan Murray
President and CEO	Portfolio Manager	Portfolio Manager