

Manager's Commentary

Greg Taylor, CFA

Market Insights

The first half of the year had a little of everything. We have all come to expect the unexpected under President Trump but the events that have unfolded caught even the most cynical off guard.

Heading into 2026, one of the consensus calls was that the Federal Open Market Committee (FOMC) would cut interest rates. They were one of the last central banks to normalize policy after the aggressive rate hikes over the past few years, and it was time to correct that. Inflation was expected to fall and yields would follow. But as is often the case when everyone agrees, that wasn't what happened.

It started with a shocking strike on Venezuela that resulted in the US essentially taking control of the country (and its oil reserves) in a matter of hours. Markets appeared to cheer this outcome and that likely emboldened President Trump to take further action. After a year of tariff wars, the pivot was to actual combat wars.

By the end of February, the attack began on Iran with expectations of a similar result to Venezuela. But, it wasn't that easy. There was no decisive outcome, and the attacks resulted in an almost worst-case scenario. The old regime remained in place with the Strait of Hormuz blocked, and commodity prices skyrocketing higher.

Crude oil prices that had been drifting lower surged to over \$110 a barrel on WTI. Grains and other commodities followed. Suddenly that dream of a drop in inflation vanished and with it, yields spiked. The month of March saw a rise in volatility and a fall in equity prices. Investor sentiment fell with the market.

To further add to market uncertainty, the rise of AI was suddenly seen as a threat to many software companies as well as white-collar jobs. The Mag7 names that had previously looked invincible started to show cracks. The race to build data centres was sucking up the vast majority of the free cash flow these companies could generate.

Most symbolic of the AI spend was the price of Dynamic Random-Access Memory (DRAM). This overlooked technology commodity is in everything. As demand surged, prices followed, and we suddenly had another source of inflation. We believe the rise of DRAM, the move higher in oil prices, and the still present tariffs are likely making the case for interest rate cuts a challenge. We are even hearing calls for rate hikes, a scenario that had almost a zero chance of happening a few months ago.

Yet this is far from the worst start to the year for equity markets. Most equity indices are up around 10%, and bond markets are positive. In our view, there remain elevated levels of cash on the sidelines looking to buy on any dip and that is helping to keep a bid to markets and prevent the selloff many had feared.

But at the halfway point of the year, while hard to believe, it's difficult to expect the second half to be much calmer. One overwhelming positive has been that corporate earnings were stronger than expected, and continued earnings resilience will likely remain important. There is also an expectation that the worst may be behind us for the US-Iran war, as neither side seemingly wants this to continue. In addition, there is a new FOMC Chair who must thread the needle of the need to lower inflation and not look like a puppet for a President Trump desperate for a strong

economy heading into the Mid-Term elections. For Canada there remains the unlikely ability to reach an agreement on a new USMCA deal. All these questions will keep investors on their toes and have the potential to elevate volatility.

One nuance to this market that is different from past years, is the amount of new equity and bonds in circulation. After many years of a corporate buybacks shrinking supply, that has flipped. The SpaceX IPO looks to be just the start as other large deals are to follow. On the fixed income side, it has already been a record year for high yield bond issuance. Going back to simple supply and demand models, the underlying support of fewer shares outstanding has gone away, and increased supply is now a headwind.

Summer markets are tricky to predict due to light attendance and lower trading volumes but are notoriously volatile. While investors should be thankful for the positive start to the year in the face of several real struggles, this is hardly the time to get complacent. We believe there will be opportunities for active managers to prove their worth in this environment, and they need to do so. Enjoy the warm weather but be ready to act on market dislocations.

Fund Update

The Pender Alternative Select Equity Fund was lower by -2.8%¹ for the month of June to finish the first half of the year up 19.2%. This compares to the S&P/TSX Composite return of 0.5% for June and 11.2% for the year-to-date. We came into June defensive with a higher amount of cash and an overweight position in precious metals (gold). We had also trimmed exposure to areas of the market that seemed overbought and expensive on a valuation basis. However, the month didn't go as planned as our gold exposure acted as a drag, and several companies we had sold from the Fund kept moving higher. Regardless, it has been a good start to the year, and we are optimistic for the second half.

The strength of the US dollar remains one of the biggest headwinds to the portfolio. We remain positive on the commodity complex due to attractive supply vs demand metrics but until the US dollar breaks, lower prices will be under pressure. On weakness, we have added to this theme with a focus on the senior gold producers, Agnico Eagle Mines Ltd. (AEM), as we believe it should lead the rebound as rate hike expectations fade and the dollar moves lower. On the last day of the month, we added exposure to several of the Mag7 names, Microsoft Corp. (MSFT) and Amazon.com Inc. (AMZN), which have had a difficult start to the year. These companies have been punished as 'AI losers', but the more we look into this, we believe that these Hyperscalers will be leaders in the next cycle. Building a position in the MSFT after its worst month ever seems like a good entry point.

The rise of levered ETFs is also starting to be a concern and might be the cause for some volatile movements this summer. During thinly traded markets, it's usually best to be ready to react to opportunities, and that is what we plan to do. Earnings season will be a key focus for the coming weeks as companies will attempt to justify their price increases. A rotation back towards the cyclicals looks likely for the balance of the year, and we are setting up to capture that.

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¹ All Pender performance data points are for Class F of the Fund unless otherwise stated. Other classes are available. Fees and performance may differ in those other classes. Standard Performance Information for Pender's Liquid Alternative Funds may be found here: <https://penderfund.com/fund/pender-alternative-select-equity-fund/>