

## Manager's Commentary

### David Barr, CFA and Sharon Wang

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#### Fund Performance

Our Fund has built upon the strong start to the year, up 4.3%<sup>1</sup> over the quarter compared to the S&P/TSX Composite Index that was down -0.5%, and small cap markets in Canada and the US that were up 0.8% and down -2.3% as measured by the S&P/TSX Small Cap Index (CAD) and the Russell 2000 Index (CAD) respectively. We have been getting used to good quarters in the small cap world being followed by sell-offs, so we were encouraged to see the continued strength in the small cap market. At some point the significant divergence of small cap from large cap performance is likely to reverse itself and two strong quarters suggest we may be close. Recently, weekly ETF flow data showed small cap flows into the IWM Russell 2000 ETF at \$1.9 billion, the second-best week ever, nearly matched by outflows from large cap SPY S&P 500 ETF of \$2.1 billion<sup>2</sup>.

In the previous quarter's commentary, we talked about how M&A is here to stay and well, the proof is in the pudding. One of our largest holdings, Copperleaf Technologies Inc (TSX: CPLF) announced it was to be acquired for \$12.00 per share. While this is short term good news for us unitholders, it is sad to see our compounding with another high-quality Canadian growth company cut short! But this is an occupational hazard of buying high quality companies. Given our track record of identifying companies that get taken out, we often get asked how we identify these companies in advance. The reality is the takeouts are a side effect of our process. When we identify really strong companies that are in the early stages of growth, we are not the only ones that want to own them. Competitors of the investment company or companies within the same industry are also highly motivated to own them.

#### New to the Top 10

During the quarter we took the opportunity to increase our weight in D2L Inc. (TSX: DTOL) (Desire2Learn) and make it a top ten holding. D2L provides cloud-based learning management system (LMS) software to higher education, K-12 and corporate customers. Annual recurring revenue has grown from US\$112 million revenue exiting FY 2020 to US\$188 million at the end of FY 2024, representing a CAGR of approximately 14%. Despite modest market share across its current geographies, D2L has a win rate of approximately 50% for new implementations in higher education. More recently in the quarter, D2L announced the spinoff of SkillsWave to prioritize its core Brightspace platform, which also heightens D2L's focus on balancing growth and profitability. The spinoff is partly owned by the CEO as well as D2L, and D2L is providing a shareholder loan to help finance the company. This transaction was initially frowned upon by shareholders given the non-arms-length nature of the transaction. After digging in, we gained confidence this was in the best interest of all shareholders. We think D2L is well suited to win a notable share of contracts that are upcoming for renewal given Brightspace's differentiated LMS platform.

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<sup>1</sup> 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.

<sup>2</sup> Source: U.S. Weekly FundFlows Insight Report.

On July 25, it was announced that KKR & Co Inc and Dragoneer Investment Group are acquiring D2L's key competitor, Instructure Inc, for US\$23.60 per share (US\$4.8 billion enterprise value). This works out to an EV/Revenue multiple of 6.6x (2025E) whereas D2L currently trades with an EV/Revenue multiple of 1.9x (2025E), which illustrates the discrepancy in public and private market valuations in the Education Technology space. As D2L continues to grow and increase profit margins, we see significant room for share price growth.

### Contributors and Detractors

Our top three contributors for the quarter were Copperleaf Technologies Inc (TSX: CPLF), Sylogist Ltd (TSX: SYZ), and TerraVest Industries Inc (TSX: TVK). These three companies contributed around 5.5% to performance, with the Fund clearly benefiting from the takeout of Copperleaf. On the detractors side, Dye & Durham Ltd (TSX: DND), Chesswood Group Ltd (TSX: CHW), Aviat Networks Inc (Nasdaq: AVNW) detracted approximately 2.7% from portfolio performance.

Chesswood has faced some significant headwinds in the specialty lending space and the CEO recently left the company. We continue to review our thesis on this position, however the company has several large shareholders who are very much aligned with all shareholders. We think the probability of a sale or windup has increased and continue to hold.

### Portfolio Activity

Our portfolio activity has slowed down from the previous few years as we have high conviction in the current portfolio and the top 20. We have predominantly higher quality growth focused companies as larger positions in the Fund, with several interesting special situations as smaller positions in the Fund.

The merger of the Pender Small/Mid Cap Dividend Fund into the Pender Small Cap Opportunities Fund created a number of additional small positions in the Fund and has increased the total number of positions. We expect this to normalize by the end of September.

We were actively trimming and adding to positions in the portfolio during the quarter. With the strong performance, some of our companies went beyond our target weight, so we trimmed those to redeploy into positions that we saw as better opportunities. We continue to find compelling businesses with attractive fundamentals and are encouraged to see that headwinds could be turning to tailwinds, creating an attractive set up for small caps.

### Final Note

On a final note, the Fund recently passed its 15-year anniversary, having launched in June 2009. We are grateful for the support of all of our investors over that period who have adopted a longer-term approach to investing with this asset class. Since inception we have compounded returns at 15.2%<sup>3</sup> through different market environments, employing a consistent approach focused on protecting and growing wealth for investors over time.

**David Barr, CFA and Sharon Wang**

July 29, 2024

<sup>3</sup> 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. Since inception return is from June 1, 2009

