PENDER FIXED INCOME

THE MANAGER'S MONTHLY COMMENTARY – JANUARY 2023

The Pender Corporate Bond Fund returned +2.2%[1] in extending its rebound from 2022 lows amid generally strong market conditions.

Most of the Fund's holdings rose in the month, as lower benchmark yields coincided with narrowing spreads for corporate bonds. Some of the more significant performers included positions in discounted convertible bonds as holdings in Eventbrite Inc., Liberty TripAdvisor Holdings, Inc. and Esperion Therapeutics Inc. each gained in excess of 10% in January. Our investment in the capital structure of Forum Energy Technologies Inc. continued to perform well as the equitization of a portion of the issuer's convertible bond occurred into a period of strength.

The Fund had relatively few positions that detracted from performance in January, although one weak spot was in the Fund's relatively small holdings of re-org equity securities, which faced volatility despite no fundamental business erosion being apparent at the issuer level.

Keeping Things Simple

2023, at least what we know of it so far, is not the most straightforward year. The macro picture is full of unusual relationships, such as a steeply inverted yield curve. There is a major war underway and a host of other geopolitical crosscurrents. Faced with these complexities in the broader environment, investors are a little twitchy.

At such moments, it is a good policy to keep things simple. And simplicity, for us, can be expressed through the following ideas:

<u>Invest in a manageable number of ideas:</u> Having multiple holdings, of course, has its benefits. It allows the Fund to distribute maturities by tenor and it provides for some diversification of industry-specific or idiosyncratic issuer risks. But the downside to diversification is that it diverts attention from critical issues and opportunities relating to our portfolio companies. For this reason, we like the ability to focus on a manageable number of names. Over 80% of the Fund is invested in its top 60 issuers. And, given that many of our investment grade issuers like PepsiCo, Inc. and McDonald's Corporation create very little credit drama, we are really able to focus our team's attention on just a few dozen wide spread credits.

<u>Own positions in inexpensive capital structures:</u> In a world where the future seems somewhat uncertain, why invest in the securities of a company where there is little margin of safety? Investing in a company that is fairly valued far more than the trading value of its debt is not just a good return generation strategy; it is a fundamentally simplifying activity. If a business runs into temporary difficulties, having an undervalued capital structure delivers extra benefits. Assets can be sold to raise cash without being dilutive to bond interest coverage. Such a company might also be taken over by a rational acquirer, taking bonds to par. Good things happen to cheap companies. And undervaluation simplifies the life of a credit investor.

<u>Be willing to accept a bit of "boring" weight:</u> Not every deal that comes along is a low-risk structure with large, anticipated returns relative to minimal downside. Rather than force the issue in a market with a fair amount of risk, we feel no shame in holding some weight in a few relatively lower yielding, less

[1] *All Pender performance data points are for Class F of the Fund. Other classes are available. Fees and performance may differ in those other classes.*

intellectually challenging credits. We like the prospects for Pepsi repaying its 2.15% notes due in May of 2024, currently yielding 4.5%. So do a lot of other people. But we think it's OK to accept a portion of the Fund being invested for unexciting returns while waiting for fatter pitches to emerge over time.

New Positions

In January, we participated in a successful "reverse enquiry" deal that allowed us to recycle an existing position into a higher coupon, lower-leverage position in the same issuer, W&T Offshore, Inc. Our pitch to the company through our intermediary was that while we believed they would have been able to refinance an existing November 2023 bond issue on its November maturity, the presence of a large current maturity on the company's balance sheet created an overhang over the whole entity. Instead, we suggested the company repay its existing $552 million and issue a three-year note of half that size, drawing down some of the company's ample cash on hand. The company and its advisors agreed with the merits of our suggestion and issued a replacement note of only $275 million.

A nervous market, W&T's small issuance size, and a punitively low rating from Moody's required the company to market the three-year replacement deal at an 11.75% coupon. Considering W&T's total proforma debt to 2022 EBITDA is well below 1.0X, we were happy to take on this "cream puff" exposure, joining the top ranks of the issue's holders list alongside company management.

Also in January, we added weight to our existing bond holdings of Darling Ingredients Inc., where we added to the 6% 2030 notes at a modest discount to par. We like Darling, whose business entails the collection and recycling of grease drippings and used cooking oil from restaurants, processing these materials, and then selling them into diverse ingredients markets for end uses such as cosmetics and skin care. A public company since 1994, Darling has never posted an EBITDA loss. In the past 12 months, Darling's Operating income covered interest charges by over 10X.

Fund Positioning

The Pender Corporate Bond Fund yield to maturity at January 31 was 7.3% with current yield of 5.5% and average duration of maturity-based instruments of 3.7 years. There is a 2.5% weight in distressed securities held for workout value whose notional yield is not included in the foregoing calculation. Cash represented 3.2% of the total portfolio at January 31.

Geoff Castle
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