Manager's Commentary

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Dear Unitholders,

The Pender Alternative Arbitrage Fund was down -0.4%[1] in April 2024. The Fund's benchmark, the HFRI ED: Merger Arbitrage Index (USD) returned -1.8% during the same period.

M&A Market Update

Global M&A totaled $1.13 trillion through the end of April up 31% from last year. The US continues to see a recovery in deal activity with transaction volumes up 54% over last year with deal volumes up 34% in Canada[2]. The technology sector leads deal volumes over this period followed by the energy & power and financials sectors. Notably, consumer staples and industrials, two sectors which saw a large pick-up in deal activity in 2023 driven by inflation and companies seeking scale in order to generate synergies to compete, are seeing a decline in activity this year. There continues to be a pickup in mega merger deals with two deals over $10 billion announced during the month of April. This includes Silver Lake Technology Management LLC's acquisition of Endeavor Group Holdings, Inc. (NYSE: EDR), valued at over $21 billion and Johnson & Johnson's (NYSE: JNJ) acquisition of Shockwave Medical Inc. (NASDAQ: SWAV) valued at over $12.9 billion. The return of large merger deals is evidence of improved confidence and financing conditions, particularly for large US acquirers.

Last year saw a decline in private equity M&A transactions as higher interest rates, uncertain markets and challenging financing conditions impacted the ability to complete deals. We have started to see a recovery in PE deal activity this year, with commentary from one of the largest private equity firms, KKR & Co Inc (NYSE: KKR) predicting a recovery in IPO and takeover activity. With over $3 trillion in unsold investments in the private equity industry, the reopening of the IPO and leveraged credit markets is likely to lead to an increase in public debuts and M&A transactions.[3] Despite the market reining in expectations of rates cuts this year and as inflation remains more persistent than expected, banking advisors are suggesting acquirers can no longer wait on the sidelines and need to move on making deals. Unlike the last few years which saw a rapid increase in interest rates, the environment today is more predictable and as companies refinance debt, their cost of capital is readily observable therefore allowing acquirers to price and put transactions together. Historically the current level of interest rates has not been an impediment to deal activity for periods in 2000 and 2007 when the fed rate was also over 5% while

[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.
[2] LSEG - Investment Banking Scorecard, Deal Intelligence | as of May 9, 2024
[3] https://www.ft.com/content/e1c1bfc0-ed89-47ac-be6f-f5775e9a6f4d

experiencing deal volume peaks.[4] With the share prices of buyout targets rising, there is increased urgency for deals and private equity firms with their trillions of dollars in cash reserves are incentivized to complete transactions to start generating fees.

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SPAC Market Update

Following a month of some renewed attention in SPACs largely driven by the media attention and volatile trading of de-SPAC Trump Media & Technology Group (NASDAQ: DJT), April was a return to a monotonous SPAC sector in decline. There were no SPAC IPOs in April with four SPAC deals closing and three SPACs liquidating.[5] As of the end of April, there were 234 active SPACs in the market with assets of $13 billion with 100 of them actively searching for targets. Our positioning in SPACs remains conservative, focused on SPACs liquidating or redeeming and targeting a yield in excess of 6.5%.

At the end of April 2024, SPACs searching for targets were trading at a discount to trust value, which provided a yield-to-maturity of 6.70%.[6] With SPAC arbitrage effectively equivalent to acquiring a Treasury Bill at a discount, SPACs currently provide a similar yield to US Corporate Investment Grade Bonds with lower credit risk, shorter duration and a tax advantage, as SPAC returns are primarily capital gains.

Portfolio Update

The sell-off in equities, expansion in yields and market volatility experienced during April led to a broad widening of merger spreads. We saw the spreads of several deals held in the Fund widen during the month and are subsequently seeing them narrow as these deals close and we harvest those returns. With increased selling volumes and limited arbitrage capital to meet that demand, arbitrage spreads typically widen in the short-term during periods of equity market selloffs. As the various catalysts occur which causes a merger deal to close, those spreads quickly tighten and with a diversified portfolio of deals with different durations those catalysts are occurring at regular intervals resulting in a return profile that has low correlation to markets. We picked away at some deals during this period and remain positioned to take advantage of new opportunities with an expanding pipeline of rumored mergers many of which we anticipate should be definitive in the coming weeks. During the month, the Fund initiated positions in 20 new merger deals with 12 deals held within the Fund closing. We are positioned to take advantage of high quality small and mid-cap merger deals with the closing of serval merger deals near the end of the month providing the Fund with excess capital to redeploy. At the end of April 2024, the Fund had 33 investments in small cap deals under $2 billion, 24 of which were valued at under $1 billion.

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[4] https://www.wsj.com/finance/investing/dealmaking-is-looking-up-as-companies-stop-waiting-out-the-fed-db447738

[5] https://www.spacresearch.com/

[6] https://www.spacinsider.com/

A notable trend in M&A particularly in Canada has been private equity buyouts with management and key investors rolling their equity into the new privatized company. These effective buyouts of minority investors have received some pushback from investors as they are similar to management buyouts where there is an asymmetrical information advantage between insiders and minority shareholders which leads to the potential and certainly the perception, that these businesses are being acquire below intrinsic value. While there are clearly governance issues with two types of shareholders who hold equal economic interest on a per share basis being treated differently it also creates conflicts of interests and makes it challenging for minority investors to vote against a merger deal that is supported by management. In many cases a minority investor's investment thesis may be predicated partly or entirely on the founder or management team of a company and their ability to create value for the company. When that management team supports a privatization transaction allowing them to continue to run the business while maintaining their economic interest, it can't help but feel like management is breaking-up with minority investors. Voting against the merger deal and forcing management to keep the status quo is likely to lead to resentment, conflicts of interest and potential turnover and a sale to another party may not be possible especially if insiders have voting control. With blocking the merger potentially leading to a negative outcome many minority investors may feel forced to support a buyout even if they believe it's below fair value. Examples of these minority buyouts previously held by the Fund include Magnet Forensics, H2O Innovation Inc., Q4 Inc., and Neighbourly Pharmacy.

Montreal based payment processing technology company Nuvei Corporation, a new Fund holding, is the latest example of this type of buyout with the company announcing in early April that they had entered an agreement to be acquired by private equity firm Advent International for $34 per share. The CEO founder of the business, and key investors Novacap Management Inc. and CDPQ are rolling the vast majority of the equity interest in the company resulting in them collectively owning 54% of the privatized company.[7] With these three investors collectively representing 92% of the voting power of the company, the transaction has majority shareholder support. While this deal and these sorts of transaction also require support from the majority of minority shareholders, we believe there's a high probability of approval, as even minority shareholders who are unhappy with the business being sold or the price of the transaction are unlikely to vote against a merger backed by the CEO founder. From an arbitrage investment perspective, we are typically indifferent on minority investor buyouts if we have high confidence that the deal can be financed, receive regulatory approval, and have majority of the minority shareholder support in favor of the acquisition. These deals also provide some positive optionality as dissenting shareholder may push back against the buyout and while they are unlikely to block the merger, they may be successful in getting the acquirer to increase the consideration for the deal. With many

[7] https://nuvei.com/company/press-releases/nuvei-enters-into-agreement-to-be-taken-private-by-advent-international-alongside-existing-canadian-shareholders-philip-fayer-novacap-and-cdpq-at-a-price-of-us34-00-per-share/

technology businesses trading at large discounts to intrinsic value, we are likely to see more of these minority investor buyouts.

Outlook

After a euphoric March where multiple assets classes reached all-time highs, April poured cold water on the euphoria halting the market's year-to-date rise. The S&P fell 4.1% in its first monthly decline in 2024 with the NASDAQ down 4.4% and the S&P/TSX Composite Index down 1.8%. Yields on treasuries also rose in the month across the curve with the five-year treasury note seeing a 51 basis point increase. Inflation has proven to be more persistent than expected with the Fed continuing to push out and the lower the projected number of rate cuts this year. Fed officials have suggested that there has been a lack of progress on further lowering of inflation and until evidence of disinflation materializes, rates are likely to remain at current levels. Another hit to sentiment was the lower than expected US GDP growth in the first quarter of 2024, increasing concerns that the economy could experience stagflation. The quick turn in inflation, prices and sentiment demonstrates the risk inherent in traditional markets with both equity and bond prices falling in the month and highlights the potential benefiting of adding an allocation to non-correlated, alternative investment strategies to a portfolio.

While deal activity in our core universe was slow during the month, we continue to expect an increase in small cap M&A driven by both strategic and financial acquirers. We believe valuations for many small cap companies owned or followed by our equity team remain dislocated with activism on the rise seeking to unlock that value. As many of these businesses continue to execute their growth plans and increase their intrinsic value, their share prices are rising even if their valuations remain at a discount. This dynamic is driving increased urgency by acquirers to complete a deal before other investors or acquirers see the opportunity and close the discount themselves. Even with interest rates remaining at high levels, advisors, investment bankers and the companies themselves have indicated they expect deal activity to rise as urgency and incentives drive buyers and sellers to reach an equilibrium where a deal can be struck.

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