PENDER
ALTERNATIVE ARBITRAGE FUND

May 2024

Manager's Commentary

Amar Pandya, CFA

Dear Unitholders,

The Pender Alternative Arbitrage Fund was up 0.4%[1] in May 2024. The Fund's benchmark, the HFRI ED: Merger Arbitrage Index (USD) returned 1.6% during the same period.

M&A Market Update

Global M&A totaled $1.29 trillion through the end of May up 24% from last year. Energy & Power, High Technology and Financials are leading deal activity volume on a sector basis with the Telecommunications and Media and Entertainment sectors seeing the highest change in year-over-year volumes. The US Energy sector continues to see a wave of consolidation with the sole mega merger deal in May being ConocoPhillips' (NYSE: COP) $22.8 billion proposed acquisition of Marathon Oil Corporation (NYSE: MRO). This follows the closing of Exxon Mobil Corp's (NYSE: XOM) $70 billion acquisition of Pioneer Natural Resources Company which closed in early May. With oil majors seeking cost synergies and bulking up their reserve base we are likely to see further consolidation in the sector from acquirers who have been on the sidelines watching their competitors gain market share. As we have previously discussed, the completion of key infrastructure projects like LNG Canada and the Trans Mountain Expansion are likely to be catalysts to spark energy sector M&A activity north of the border.

Dealmakers continue to expect a pick-up in M&A activity this year with Barclays PLC. indicating they expect to see 15% to 20% growth in M&A over the next 12 months "as conditions and optimism have improved and a very quiet 2023 left much pent-up deal activity."[2] With inflation decelerating, investment grade and high yield bond spreads tight and equity markets near record highs, there are favorable conditions and increased confidence for acquirors to target deals. This positive outlook on M&A was also reaffirmed by recent Ernest and Young analysis, the EY-Parthenon Deal Barometer which incorporates the latest macroeconomic figures and also estimates that US M&A deal volume will rise 20% in 2024[3]. "This perspective aligns with the EY CEO Outlook survey pointing to CEOs and institutional investors having a positive M&A outlook for corporate deals and PE activity in 2024. CEOs are looking at deal-making activity as a key lever to address their near-term priorities, with the top deal driver being the acquisition of technology, new production capabilities or innovative startups. They are also looking at their current portfolio of assets and operations and considering what will help their longer ambitions. The spike in intentions to divest assets over the next 12 months, which is broadly based across geographies and

[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] https://www.bloomberg.com/news/articles/2024-05-31/double-digit-growth-in-m-a-activity-to-continue-says-barclays

[3] https://www.ey.com/en_us/insights/mergers-acquisitions/m-and-a-outlook

sectors, highlights how far CEOs are along their path to futureproofing for a different environment."

SPAC Market Update

May saw a pickup in IPO activity with three new SPAC debuts raising $600 million in capital, there were also five SPAC deals closing during the month and one SPAC liquidating.[4] As of the end of May, there were 219 active SPACs in the market with assets of $12.5 billion and 99 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 May 2024, SPACs searching for targets were trading at a discount to trust value, which provided a yield-to-maturity of 6.73%.[5] 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.

> "Pender's equity portfolios are primed with many businesses we believe have the potential to be acquisition targets."

Portfolio Update

The rebound in equity markets during the month drove spreads tighter in the majority of merger deals held by the Fund. Several key deals held in the Fund closed during the month after achieving their final approvals. This included some of the Fund's largest positions such as: Tricon Residential Inc, Carrols Restaurant Group, TrueContext Corp and MDF Commerce Inc. We continue to focus the Fund on investing in high quality, small and mid-cap merger deals which offer shorter duration and a greater potential for mispricing. While our SPAC exposure has typically remained in the mid-to-high single digits through the year, the summer months will see a pickup in SPAC expirations which should drive an increase in SPAC redemption and liquidations and therefore a temporary higher weighting of SPACs. We are actively seeking opportunities to add SPAC positions which offer a greater than 6.5% annualized yield. During the month, the Fund initiated positions in 17 new merger deals with 10 deals held within the Fund closing.

While overall M&A activity is higher this year, deal activity within our M&A activity in our core universe has experienced fits and starts with the year starting off strong while activity slowed in late March and April. In the final couple weeks of May we saw a broad pick-up in M&A activity with several small and mid-cap merger deals initiated in the Fund. Based on outlooks from deal makers, conversations with company management, strategic reviews and formal sale processes, we expect elevated activity to persist in the coming months. At the end of May 2024, the Fund had 38 investments in small cap deals under $2 billion, 27 of which were valued at under $1 billion.

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

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

Outlook

Markets were back to making record highs in May with the S&P 500 up 5.0% in the month bringing its year-to-date return to 11.3% while the NASDAQ was up nearly 7.0% through May. Even with falling commodity prices and weak energy tape, the S&P/TSX Composite was up 2.8% in the month. With equity markets broadly moving higher, bond yields declined during the month although persistent inflation in the US has weighed on yields. While inflation has remained higher than hoped by the Fed, April’s CPI data suggested inflation has resumed its slight downward trend with CPI rising 0.3% in the month vs. 0.4% the previous month declining to 3.4% on a twelve-month basis. With US Q1 2024 being revised lower from 1.6% to 1.3% there is concern about the potential for stagflation if sticky prices and a strong job market prevents the Fed from cutting rates as economic growth lags. In Canada the disinflation trend has been more prominent with headline inflation falling to 2.7%. For the first time in nearly three years, headline inflation is within the target range, providing a clearer path to rate cuts. With hard to predict inflation, wage, labour and economic trends, the path forward for the US and Canadian economy remains uncertain.

We continue to see a widening gap between small and large cap company valuations, most prominently in the technology sector where many high quality small-cap tech companies trade at deeply discounted levels. While deal activity in our core universe slowed during March, the pick-up in activity seen in late May is encouraging and we expect it to persist in the coming months. With encouraging outlooks from deal advisors, bankers and CEO survey’s it appears that there is pent up demand for deals with motivated buyers. Pender’s equity portfolios are primed with many businesses we believe have the potential to be acquisition targets. With equity markets broadly higher and the AI, electrification, space and reshoring trends driving growth expectations higher, businesses will be looking to acquire the capabilities and skills needed to compete for the long-term.

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14 June 2024