

Manager's Commentary

Geoff Castle

The Pender Corporate Bond Fund enjoyed a profitable July, returning 1.5%¹. The good result was due to a number of holding-specific catalyst events that allowed the Fund to outperform benchmarks.

One key contributor for the period was our stake in the capital structure of **Esperion Therapeutics Inc.** Management's successful efforts in extending the cholesterol-lowering drug maker's patent runway to 2040 through agreements with generic drug companies, led to double digit percentage increases in Esperion's stock and bond prices. Another contributor was our position in convertible notes of **Wolfspeed Inc.**, North America's leading producer of silicon carbide substrate for semiconductors. Wolfspeed's June 30 pre-packaged Chapter 11 filing, which shaved off over \$5 billion in debt from its capital structure, positions the company well to capitalize on the high demand growth in this area. Our notes increased in price by over 20% through July as market participants re-assessed Wolfspeed's prospects considering this recapitalization. Finally, **Petroleos Mexicanos** ("Pemex") debt rallied as much as 10% for reasons discussed in greater detail below.

Offsetting broad-based strength, a few distressed files were significantly weaker in July. These included both **Spirit Aviation**, where we believe unreasonable pessimism exists against an improving fundamental picture for the company, and **New Fortress Energy**. In the case of New Fortress, where secured bonds have traded into the mid-30's, the look-through value, even in the event of bankruptcy, seems quite attractive to us.

Pemex is Mexico. Mexico is Pemex

July proved to be a positive turning point for our position in Pemex bonds which, with an issuer level weight of three per cent, is the Fund's largest exposure to any corporate entity. Since the summer of 2023 the Pemex 6.75% notes have risen from the low 60's dollar price to \$77 at the end of July, delivering an internal rate of return of more than 20%.

In 2023, Pemex was clearly in trouble. Over two decades, the state-owned company's cash generation had withered due to declining production in its upstream business and operational problems in its refining complex. High levels of cash transfers to government had left the company without the resources to reinvest in production and government policies that capped consumer fuel prices did not help.

However, what we saw at the time, and what has since become more clear, was that Pemex had important but unrealized sources of credit strength. First, the company owns essentially

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 Fixed Income Funds may be found here: <https://www.penderfund.com/fixed-income/>

100% of the hydrocarbon resources in Mexico. Although Pemex had not yet taken full advantage of its resource base, it was clear to us that its undeveloped Mexican assets were still worth quite a lot relative to its debt.

And the second factor we saw was that the government of Mexico clearly had debt capacity which could be used to bail out Pemex. In August 2023, Mexico's 10-year USD bonds yielded 5.8% while Pemex 2033 USD bonds yielded about 12%, a yawning gap of more than six per cent. Seeing as the interest charges on both Pemex and Mexican sovereign debt ultimately are paid by the same taxpayers, it seemed logical to us that a determined central government could collapse the spread. In that respect our thesis was simply that Pemex is Mexico and Mexico is Pemex.

The election of Claudia Sheinbaum as Mexican President in October 2024 has set in motion policies which allow Pemex to capitalize on its unrealized sources of credit support. Her government has made constitutional amendments that have now allowed Pemex to joint-venture new energy development projects with international oil companies. That step will allow Pemex to return to production growth using foreign capital instead of its own, slashing capex needs going forward. In July, Sheinbaum's government also raised USD \$12 billion in asset-backed "P-Cap" notes. This transaction artfully navigated the problem of how to bail out Pemex without resorting to formal government of Mexico guarantees on Pemex debt (which had the potential to lower Mexico's sovereign credit ratings).

With Pemex on the path to financial sustainability, we see the potential for Pemex's debt, which still sports yields of over 9% in the longer tenors, to come in line with benchmark Latam "BB" yields of approximately 7.5%. So there is still upside in this picture, although a fair amount of the points potential in the bond prices has now been realized.

New Positions

In July we extended our position in the 10% secured notes of **Rivian Holdings**, which represents the top \$1.25 billion of a capital structure valued at more than \$15 billion. We see Rivian making significant progress in terms of growing its topline while reducing cash losses as its brand becomes established as the leading electric truck/SUV player in North America. The company's \$7 billion cash pile and \$7 billion in additional tangible assets provide further credit support to this unrated bond issue, which ended July yielding more than 11% to a 2031 maturity.

Also in July we initiated a position in the unsecured bonds of **AppLovin Corp.** AppLovin runs a marketplace that matches advertisers with the owners of mobile applications which allows the "app" sponsors to generate revenue on a pay per click basis. Applovin has grown quickly to be the largest independent advertising marketplace in the mobile application space, and currently generates over \$4 billion annually in gross margins. At the 2031 tenor, Applovin's split-rated bonds yield more than 130 basis points over treasuries, notwithstanding EBIT coverage of interest that we estimate at more than 10 times. We view 1 year default probability for Applovin at less than 0.1%.



Fund Positioning

The Pender Corporate Bond Fund yield to maturity at July 31 was 5.63% with current yield of 5.16% and average duration of maturity-based instruments of 4.06 years. The Fund holds a 5.15% weight in distressed credit instruments where positions are held for a target value lower than par, and therefore the headline yields of these securities are not included in the foregoing calculation. Cash represented 1.5% of the total portfolio at July 31.

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