PENDER
CORPORATE BOND FUND

THE MANAGER'S MONTHLY COMMENTARY – AUGUST 2017

The Pender Corporate Bond Fund had a flat result in August, neither losing nor gaining materially in overall net asset value. A group of bonds that declined in price offset the coupon income we received from our investments. Nevertheless, the month was an important period from the fund management point of view as we added several new positions that we believe will drive further gains going forward.

Credit was tougher in August in general. The Bank of America Merrill Lynch High Yield Index spreads widened from approximately 361 basis points to 385 basis points in the month, and we noticed a lot of small downticks within the portfolio, consistent with that overall market move. Particular weakness existed in Vitamin Shoppe and Portfolio Recovery Associates (PRA Group), where weaker than expected quarterly reports drove stocks and related convertible note prices lower.

A couple of bright spots in an otherwise difficult month included Gain Capital, whose 2018 convertible notes increased several points on a refinancing announcement and a group of floating and adjustable rate preferred shares which benefitted from improved sentiment towards this type of instrument in the Canadian market.

Attractive Risk-Reward in Energy Related Credit

After being largely absent from oil and gas credit in 2017, we decided to add some exposure to this area as we began to see shrinking crude oil inventories around the world, healthy looking futures markets and widespread investor pessimism on the sector. Hurricane Harvey, which resulted in devastating impacts to people living in the Gulf of Mexico coastal regions, also reduced production capacity in the oil market temporarily. Given this context it appears possible that oil prices around current levels may be sustainable for some time.

With that backdrop, we established a position in the 9% 2020 second-lien bonds of W&T Offshore, which we purchased at a significant discount to par. W&T is a smaller, asset rich, Gulf of Mexico oil producer which has made significant progress restructuring its debts and lowering its cash costs over the past two years. Based on recent comparable transactions of similar oil resource assets, we believe the asset valuation provides ample coverage of the liabilities to the level of the second lien. Given solid cash generation and relatively low leverage, the company's 1 year Bloomberg default probability is approximately 1.4%. This appears to be reasonable risk to bear in light of a potential yield to maturity in excess of 14%.

Another position added with indirect exposure to oil and gas markets was the 5¼% March 2019 senior unsecured bonds of Texas-based helicopter operator PHI Inc. PHI operates both in the medical emergency helicopter business as well as the offshore oil and gas helicopter market. Although profitability of PHI has declined with the downturn in oil and gas activity, we are comfortable that the value of the company's helicopters, combined with considerable net working capital is sufficient to allow the company to either repay or refinance this $500M maturity. Yielding over 7% to 2019, we see this position as a well-covered short duration bond that can provide an attractive return without being price-sensitive to the overall direction of interest rates.

What to Make of Maple Bonds? (Should "Them Able Leave Forever?")

For most of the past year, we scratched our heads as high quality US bonds rose in yields, while Canadian yields for investment grade issuers remained puny. Clearly we had some company in our bewilderment as the Maple market, that is the market of Canadian dollar bonds issued by foreign entities, has sprung to life in 2017. We believe the driver of the revival of the Maple bond market is the yield gap that has opened between the US and

Canadian government market. Earlier this summer we saw Canada's 10 year bond yielding about 0.75% less than similar duration US Treasuries.

That yield gap in investment grade rates woke up the corporate treasury departments of large multinationals to the idea that they could raise money more cheaply in Canada than in the US. This idea was particularly attractive to entities like Pepsico, Apple and UPS, each of whom have large operating subsidiaries in Canada, because it gives those companies an opportunity to match the CAD assets held by those subsidiaries with same-currency financial liabilities. They benefit not only from a reduced cost of funds, but also by reducing the foreign exchange exposure within their businesses.

"Boring!" you say. Well, it becomes interesting within the context of the Canadian credit market where there has been a shortage of high grade corporate paper, meaning the few top tier Canadian credits (Bell Canada, Power Financial, Thomson Reuters etc.) had been able to access the bond market at incredibly cheap prices. Bell Canada, for example, had 10 year bonds yielding about 2.7% earlier this summer.

We believe the presence of foreign Maple bond issuers may cause a change in the Canadian investment grade bond market. With more high quality foreign domiciled issuers to choose from, investors may decide to ask for additional premiums from existing issuers. Ultimately we think the pressure of new foreign issuance will drive up yields and spreads in Canadian investment grade credit to more attractive levels.

Seeing as we have been largely absent from Canadian investment grade bonds, such a change represents an opportunity for us. And indeed, we took advantage of a decent offer side supply around the time of this past month's Apple CAD issue to establish a position in the April 2019 bonds of NAV Canada, the monopoly operator of Canada's air traffic control system. While the yield of that issue, around 1.9%, is not massive, it does represent a significant uptick from the 1.2% yield for the same issuer earlier this year. Baby steps.

Fund Positioning

The Fund yield to maturity at August 31 was 5.6% with current yield of 4.7% and average duration of maturity-based instruments of 2.5 years. There is a 5.9% weight in distressed securities purchased for workout value whose notional yield is not included in the foregoing calculation. Cash represented 4.5% of the total portfolio at August 31.

Geoff Castle
September 6, 2017

For full standard performance information, please visit: http://www.penderfund.com/funds-and-performance

PENDER
Forward thinking. Finding value.

www.penderfund.com @penderfund PenderFund Capital Management

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the simplified prospectus before investing. The indicated rates of return are the historical annual compounded total returns including changes in net asset value and assume reinvestment of all distributions and are net of all management and administrative fees, but do not take into account sales, redemption or optional charges or income taxes payable by any security holder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. This communication is intended for information purposes only and does not constitute an offer to buy or sell our products or services nor is it intended as investment and/or financial advice on any subject matter and is provided for your information only. Every effort has been made to ensure the accuracy of its contents. Certain of the statements made may contain forward-looking statements, which involve known and unknown risk, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

© Copyright PenderFund Capital Management Ltd. All rights reserved. September 2017.