PENDER
ALTERNATIVE ARBITRAGE FUND

MANAGER'S COMMENTARY – APRIL 2022

Dear Unitholders,

The Pender Alternative Arbitrage Fund (PAAF) ended the month of April 2022 with a NAV of $10.23 per unit[1].

After a slow-down last month, M&A activity is picking back up with the value of global deals rising 23% in April[2]. Global M&A totaled $1.4T at the end of April, down from the record $1.8T level at this time last year but still representing the third highest level on record. Notably, there has been a rise in mega-deals of mergers greater than $5B with 12 mega-deals announced this month, up from six in March. The tech sector continues to lead activity with $345M of deals announced through April, the second-highest total on record. The tech sector represents nearly a quarter of M&A deal value YTD and is also the most active sector for deal volume. Much of this activity has been driven by private-equity led leverage-buyouts of technology businesses which have seen their valuations cut significantly in the last few quarters with rising rates and the broader sell-off in many growth companies. Savvy financial buyers looking to deploy capital into acquisitions, despite spiking inflation, risking rates and geopolitical tensions, speaks to the opportunity and suggests a robust environment remains for merger activity.

The negative impact of the SEC's new proposed rules for SPACs discussed in last month's commentary is weighing on the SPAC sector with a notable drop in SPAC IPOs. A record 21 SPAC IPOs seeking to raise $6.9B were scrapped in April bringing the total number of SPAC IPOs called off this year to 62, which were collectively seeking to raise over $17B[3]. With over 600 SPACs seeking a target, the new SEC rules impeding the ability for SPACs to find, and ultimately close, a business combination with a target as well as the poor performance track records for de-SPACs, sentiment in the sector has gone from bad to worse. This has resulted in SPAC arbitrage spreads widening with an expectation that we will start seeing a wave of liquidations over the coming quarters as hundreds of SPACs which raised billions in capital will mature and return the cash raised to investors. At the end of April, SPACs searching for targets were trading at a discount to trust which provides a yield-to-maturity in excess of 2.85%[4]. While the current SPAC arbitrage opportunity may be short-lived and transient, it offers highly attractive risk-adjusted returns and could see a growing presence in the Fund over the next few months.

Portfolio Update

While April was an active month globally with a pick-up in M&A activity, it was a relatively slow month for the PAAF. The Fund initiated positions in six new or previously announced merger deals with 11 deals closing. We are monitoring many of the deals announced over the past few weeks, waiting for an attractive risk-adjusted entry point which may be spread, deal-risk or timing-risk dependent. Reflecting that we are in the midst of an aggressive rate hike cycle, we are focusing on merger deals with shorter durations, initiating positions in existing deals with the majority of approvals in place, avoiding deals with extension risk and increasing our exposure to mergers we believe have a short period to closing. The Fund's positioning remains focused on smaller deals which provide attractive spreads, mispricing opportunities resulting from a lack of followers and are subject to lower regulatory risk. The opportunity with SPAC arbitrage is increasingly compelling as we enter a period over the next few quarters where hundreds of SPACs will likely mature without finding a target and liquidate their trust value, returning cash to shareholders. As the duration of these SPAC arbitrage investments shortens to a similar period as merger arbitrage, roughly three to five months, there could be an opportunity to increase the Fund's SPAC exposure.

Coherent, Inc. (NASDAQ: COHR), Tufin Software Technologies Ltd. (NYSE: TUFN), SailPoint Technologies Holdings, Inc. (NYSE: SAIL), Redline Communications Group Inc. (TSXV: RDL), American Campus Communities, Inc. (NYSE: ACC) and Checkmate Pharmaceuticals Inc. (NASDAQ: CMPI) were among merger deals initiated in the Fund during the month.

Level One Bancorp, Inc. (NASDAQ: LEVL), Veoneer, Inc. (NYSE: VNE), People's United Financial, Inc. (NASDAQ: PBCT), Vigil Health Solutions Inc. (TSXV: VGL), SPX FLOW, Inc. (NYSE: FLOW), WOW! Unlimited Media Inc. (TSXV: WOW), Houghton Mifflin Harcourt Company (NASDAQ: HMHC), SOC Telemed, Inc. (NASDAQ: TLMD), Spirit of Texas Bancshares, Inc.

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[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] *https://www.investmentexecutive.com/news/research-and-markets/global-ma-perks-up-in-april-refinitiv/*

[3] *https://www.bloomberg.com/news/articles/2022-04-29/palihapitiya-s-ex-spacs-tumble-in-april-leading-industry-plunge*

[4] *https://spacinsider.com/stats/*

(NASDAQ: STXB), Ferro Corporation (NYSE: FOE) and Macro Enterprises Inc. (TSXV: MCR) were among merger deals that closed in April.

At the end of April, the Fund had 27 investments in small cap deals under $2B with 21 of those deals under $1B. One of these small cap deals is a new holding, Redline Communications Group Inc (TSXV: RDL), which entered into a definitive agreement to be acquired by Aviat Networks, Inc. (Nasdaq: AVNW). Both the target and acquirer are holdings in the Pender Small Cap Opportunities Fund with RDL being a long-term holding, allowing the Fund to benefit from Pender's existing research, insights and private-market valuation estimates. Pender's equity funds have seen seven take-outs YTD with the majority of those deals initiated as holdings in the PAAF. With the high level of merger and leverage buyout activity in the US focused on large-cap technology companies, it may only be a matter of time before acquirers move down market seeking out opportunities in small and mid-cap tech businesses where valuations appear even more attractive. Given Pender's equity team's focus and expertise in investing in small/mid-cap technology businesses there is potential for the Fund to benefit from future take-outs. This is particularly beneficial given the regulatory environment where large-cap deals are facing greater scrutiny. The PAAF will continue to leverage Pender's existing insights, analysis and trade execution competencies in small and mid-cap equities, tactically adding value when opportunities are presented.

Outlook

The challenges of navigating the current market environment continues with bruising losses and extreme volatility. The S&P 500 ended the first four months of the year down 13.3%, the worst start to a year since 1939. While the Nasdaq fell 21.2% through April, the largest fall since the advent of the index in 1971. US Treasury yields have also advanced across the board, with the 10 and 30 year rate seeing their largest monthly spike in decades during April. There has been no respite for equities or bonds with the Bloomberg US EQ:FI 60:40 Index declining more than 12% through to the end of April. With traditional assets exhibiting dismal performance, it is imperative that investors consider diversifying their portfolios. The differentiated, non-correlated and absolute returns offered by alternative strategies can complement traditional assets well. Analysis on portfolio diversification recently published by JP Morgan looked at annualized volatility and returns from 1989 through September 2021 and found that the optimal historical portfolio allocation for risk-adjusted returns was 50% equities, 30% alternatives and 20% fixed Income[5].

The US inflation rate jumped to 8.5%, the highest rate in 40-years, with Canadian inflation spiking to a 31-year high of 6.7%. Central bank actions to tame inflation have so far been unsuccessful, with the spike in prices increasing month over month in March despite both the BOC and Fed raising rates during the month. As central banks accelerate their plan of action to tackle inflation, shrinking their balance sheets and undertaking aggressive rate hikes, with more expected to come, traditional fixed income investments remain under pressure. The Bloomberg Global Aggregate Index, comprised of over $61T of assets, is down more than 11% this year while the Bloomberg US Aggregate Corporate Bond Index declined by over 9.5% through April. Merger arbitrage and SPAC arbitrage currently offer a compelling alternative to traditional fixed income. Merger arbitrage returns have historically exhibited a positive relationship with rising rates acting as a hedge to rising interest rates, with low volatility and low correlation to equity markets. Conditions for merger arbitrage remain favourable with a high value and volume of deal activity, wide-spreads and high success rates. The opportunity with SPACs provides a low risk, low volatility yield with an increasingly shortening duration. It is a challenging time for investors but alterative strategies provide tools to navigate through this market environment.

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[5] *https://am.jpmorgan.com/us/en/asset-management/adv/insights/market-insights/guide-to-alternatives/ Slide 10*