PENDER

STRATEGIC GROWTH AND INCOME FUND

THE MANAGER'S COMMENTARY – SECOND QUARTER 2022

Dear Unitholders,

The second quarter of 2022 was challenging for investors. Macro trends from the first quarter of the year continued and the headwinds intensified. The war in Ukraine, elevated commodity prices, and persistent and rising inflation all contributed to investor uncertainty. Central banks have moved swiftly to withdraw stimulus from the economy, raising benchmark interest rates to bring inflation back within target levels. This backdrop drove weak performance across most asset classes.

In the quarter, the S&P 500 Index (CAD) was down 13.4% and the S&P/TSX Composite Index shed 13.2%. So far this year, the S&P 500 Index (CAD) was down 18.6%, while the S&P/TSX Composite Index was down 9.8%. The resource-heavy Canadian market has been buoyed this year by elevated commodity prices, which gave way in the second quarter as the probability of an economic recession grew. The US bond market is on pace for its worst year in history with a first-half loss of 10.4%. Entering the year, the 2.9% decline in bonds in 1994 was the largest ever[1].

In this challenging environment, the Pender Strategic Growth & Income Fund (PSGIF) returned -8.2% in the second quarter, bringing year-to-date returns to -10.1%[2]. Our equity and fixed income holdings ended the quarter lower overall, but outperformed relative to their respective asset classes.

Equities

Within equities, we saw positive contributions from individual holdings, including Spartan Delta Corp. (TSX: SDE) and Burford Capital Limited (NYSE: BUR), while Brookfield Asset Management Inc. (TSX: BAM) detracted from performance.

Spartan Delta has benefited from high oil prices and is firing on all cylinders. This was demonstrated by its first quarter results, which highlighted significant free cash flow and production levels above expectations. The company is de-levering its balance sheet and, in our view, should hit its 0.5x leverage target by the end of the second quarter. The robust operating environment and positive operational results pushed the company's share price higher during the quarter, and we exited our position. We added Starbucks Corporation (NASDAQ: SBUX) with the proceeds, an iconic category leader and dividend grower after it sold off to attractive levels during the market drawdown.

Burford Capital, a leading asset management firm focused on financing litigation, has continued to raise capital in this growing and developing asset class. There is pent-up realization of its potential high-return cases that the company is well-positioned to capitalize on over the next few years, as courts open following pandemic-related shutdowns. These litigation finance assets are not correlated with overall markets and a strong pipeline of cases should underpin the fundamentals and cash flows of the business. We are also closely watching a large case that could be a near-term catalyst for the company.

Brookfield Asset Management sold off during the quarter amid rising uncertainty in the near-term outlook as its earnings are tied to asset markets. The company has a history of counter-cyclical capital allocation, finding high-return investment opportunities in downturns. Despite the pullback, we remain confident in the long-term outlook of rising penetration of alternative investments with investors. We maintain a core position in the portfolio and see the company as a high-quality, long-term compounder.

The portfolio's small-cap investments through the Pender Small Cap Opportunities Fund (PSCOF) detracted from performance in the second quarter. Our holdings in small cap companies sold off in tandem with equities more broadly as multiples have continued to compress in small caps this year. This has created an attractive opportunity in smaller companies where the underlying fundamentals of the business continue to grow at healthy rates. We take a long-term view and have been adding to

[1] Worst since Bloomberg US Aggregate Total Return index was created in 1977.

[2] 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.

high-quality businesses that we believe can compound for many years. For more details on the PSCOF, see the June monthly update here.

Fixed Income

This was a challenging quarter for fixed income markets, as yields continued to rise, and spreads widened. In the government bond market, investors discounted even higher policy rates as central banks continued to tighten. In corporate credit, recession fears led to further volatility, with all tiers of credit exhibiting wider risk premiums, most noticeably for entities without robust current-period profitability.

With the challenges in the second quarter and so far in 2022, the rising and persistent inflation backdrop has been at the centre of it all. We are starting to see signs of slowing inflation with commodity prices rolling over, financial conditions tightening and consumer confidence plummeting. A positive signal that inflation has peaked may be an important potential catalyst for reversing the current market weakness.

In the portfolio, we are continuing to allocate towards the investment grade end of the spectrum, as we anticipate this area will be first to benefit from a waning inflation picture and should also be the most resilient to risks of a recession. Within the high-yield part of the portfolio, we are increasing weights into what we believe are the most economically resilient issuers with strong coverage factors. We are also extending slightly more duration than we have recently as we believe longer-term bonds, at least in the higher grades, stand to generate a higher total return should rates subside.

While these are all directions that we believe are sensible in the current context, we never want to let a top-down strategy prevent us from capitalizing on an excellent bottom-up idea. We therefore continue to turn over rocks, particularly in the deeply discounted segment of the market, to see if we can find situations where market pricing has moved too far. As always, we remain on the lookout for a great risk-adjusted return opportunity in a very low-priced bond.

The Pender Corporate Bond Fund closed the quarter with a yield to maturity of 8.5%, current yield of 5.7% and an average duration of maturity-based instruments of 3.4 years. There is a 2.6% weight in distressed securities held for workout value whose notional yield is not included in the foregoing calculation. Cash represented 1.1% of the total portfolio at June 30. For more details on the PCBF, see the June monthly update here.

Asset Mix

The portfolio ended the quarter with approximately 55% invested in direct equities, 6% allocated to PSCOF, 34% invested in the PCBF and limited cash. The Fund also owns the Pender Alternative Absolute Return Fund and the Pender Alternative Arbitrage Fund in the portfolio at approximately 3% and 2%, respectively. We believe these alternative strategies are well-suited for this environment and should dampen overall portfolio volatility, while delivering low correlation returns to the overall portfolio.

Outlook

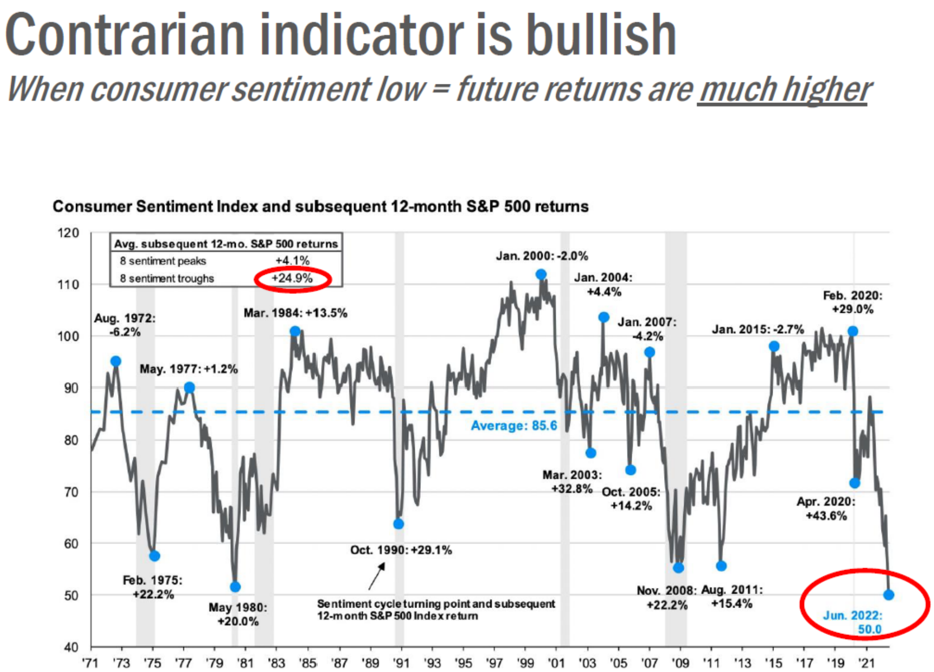
Central banks face the challenging task of engineering a soft landing while facing high interest rates and slowing growth. They have been raising interest rates aggressively and that is expected to continue in the coming quarters. The Fed's fear of allowing an entrenched inflationary cycle to take hold, for the moment at least, seems to take priority over maintaining economic exposure or promoting full employment.

With the macro environment likely to remain murky in the back half of the year, growth has now been repriced and multiples have compressed in equities. Valuations are lower, potentially foreshadowing higher returns. We are seeing better absolute values in credit, as rates have risen, and spreads have widened. We are finding opportunities in fundamentally attractive investments at decent prices. With our equities focused on dividend-paying companies, relatively conservative positioning in our credit portfolio and exposure to alternative strategies as part of the asset mix, we feel this balanced positioning is prudent and allows us to capitalize on the opportunities we are finding in today's market.

Looking beyond gloomy headlines, we believe there is plenty to be constructive about, particularly for investors with longer time horizons. There are some signs that inflation may have peaked, including moderating commodity prices that in most cases have come off their earlier peaks. The Fed's "preferred measure of inflation" is already cooling,[3] which could reduce market expectations for future rate hikes.

The stock market's recent selloff may signal that the U.S. is already in a recession. Economic downturns since 1945 have ranged from two months with the COVID-19 Recession to roughly 18 months with the Great Recession, with the average recession lasting for approximately 11 months. The good news is that the stock market is a leading indicator, which typically bottoms three to six months before the economy in anticipation of renewed growth. We believe the market could be turning around soon if the recession ends sometime in the second half of 2022. The S&P500's first half decline was the worst since 1970. Routs this deep have historically been followed by strong market recoveries in the second half of the year.

Finally, consumer sentiment[4] has historically been a decent contrarian indicator for future returns, providing some empirical backing to Buffett's advice: *"Be fearful when others are greedy, and greedy when others are fearful."* When consumers feel optimistic, market returns over the next 12 months tend to be more modest. When consumers feel pessimistic, returns over the next year tend to be well above average. The US Consumer Sentiment Index hit *an all-time low* in June 2022. Time will tell if this is potentially another wildly bullish market signal for the year ahead.



Source: JP Morgan

Felix Narhi, CFA & Geoff Castle
July 22, 2022

PENDER
PenderFund Capital Management Ltd.

Standard Performance Information for Pender's Balanced Funds may be found here: https://www.penderfund.com/balanced/
This commentary is subject to the Disclaimer found here: https://www.penderfund.com/disclaimer/

[3] Core personal consumption expenditures (PCE) index was down to 4.7% in May. This is the third straight decline and could lower rate hike expectations.
[4] The US Index of Consumer Sentiment (ICS), as provided by University of Michigan, tracks consumer sentiment in the US, based on surveys on random samples of US households. The index aids in measuring consumer sentiments in personal finances, business conditions, among other topics. Historically, the index displays pessimism in consumers' confidence during recessionary periods, and increased consumer confidence in expansionary periods.