Manager's Commentary

Geoff Castle

Highlights:

- Positive contributors to the Fund were Cineworld Group PLC and Federal National Mortgage Association (Fannie Mae). Detractors included Canadian rate-reset preferred shares due to negative price momentum, and Emergent BioSolutions, which we have added to on price weakness.
- New positions include Nuveen Quality Municipal Income Fund (NAD US Equity), a closed-end fund that holds a variety of highly rated US municipal issues, and bonds in Mexican national oil company, Petroleos Mexicanos (Pemex).

The Pender Corporate Bond Fund returned a modest 0.1%[1] in August, a period that was characterized by slightly higher benchmark rates and selective risk asset weakness.

Stronger positions included our stake in reorganized Cineworld Group PLC, as the striking success of the "Barbenheimer" double-header drew attention to the rebound in the cinema industry and this capital structure, in particular. Our longstanding position in Federal National Mortgage Association (Fannie Mae) preferred shares also rallied on a $612 million federal jury award – a sudden and positive development in the ongoing effort to recover post-financial crisis earnings "swept" into US federal coffers.

However, the Fund's positive movers were largely offset by several lower marks in a somewhat illiquid August market. Of note, Canadian rate-reset preferred shares were generally weaker, as negative price momentum outweighed their attractive valuation fundamentals. Our holding of bonds in the US specialty pharmaceuticals player Emergent BioSolutions fell on a ratings downgrade. We continue to like the position, now priced at 48% of face value, and added weight on the price movement.

We've Come a Long Way (Baby?)

It was only three years ago. In August of 2020, with the world still in the full throes of a pandemic, the 10-year US Treasury bond traded at 0.5% yield to maturity. At the time, relative to many other sovereign bonds, 50 basis points amounted to juicy compensation. $18 trillion worth of global bonds that year were yielding less than zero. Now, there are none.

In the two years immediately following the extraordinary, generational lows of bond yields, asset prices exploded to the upside. 2021 was a year of unicorns, SPACs, cryptocurrency, NFTs and IPOs. In 2022, re-opened economies demanded goods faster than they could be produced, ports clogged, and supply chains screamed "uncle!"

[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.*

Now we sit with a risk-free Fed funds rate of more than 5%. US money supply, as measured by M2 has shrunk by more than 5% since Q1 2022. Central banks are in quantitative tightening mode. We don't know for certain what the outcome of such shock therapy might be. But if a massive easing of monetary conditions was enough to unleash an asset price boom, then doing the opposite might result in something more akin to a bust.

This is no moment to be lulled into complacency by the tranquilizing effect of generally rising prices. We continue to hold a relatively large weight in investment grade issues. Where we are adding weight to non-investment grade securities, we are looking for very stark valuation anomalies combined with demonstrable near-term catalysts.

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Portfolio Activity

In August, we initiated a position in the Nuveen Quality Municipal Income Fund (NAD US Equity) a closed-end fund that holds a variety of highly rated US municipal issues. Trading in the market at a discount to daily-calculated net asset value of over 15%, we are attracted by total return prospects. We see potential total return over the next 12 months in the mid-teens in the event that the NAV discount trends back towards its longer term average of 6% combined with even a modest reduction in municipal bond yields.

Also in August, we added a position in bonds of Mexican national oil company, Petroleos Mexicanos (Pemex). Pemex bonds have recently been under pressure due to deteriorating operating metrics and many series now yield in excess of 11%. The spread of Pemex bonds in comparison to the US dollar sovereign bonds now sits at an historic high. While we believe the problems of Pemex are non-trivial, the prospect of meaningful central government support for Pemex, either in terms of reduced cash transfers from Pemex to the central government or in terms of governmental credit support for Pemex, creates credit value opportunities for investors in Pemex's dollar bonds here.

Fund Positioning

The Pender Corporate Bond Fund yield to maturity at August 31 was 8.5% with current yield of 5.8% and average duration of maturity-based instruments of 3.3 years. There is a 3.8% weight in distressed securities held for workout value whose notional yield is not included in the foregoing calculation. Cash represented 2.7% of the total portfolio at August 31.

Geoff Castle
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