PENDER FIXED INCOME

THE MANAGER'S MONTHLY COMMENTARY – APRIL 2021

The Pender Corporate Bond Fund gained 0.5%[1] in April, a modest advance within the context of a positive high yield credit market and a neutral period for investment grade issues.

Leading the way for the Fund were positions in the commodity and transportation areas. This group includes the 5% convertible notes of Eagle Bulk Shipping which have rallied over 20% since their addition in February. While we believe the ultimate outcome in our shipping convertible bonds may be much higher, we did sell a portion of this issue in April. Other notable strength in the month included positions in Chemtrade convertible debentures, our stake in Fannie Mae preferred shares, and the rate reset preferred shares issued by Cenovus and Bell Canada.

Offsetting the gains, to an extent, were a few decliners, most notably our position in the reorganized capital structure of McDermott International. While this engineering and construction firm has made progress in deleveraging and rebuilding its order book, its exposure to a major project in Mozambique was a source of concern for some investors in April, given terrorist activities there. We do not expect these issues to have a material impact on McDermott and intend to ride out this particular storm.

What's Left to Go Up? Looking at Healthcare Beyond COVID

Life in the waning days of the pandemic is still governed by that sombre rhythm that first emerged last springtime. Who could have imagined playing this amount of Scrabble? And the boisterous hum of an after work public house? That sound is just another fading memory to accompany one's thoughts while sipping a quiet evening whiskey.

But change is coming. Although tragedy and sickness are everywhere, so too are the signs of the pandemic's end. Vaccination counts are climbing. Cruise ships are accepting bookings. And, although the precise timing of 'back to normal' is uncertain, every day that passes only serves to strengthen the case that COVID's unwelcome interruption of our lives is set to expire.

The foregoing musings are hardly a contrarian opinion. The "re-opening trade" is pretty much street consensus in May 2021. But one corner of the market has so far resisted the enthusiasm that has engulfed movie theatres and airlines. And, oddly, it is healthcare. Not *vaccine healthcare* mind you – Moderna is flying to new highs, up over 10 times – but the rest of healthcare. An area one wouldn't think investors would have forgotten about, given that interviews with Intensive Care doctors typically lead the nightly news, but healthcare sure looks cheap to us.

The idea that healthcare is a re-opening sector is somewhat overlooked. But, as busy as ICU's have been, the rest of the healthcare ecosystem has seen a fall-off in demand as elective procedures are postponed and diagnosis activity has diminished. Rather than visit the doctor about an arthritic knee, or plunk down cash on cosmetic surgery, patients have elected to reduce this activity as part of pandemic-induced social distancing. As the pandemic ends, we expect these areas to rebound.

Themes are one thing, and securities trading at attractive prices is another. What do we like in this space? One area to start with is hospitals themselves. Emergency room subcontractor Team Health, with its secured credit yielding over 6% to maturity looks attractive to us. Smaller city hospital operator Community Health offers similar value in our view.

Drugs, diagnostics and therapeutics also offer interesting value. Top ten holding, Paratek Pharmaceuticals offers extraordinary credit value here, in our view. With Paratek's 4.75% convertible notes of 2024 priced to yield 8%,

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[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.

we see upside in this exposure to the producer of the novel antibiotic Nuzyra. The company's revenue is forecast by the "street" to grow from $47M last year to more than $150M in 2021. Were that fortunate situation to occur we believe there is a chance that the conversion feature of this busted convert may become relevant again, and that an outcome above par may be possible.

Other risk/reward positions in healthcare includes our position in the debt of kidney therapy developer, Tricida Inc. In this case, the company's cash balance exceeds the market value of its debt by a factor of two, and yet the 3.5% notes of 2027 trade at less than 40% of face value, yielding over 30% to maturity. In the spirit of full disclosure, Tricida's struggle with the FDA for drug approval does represent a nontrivial risk, but we believe our low entry price offers good compensation. With renowned hedge fund manager Stephen Cohen's Point72 Asset Management recently investing over $10M in Tricida's common stock, we are no longer devoid of active company involvement in this investment. May fortune favour the bold.

In the shadow of COVID, we view healthcare securities as oddly in the value category. Often priced at a premium for its predictability, healthcare finds itself price discounted for risk. As the pandemic fades, we are considering the possibility for this unusual situation to reverse, in our favour.

New Positions

In April we added a position in the convertible notes of North Carolina-based Lending Tree Inc. Lending Tree operates an online marketplace that matches consumers with competitively priced offerings in areas such as credit cards and mortgages. The company has faced some setbacks during the pandemic as credit card activity, in particular, has reduced. Nevertheless we like the credit and find the company's 0.5% convertible notes of 2025, priced just above 90c on the dollar, an interesting mix of attractive shorter-duration yield (approximately 3%) with not implausible equity upside. We view annual default probability for this issuer at less than 0.1%.

We also participated in a new issue of existing holding SFL Limited, which raised 7.25% bonds due in 2026. SFL is the ship financing business linked to Hemen Holding Ltd, the holding company of billionaire Norwegian shipping magnate, John Fredriksen. As we wrote in our February update, we like the longer-term prospects of the shipping industry at this point and consider SFL to possess both the expertise and the creative disposition to take advantage of a rebound in this area.

Fund Positioning

The Corporate Bond Fund yield to maturity at April 30 was 4.9% with current yield of 4.9% and average duration of maturity-based instruments of 3.7 years. There is a 1.1% weight in distressed securities held for workout value whose notional yield is not included in the foregoing calculation. Cash represented 5.4% of the total portfolio at April 30.

Geoff Castle
May 5, 2021

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PenderFund Capital Management Ltd.