PENDER FIXED INCOME

THE MANAGER'S MONTHLY COMMENTARY – OCTOBER 2022

The Pender Corporate Bond Fund delivered a result of -0.2%[1] in October, a period during which risk-free bond yields continued to rise and some specific credit positions within the portfolio came under pressure.

Bright spots for the Fund included our position in the capital structure of McDermott International, Ltd. as the engineering and construction firm continued to increase its order backlog, bolstering a recovery that has been over two years in the making. Other winners included the 2028 secured notes of PetSmart, Inc., as investors bid up higher yielding bonds of businesses possessing stable earnings profiles.

These gains, however, were offset by lower prices across the investment grade bond complex, which reacted to a higher yield curve. In addition, the Fund had a few specific spots of credit weakness, including our now small exposure to Country Garden Holdings Company Limited which was, frankly, pummeled by a stampede of investors fleeing China's property market.

In addition, our position in first lien credit of National CineMedia, Inc. sold off as that company entered a grace period relating to the negotiation of a covenant waiver. In our view, the cinema sector does appear to offer unique value in the current market as an underlying rebound from the pandemic has been slow to take hold. However, this slowness appears to be driven more by the clunky timetable of major film releases than by changes in end-consumer behaviour. With improved prospects for 2023 theatrical releases, we believe that several stressed or distressed credits in the industry, including National CineMedia, stand to make a solid rebound.

Cheap and Forgotten – A Portfolio of Under-the-Radar Opportunities

We are fortunate to enjoy a flexible mandate that allows us to roam the various credit markets looking for situations with great risk/reward characteristics. With a tip of the hat to Rodney Dangerfield, here are some of our favorite sectors that are getting "no respect."

Specialty Chemicals: This is an interesting sector, usually, as the moats around specialty chemicals businesses tend to be stronger than for bulk commodity players due to supplier discipline and more careful capacity management. However, in 2022, all chemicals are unpopular, and we see some great credit deals. In titanium dioxide, we like **Tronox Holdings plc's** 4 5/8 2029 notes at approximately 77c to yield over 9%, a price which creates the company at its lowest historic EV/sales multiple. In methanol, we like **Methanex Corporation's** 5.65% of 2044, priced near 70c on the dollar, again at a level that rivals the company's lowest historic enterprise multiples over the past 19 years.

Dredging: It's hard to get more under the radar than dredging, but this rather necessary industry enjoys the advantage in the United States of a complete absence of foreign competition thanks to the Merchant Marine Act of 1920, otherwise known as the Jones Act. Here, we like **Great Lakes Dredge & Dock Corporation.** Never unprofitable at the EBITDA level in 16 years as a public company, Great Lakes' 2029 bonds trade at 79c on the dollar to yield just shy of 10%. An acquirer could buy the whole enterprise for a price that approximates 5.5x estimated EBITDA. At an enterprise level, free cash flow yield (excluding swings in working capital) was recently 13%. Good things happen to cheap companies.

Tire Distribution: Everybody's talking about the next generation of electric cars, but who, we ask, is talking about the next generation of tire distributors? No one, as far as we can tell, and that's okay with us. The sheer un-sexiness of tire distribution perhaps explains the unchallenging enterprise value

---

[1] Class F of the Fund. Other classes are available. Fees and performance may differ in those other classes.

multiples of **American Tire Distributors, Inc.** Another company with 10% free-cash-yield to the enterprise level, ATD benefits from an industry not as prone to technological disruption as the auto business and a nice, stable demand as a replacement item. The balance sheet-focused management team continues to drive deleveraging, on a debt stack that is currently around 5.5x EBITDA. We like our senior debt position here that currently yields over 12% to a 2028 maturity.

These credits fit a pattern that we like. The debt, in our view, is cheap. The *enterprises*, in our view, are cheap to their underlying economics. And the business activities, while exposed to some modest economic vagaries, are well tested over a variety of cycles.

New Positions

In October, we picked up a position in the convertible bonds of **Eventbrite, Inc**., a leader in the online provision of ticketing services for trade shows and other small venue events. With an enterprise value less than one quarter of its 2018 peak, Eventbrite has suffered the valuation compression of the formerly popular internet services sector. Nevertheless, the credit profile of Eventbrite is attractive, in our view, as cash exceeds total debt by more than $300 million and the company currently generates over $60 million of free cash flow. We highlight the busted 0.75% converts of 2026, which are priced at 69c on the dollar to yield over 10% to a maturity less than four years away. One-year default probability here is estimated at less than 0.8%.

Another October purchase was in the super priority debtor-in-possession (DIP) term loan of **Cineworld Group plc**, the owner of a variety of global motion picture theatre chains, including the American 7,200-screen chain, Regal Cinemas. As mentioned above, the cinema sector has suffered a lagged re-opening as compared to some other pandemic-affected sectors of the economy, due to a shortage of motion picture releases by the major studios. Cineworld filed a chapter 11 bankruptcy in September in order to reject a number of uneconomic theatre leases, the resolution of which should significantly improve the company's earnings prospects. We purchased a portion of the first lien super-priority DIP loan in the secondary market, which has a senior claim against the company's assets and yields approximately 13%. We like the strong valuation coverage of the DIP and expect that ongoing improvements in theatre attendance in 2023 can further strengthen our collateral position.

We also expanded our position in the 8.75% 2027 notes of **Baytex Energy Corp.**, priced to yield approximately 8% to a four-and-a-half-year maturity. Strong energy prices have led to copious levels of cash generation at Baytex, which has paid down more than $650 million of debt over the past six quarters. We expect deleveraging to continue, which would further reduce the company's default probability, which we estimate at less than 0.3% on a one-year basis.

Fund Positioning

The Pender Corporate Bond Fund yield to maturity at October 31 was 7.7% with current yield of 5.7% and average duration of maturity-based instruments of 3.4 years. There is a 4.1% weight in distressed securities held for workout value whose notional yield is not included in the foregoing calculation. Cash represented 2.3% of the total portfolio at October 31.

Geoff Castle
November 7, 2022

PENDER
PenderFund Capital Management Ltd.

Standard Performance Information for Pender's Fixed Income Funds may be found here: https://www.penderfund.com/fixed-income/
This commentary is subject to the Disclaimer found here: https://www.penderfund.com/disclaimer/