PENDER
ALTERNATIVE ABSOLUTE RETURN FUND

MANAGER'S COMMENTARY – NOVEMBER 2021

Dear Unitholders,

The Pender Alternative Absolute Return Fund finished November with a unit price of $9.91 and distributions of $0.05 per unit[1].

November was the weakest month for the high-yield market since September 2020 as the iBoxx USD Liquid High Yield Index returned -1.06% and the Bloomberg US Corporate High Yield Bond Index returned -0.97%. Spreads widened with the Option Adjusted Spread increasing 50bp in the month to finish at 337bp and the yield to worst for the index finishing at 4.80%, close to a 12-month high. The market had weakened significantly prior to the emergence of the Omicron variant late in the month, mostly driven by market technicals with a heavy supply of new issuance, combined with outflows from the market that peaked at US$3.3 billion for the week ending November 24[2].

Portfolio Update

The Fund had exposure to risk asset hedges in November, which included high-yield ETFs, individual high-yield bonds, equity ETFs as well as individual equity short positions. The Fund had relied primarily on high-yield ETFs as a risk hedge prior to the market volatility, which spiked late in the month. With the dramatic "risk-off" day on November 26, we recognized that the market dynamics had shifted, and the portfolio was repositioned accordingly to protect capital in the event of continued market volatility.

Earlier in the month, the Fund had exposure to some relative value trading in Navient Corp. (Nasdaq: NAVI) as a new issue became available with a large concession to existing bonds in the capital structure. We captured this concession on a hedged basis and once the valuation relationships within Navient's debt structure normalized, we exited our positions.

The Fund was not immune to broad market weakness, as many of our holdings saw their spreads widen in the second half of the month. We added some attractively priced high-quality, high-yield positions, including Bath & Body Works Inc. (NYSE: BBWI) and SS&C Technologies Inc. (Nasdaq: SSNC). Further along the risk spectrum, the Fund added a position in McLaren Finance PLC, which we believe offers good value and has some positive optionality to a potential sale or IPO of the business. The Fund also added a 1st lien secured position in Life Time Group Holdings Inc. (NYSE: LTH), which had sold off multiple points from recent highs, despite the company completing an IPO in October. This significantly reduced secured debt in their capital structure, improving the standing of the 1st lien bond.

In response to evolving market conditions, the Fund increased Option Adjusted Duration to 1.0 years, which we believe effectively neutralizes the portfolio's exposure to rising interest rates, now that credit spreads have widened somewhat. The Fund's equity macro-hedges are in place to help offset the potential for sharp rallies in our treasury shorts, given the potential for strong demand for safe-haven assets when fear is the dominant driver of market dynamics.

---

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

[2] Lipper via S&P Global Market Intelligence

At month end, the Fund was 143% long, with 53% of these positions in our Current Income strategy, 43% in Relative Value and 4% in Event Driven. Forty percent of the Fund was short, including 18% in treasuries to limit exposure to interest rates, 9% individual high-yield bonds and 13% short equities.

We believe that a taper tantrum-type environment is possible based on the Fed's policy being behind the curve with both employment and inflation arguing for higher interest rates. The Fund is now set up with a goal of protecting capital in both risk-off and taper tantrum market dynamics, while opportunistically looking for mispriced securities to drive returns.

Outlook

With the emergence of the Omicron variant and the hawkish Federal Reserve commentary within a week of each other in late November and early December, we believe there is increased potential for volatility, although it is possible that both developments can be navigated without much impact on risk markets. With a strong recovery in risk assets in early December, we believe that markets are generally pricing in a high degree of stability, and while underlying economic trends are positive, there are many known and unknown risks that could cause an uptick in volatility.

Perhaps most importantly, the treasury market has priced in a fairly abbreviated hiking cycle with the 10-year bond trading at about 1.5% at the time of writing. Perhaps the market is accurately projecting a policy error that could bring about a near-term recession. The market might also be reflexively looking at the 2010-2019 period and assuming the future will look like the past. This was the case early in the last cycle as the 10-year treasury approached 4% several times in 2009 and 2010 before recognizing that there was a 'new normal' as the consumer deleveraging cycle took place in the aftermath of the Global Financial Crisis.

The economic fundamentals that should be driving interest rates appear to be quite different this time. In late 2010, 18 months after the 2007-09 recession had ended, there were about 3 million job openings in the US, while as of October 2021, there are 11 million unfilled job vacancies. Housing starts were about 500k on an annualized basis in the US in the second half of 2010, while reported numbers have come in at over 1.5 million annualized every month in 2021, except for February. The bond market is providing a projection of what the future might be, but there is a possibility that it is not accurately pricing in significant changes to the economy brought about by COVID-19 and policy responses to it.

The Fund will dynamically look to add or reduce risk in response to market dynamics. We believe we are well-positioned with a conservative posture to capitalize on attractive and mispriced securities.

Justin Jacobsen, CFA
December 14, 2021

PENDER
PenderFund Capital Management Ltd.