

SECOND QUARTER 2025 - NEWSLETTER

Dear Partner,

Here is our portfolio review and commentary for the second quarter.

Performance Review

During the second quarter of 2025, the **TONUS PARTNERS FUND** obtained a gross return of **2.5%**. Year-to-date, the Fund achieved a gross return of **-6.5%**.

Since the inception of the Tonus Composite¹ in October 2007, it has achieved a compound gross rate of return of **11.1%**, compared with **8.3%** for the benchmark².

Portfolio Review

The second quarter got off to a wild ride as markets plunged in April following the U.S. administration's tariff announcements before rebounding sharply from late April to the end of June. Our fund ended the quarter up 2.5%, but it would have done much better had it not been for the 5% drop in the value of the U.S. dollar against the Canadian dollar (more than half our assets are denominated in USD). Year to date, our fund was down, with most of the decline attributable to currency movements (a weaker USD). Given the high degree of uncertainty surrounding the trade dispute, we maintained a very cautious stance that tempered our returns when the market turned bullish in late April. We trust this prudence will prove justified in the coming months. While uncertainty has quickly given way to a momentum rally, the drivers behind our cautiousness still exist today.

Small caps continued to lag, as evidenced by the Russell 2000 Index, which posted a -6.6% return in Canadian dollars in the first half of the year. The volatility around single-name price movements continues to be elevated, amplified by momentum trends. Stocks that are trending down have no buyers, while popular stocks have nothing to stop them from rising. These short-term price fluctuations are opportunities for us to add/sell at attractive levels and reap larger benefits over the long term.

It's Garage, not Garbage

An excellent example of this phenomenon is **Groupe Dynamite (GRGD - \$26.25)**, a company providing women's apparel under the Garage and Dynamite brands. The company has posted impressive financial results for the past three years and has plenty of room to grow. It currently

¹ Please see page 4 for a description of the Composite.

² Please see page 4 for a full description of the benchmark along with its historical returns

has 300 locations. With only 115 stores south of the border, we think they could easily double their number of units. We bought in at the end of 2024 at an average price of \$20. We believed its business model was robust and felt its valuation, which was much lower than its peer group, was compelling. However, when the markets gyrated along with global trade negotiations, its stock price dropped to \$11. The company had already confirmed the current favourable business trends, but buyers for the stock had vanished. We took advantage of the situation and scooped up more shares, doubling our holding and reducing our average price to \$16. After posting another good quarter in June, the stock rebounded significantly. Long-term investors like us benefited as bank analysts (sell-side) warmed to the story and, after witnessing a substantial rise in the stock price, upped their investment recommendation to a strong buy. The price keeps rising on lift from strong momentum: It closed Q2 at \$26.25.

The gain has been impressive, but we believe there is still more to come. When we originally bought the stock at \$20, we felt it could double in the medium term. Six months later, we still do. GRGD's supply chain and inventory management is second to none. Almost half their merchandise takes less than 8 weeks to go from purchase order to shelves. This allows the company to manage its cash cycle more efficiently and limits the size of orders. With less inventory on hand, hardly any of their products need to be marked down. Indeed, 95% of their sales are transacted at full price. As a result, their gross margins are fat, their return on capital is remarkable, and their footprint has ample runway to grow. It took other investors a while to come around to the stock, but we are not surprised they did, because the stock is still nowhere near its ceiling.

Rebound to come

Not all our laggards have rebounded like GRGD for now. Their negative impact this year on our performance was amplified by their weight in our portfolio. Some of our largest positions to start the year declined in the first half. Two investments in particular, after a stellar performance in 2024, gave back some of their gains. **PowerFleet (AIOT - \$4.31)**, a provider of telematics solutions (fleet tracking, driver monitoring, video recording, asset management), is down 35% this year after doubling in 2024. Management slightly tempered expectations for profit growth in 2025 on the back of extended customer decision cycles caused by the uncertain global macroeconomic conditions. The stock dropped and continued to slide even if no further negative news emerged.

Uncertainty aside, the factors that initially drew us to the stock have not disappeared: a low valuation, an attractive business model and, despite the downward revision, an expected 25% increase in profits this year. The bar is low and we believe investors will eventually recognize what we like in this name and rush back in once the company reports improved results. We will then expect analysts, none of whom currently rate AIOT as a top pick, to hike their recommendation and push the stock higher. Keen readers may notice that we rarely talk about sell side analysts as we prefer to conduct all our research internally. That being said, when (even after missing a nice rally) they up their recommendations and further boost the share price, we welcome these heightened gains.

A second stock that has impacted our results year-to-date and that should bounce back is **National CineMedia (NCMI - \$4.85)**, a company that operates the pre-show advertising in most cinemas in the United States. The stock rose 60% in 2024, but is down 27% this year. Their financials are driven by two factors: a) attendance and b) advertising rates. After difficult years on account of the pandemic and the Hollywood writers' strike, a much higher number of movies are set to hit the silver screen in the back half of 2025 and into 2026, which should translate into larger

attendance. Paradoxically, the economic uncertainty is tempering advertiser budgets and forcing the company to find new clients to backfill its inventory. The stock, which reached \$7.50 in December, ended Q2 below \$5. The company has no debt, continues to generate lots of free cash flow, and has a dominant, almost monopolistic, position in the industry. Our downside is limited at current levels. In a downside scenario, the stock will tread water and we will only collect the dividend. We estimate our upside lies above the prior peak. As attendance in movie theatres improves and major advertisers return (both should happen in the coming quarters), this stock could rise significantly.

The trend

In applying our bottom-up research approach, we have observed acute stock price changes of late that have been magnified by momentum investors. These moves, both up and down, are severe, especially for small caps. Their main index, the Russell 2000, was down in the first half of the year while large caps were up. On the way down, which reached panic levels in April, both indices saw a similar number of big gainers (almost none) and big losers (approximately half).

	Small Caps	Large Caps
Index	Russell 2000	S&P 500
1H25 Return (C\$)	-6.6%	0.9%
# stocks	1998	504
Jan 1 to April 8 Distribution of Returns		
% up > 15%	3%	2%
% down > -15%	59%	49%
1H25 Distribution of Returns		
% up > 25%	15%	10%
% down > -25%	25%	4%

When markets rebounded, investors jumped on the rally. Winners will attract eyeballs no matter what, which is evidenced by the fact that both indices had a comparable percentage of outperformers in the first half. Different story for laggards. As money poured back into the S&P500, poor performers rebounded fast (only a few names are still dark in the red). This stands in stark contrast with what small caps have gone through, where one-quarter of the 2000 or so stocks comprising the index ended the first half of 2025 down more than 25%. Less inflow, less investors, less buyers. For many small caps, when they go down, there seems to be no bottom... until there is. As was the case with GRGD! Patience is essential.

As we have stated in the past, small caps are cheaper and have been lagging for quite some time (the last year they outperformed strongly was 2016). Most asset allocators remain under-exposed for now. When money starts flowing back into the category, the returns could be spectacular. As we saw this year with the large cap rebound, these inflows will not only further amplify the winners' returns, they will also draw much needed attention to forgotten stocks that lack visibility. In the meantime, our portfolio is structured to limit our downside risk with stocks trading at low-to-fair multiples. It is well positioned to benefit substantially when small caps are finally re-rated.

Wishing you all a great summer.

Sincerely,



Philippe Hynes, CFA
Partner
July 10, 2025



Aaron Warnongbri
Partner

For reference, find below the historical gross returns of our North American equity strategy:

Tonus Composite Performance – As of 06/30/2025

	<i>Tonus Composite (Gross Returns)</i>	<i>Index</i>
3 months	2.5%	6.9%
6 months	-6.5%	3.9%
1 year	10.0%	17.8%
3 years	25.0%	16.1%
5 years	20.1%	14.4%
10 years	10.4%	10.1%
15 years	12.5%	11.2%
Since Inception	11.1%	8.3%

Source: FactSet Research Systems, Inc.

Returns are gross of fees and calculated using a time-weighted rate of return. Past performance is not indicative of future results. Returns greater than 1 year are annualized. Benchmark consists of 25% Canadian Large Cap TR + 25% Canadian Small Cap TR + 25% U.S. Large Cap TR (\$CAD) + 25% U.S. Small Cap TR (\$CAD).
U.S. performance adjusted for US dividend withholding taxes

Please note that Tonus Capital serves as the investment manager for the Tonus Partners Fund. Historical returns shown are for the Tonus Partners Fund. Prior to January 2016, the returns are from the Tonus Select Fund from October 2007 to October 2011 and from the weighted average of all managed accounts (including those accounts no longer with the firm), using the same strategy implemented in the actual Tonus Partners Fund, from November 2011 to December 2015. Although the structure and the name of the investment product changed, it had for the entire period the same investment mandate, objectives, strategy, and benchmark. Past returns are not necessarily indicative of future performance. At any moment, the portfolio composition may vary widely from the benchmark. Returns are gross of fees and in Canadian dollars. Any investment in the Fund is speculative and involves substantial risk, including the risk of losing all or substantially all of such investment. This document is not to be construed as a public offering of securities in any jurisdiction in Canada and is for informational purposes only. While the information and material in this document are believed to be accurate at the time they are prepared, Tonus Capital Inc. cannot give any assurance that they are accurate, complete, or current at all times. The Tonus Composite was created October 31st, 2007 and the Tonus Partners' Funds was created January 4th 2016.