

The background of the cover features a low-angle, black and white photograph of a modern skyscraper with a grid-like facade. The image is partially obscured by large, diagonal, semi-transparent blue and grey geometric shapes that create a sense of depth and movement. The overall design is clean, professional, and modern.

**NEWGEN**

ASSET MANAGEMENT

# **NEWGEN CREDIT STRATEGIES FUND**

Monthly Commentary

**2023**



# NEWGEN

## ASSET MANAGEMENT

**Letter VII – August 2023**

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, ended August with a Class C NAV of \$11.03 and has paid \$0.12 in distributions year-to-date. This compares with \$11.01 at the end of the prior month and the inception NAV of \$10.00. A rough estimate of the breakdown of the Funds YTD gains: ~37% Interest Income, 17% Dividend Income and 46% Capital Gains, the majority of which have been realized. Our Gross and Net Exposures at August month-end were 106%/82% versus 102%/82% at the end of July.

	Price	Yield-to-Worst	Cash Yield	Credit Spread	Rate Duration
Portfolio	92.7	8.09%	6.85%	334 bps	2.05 yrs.
USD HY Index	89.2	8.51%	6.65%	372 bps	3.47 yrs.

Positive Performance	Performance Detractors
IamGold IMGCN 5.75% 10/28 Unsecureds (short)	Brookfield Office Preferred Shares
Calfrac CFWCN 10.875% 03/26 2 <sup>nd</sup> Liens	Cars.com CARS 6.375% 11/28 Unsecureds
Glatfelter GLT 4.75% 11/29 Unsecureds	Canadian Floating Rate Preferreds
‘AAA’ Asset-Backed Securities	

### **Core Corporate (50% of NAV, 24 positions)**

We continued the process we started in July of “high-grading” our Core Corporate Bond portfolio and now have ~20% of the sub-strategy in AAA asset-backed securities and ~37% invested in investment grade obligors. We exited the following positions almost exclusively for valuation reasons, however, concerns about a weakening consumer entered our thinking:

Company	Ticker	Industry
Dave & Busters	PLAY 7.625% 11/25 Secureds	Casual Restaurants
Winnebago Industries	WGO 6.25% 07/28 Secureds	Recreational Vehicle Manufacturer
Concrete Pumping Holdings	BBCP 6% 02/26 Secureds	Concrete Pumping Services
Vista Outdoor	VSTO 4.50% 03/29 Unsecureds	Branded Sporting Goods and Outdoor Products
Great Canadian Gaming	GCCN 4.875% 11/26 Secureds	Casino Gaming

Our strategy of overweighting ‘B’-rated shorter duration secured bonds early in the year has served us well year-to-date and we monetized gains on most of the positions over the last two months. We view the above-mentioned credits as having simple but strong business models, generally well-managed, modestly levered and they all generate decent free cash flow relative to their debt load. We will gladly buy back all the positions at the right price at some point in the future.

### **Event-Driven (~26%, 11 positions)**

Corporate activity picked up during the month and a bunch of new opportunities has led to us having to ration the portfolio and remove lower conviction and/or lower IRR positions in favour of better ideas. Two examples of names we have added:

#### ***Algonquin Power***

We have been studying Algonquin Power very closely for the last 12 months. AQN has a very complex debt structure and has been forced to put its renewables business up for sale and may ultimately look to monetize its large stake in Atlantica {AY} as well. The net result is the Company is shrinking and needs to bring its debt structure inline with its remaining

assets under the constraint of a mandate from the Board of Directors to maintain an IG rating. We think we have found the cheapest instrument in the entire capital structure that will benefit from the corporate actions ahead.

### ***Michael Kors / Capri Holdings***

We accumulated a position in Capri Holdings {KORS 4% 11/24} bonds after the Company agreed to a friendly all-cash take-over by Tapestry {TPR}. We think the merger has strong strategic and financial merit. The pay-off profile of these bonds is asymmetric with little downside should the merger not occur or be delayed. However, if the deal closes quickly our understanding of the financing arrangements is that TPR will need to redeem these bonds early which could result in a +8% IRR. The core risk to the deal not closing is the perceived overlap between the two woman's handbag businesses. The combined entity will have a large market share, and based on how you define the "handbag market," regulatory authorities could take the view that there is too much concentration given that the combined entity controls brands such as Coach, Jimmy Choo, Michael Kors, Kate Spade and Versace.

### **Liquidity Provision (~16%)**

The Fund had ~16% of its NAV in cash and cash equivalents at month-end.

### **Special Situations/Stressed Credit (~13%, 6 positions)**

We monetized our position in the bonds of Glatfelter {GLT 4.75% 11/29}. GLT makes a variety of products such as feminine hygiene solutions, tea bags, face masks and sanitary wipes often using what is called "non-woven" technology [https://en.wikipedia.org/wiki/Nonwoven\\_fabric](https://en.wikipedia.org/wiki/Nonwoven_fabric). For a variety of reasons, the Company entered 2023 with a stressed balance sheet. We bought the bonds at ~64 3/8 cents with the view that the capital structure was stable and new management would execute its new turnaround strategy to improve margins and de-lever the Company. After reporting its Q2 in early August, the Company lowered its fiscal year guidance, so we decided to exit the position but sold the bonds at 69.5 for a +9% gain when you include the coupons. We will revisit if the bonds drop back into the low 60s which we view as closer to fair value.

We accumulated a position in Calfrac {CFWCN 10.875% 02/26} senior secured 2<sup>nd</sup> lien bonds at ~90 cents in July and now expect them to be refinanced anytime between September 2023 and March 2024. The bonds are currently only callable at 102.72 but the call price steps down to 100 in early 2024. If not called, we will continue to clip the ~11% coupon on a performing credit waiting to get refinanced out.

We have one closed-end fund arbitrage position that added to our monthly gains. We are actively engaged with Management of the Fund to improve some of the structural features and help close the gap between the market price to the Fund's Net Asset Value. We hope to have similar success here as we had trading Brookfield Select Opportunities Fund {BSO-U} and Canso Credit Income Fund {PBY-U} earlier in the year.

### **Risk Overlay**

We were quiet in our Risk Overlay strategy during the month.

### **Summary**

We have made some significant changes to the portfolio over the last two months. We have shortened the credit duration of the portfolio, improved its credit quality, and monetized gains in fully valued securities. We have shifted our focus to shorter-term opportunistic event-driven opportunities and are waiting for better entry points in the credits we have surveillance on.



## Letter VI – July 2023

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, ended July with a Class C NAV of \$11.81 before YTD distributions or \$11.01 net of YTD distributions versus the inception NAV of \$10.00. A rough estimate of the breakdown of the Funds YTD gains: ~33% Interest Income, 15% Dividend Income and 52% Capital Gains. Dividends and capital gains provide far superior after-tax returns versus a pure interest income “carry” strategy. Our Gross/Net Exposure at month-end was 102%/82% versus 88%/78% last month as we increased our short positions.

	Price	Yield-to-Worst	Cash Yield	Credit Spread	Duration
Overall Fund**	93.7	7.56%	6.71%	295 bps	2.2 yrs.
Core Corporate Carry	91.4	7.89%	7.02%	349 bps	3.5 yrs.
High Yield Index	89.5	8.41%	6.61%	372 bps	3.5 yrs.

*\*\*Includes our relatively large cash weighting as well as event-driven positions bought for short-term capital gains not yield.*

### Core Corporate (~47% of NAV, 22 positions)

We sold our positions in Great Canadian Gaming {GCCN 4.875% 2026} and Open Text {OTEXCN 3.875% 2029} as they became too rich relative to the credit risk to justify holding. At yields between 6.50%-6.75% for a high yield bond we would rather own higher grade credit assets as this point in the cycle. We booked a modest gain on those two positions. We then rotated the capital into very cheap short duration AAA asset-backed securities trading at a discount to par. This is what we call a “yield give up” where we reduce yield but improve the credit quality and liquidity of the portfolio.

One bond added that we think is mispriced is Chip Mortgage Trust {HEQCN 1.503% 11/24}. These bonds are AAA-rated asset-backed securities tied to low LTV Reverse Mortgages. The business is unique and not well understood. We bought the bonds at 93.91 to yield ~8.05% to the July 2024 call date. Our due diligence revealed that for regulatory purposes these bonds need to be retired in advance of their maturity date meaning a return of principal would occur sooner than the market was pricing thus boosting the IRR of the position. The chart below highlights the stark difference in after-tax returns from bonds trading below par to those trading at par or above which is part of the reason we like them:

	HEQCN 1.503% 11/24 Bond	Typical Par Bond
Price	93.91	100
Yield	8.05%	8.05%
Interest Income / Capital Gain	1.503% / \$6.09	8.05% / \$0.00
Taxes Paid**	\$2.27	\$4.15
After-Tax Return on Capital	5.67%	4.15%

*\*\*Tax is calculated based on Interest Income at 50% and Capital Gains at 25%*

The main point of this table is that we would need to buy a 1-year par bond at around a 11.3% yield in order to achieve an after-tax return equivalent to the after-tax return of the bonds we bought at a yield of 8.05%. Put differently, the after-tax return is around 1.50% better for the discount bond versus the par bond.

We now expect to have close to 10% of the Fund in short duration, low dollar price AAA-rated asset-backed securities. While not fancy, we think these AAA securities are some of the best risk-adjusted positions in the portfolio. Additionally, with much of the return set to be generated from capital gains, these bonds have an after-tax return that is equal to or better than par high yield bonds. Should the overall credit markets back up to more desirable levels we will sell these securities to fund new purchases of higher yielding and possibly longer duration credit assets.

## Event-Driven (~21%, 14 positions)

We monetized a significant position in the credit-focused closed end fund *Canso Credit Income Fund*. After a careful study of the Fund's underlying portfolio, we accumulated a position in Q2 at a discount to the Fund's NAV. We used the Fund's annual redemption privilege to redeem our position at NAV which generated a capital gain for the fund. In addition, we took advantage of propensity of the Fund Manager to buy a portion of the redeemed units during what is called the "Recirculation Period". After redeeming our Units mid-month for cash, we then accumulated a new long position and then sold them into the Manager's bid at a premium to the market value prior to the Recirculation Date.

We traded AT&T CAD Long "Maple" Bonds during the quarter. We may have bought the "low tick" during one of the really dour days for AT&T following the WSJ article about contaminated lead cables. We sold them for a gain several days later.

## Liquidity Provision (~19%)

The Fund had ~19% of its NAV in cash and cash equivalents at month-end.

## Special Situations/Stressed Credit (~13%, 9 positions)

We added one new credit to the portfolio, a busted convertible from a technology company at a yield of 14.25%. The Company is free cash flow positive with an LTV of ~55% but has a levered balance sheet and shorter maturity portfolio. At present, we feel we have the maximum weighting in our Special Situations/Stressed bucket. Net of shorts, this portion of the portfolio yields mid-teens and is highly idiosyncratic with none of the positions in any major indices.

## Risk Overlay

In lieu of rolling our various options structures for July, we elected to short a handful of "high beta" high yield bonds to help neuter some market risk in the portfolio. Due to our large cash position and relative conservative positioning in our Core Corporate Carry bucket we didn't feel the need to spend premium during July. The decision saved the fund some money as liquid credit indices rallied during the month.

## Summary

Corporate credit markets had a decent rally in July. Government bonds yields are now selling off so far in August. At the same time, corporate bond yields remain sticky which spits out tighter credit spreads from the bond math equation. The "soft-landing" narrative has taken hold in corporate credit just like it has in equities. However, there is an old adage in corporate bond investing...*more people have died chasing yield than by the barrel of a gun*. While tempting to chase yield, we are not incrementally adding generic risk to the portfolio given current market conditions. Our game plan in the months ahead:

- Focus on event-driven opportunities that are agnostic to overall macro conditions and whose prices and IRRs are anchored to idiosyncratic events.
- Look for "up in quality, yield give up" trades within our Core Corporate Carry strategy to improve credit quality.
- Maintain healthy liquidity to add risk on "back-ups" in the market from rising spreads or rising underlying rates.
- Attempt to trade the positions we own for advantage and extract a liquidity premium.

One advantage of the Fund's mandate is that we can move along the credit spectrum. We own 1-year AAA asset-backed securities yielding ~6% but also own obscure floating rate perpetual preferred shares yielding > 15%. The end goal is to find the best risk-adjusted return per unit of credit risk. This has naturally drifted us towards a bit of a "credit barbell" portfolio construction. Given our size, there are plenty of opportunities to deploy capital and scale our portfolio.



## **Letter V – June 2023**

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, ended June with a Class C NAV of \$10.97 pre-distribution or \$10.93 post the \$0.04 distribution we paid mid-month. This compares to \$10.86 at the end of the prior month and the inception NAV of \$10.00. Our \$0.04/unit distribution in June represents a 4.80% cash yield based on the inception NAV of \$10.00. A rough estimate of the breakdown of the Funds YTD gains: ~37% Interest Income, 18% Dividend Income and 45% Capital Gains, the majority of which have been realized. Dividends and capital gains provide far superior after-tax returns versus a pure interest income “carry” strategy, so we factor tax efficiency into our investment decisions. Our Net Exposure at month-end was 78% and Gross Exposure was 88% versus 77%/85% at the end of April.

Price	Yield-to-Worst	Cash Yield	Credit Spread	Duration
91.75	8.09%	7.15%	360 bps	2.5 years

### **Core Corporate (50% of NAV, 22 positions)**

Positive Performance	Performance Detractors
Arko Corp. – ARKO 5.125% 11/29 Unsecureds	Argo Group 7% Preferred Share
Carriage Services – CSV 4.25% 05/29 Unsecureds	Victoria’s Secret – VSCO 4.625% 07/29 Unsecureds
GIII Apparel – GIII 7.878% 08/25 Secureds	OI Glass – OI 6.625% 05/27 Unsecureds

We exited our positions in Victoria’s Secret (poor quarter/trends) and OI Glass (valuation). Our position in the Deathcare company Carriage Services (“CSV”) appreciated in value during the month as the Company became subject to an all-cash take-over by Canadian company Parklawn (“PLC”). We have followed the Deathcare space for awhile and were originally attracted to the credit fundamentals of CSV. The position has now turned into an event-driven trade, so we have moved it to that bucket. There is uncertainty on whether PLC’s Brookfield-backed bid will succeed. Other permutations see Service Corp. (“SCI”) as a White Knight or a private equity sponsor buys CSV as a platform to roll up more funeral homes/cemeteries. On many of the nodes along our probability tree we see higher values that where the bonds are trading. Therefore, we did not sell the position after it rallied 4 points from 82 to 86 but in fact added to it. There is a reasonable probability the bonds see a 101 Change of Control Offer or stay outstanding but become the Obligor of a higher quality credit. It is not too often a large-scale Deathcare concern comes for sale we think it will be a prized cow at the auction.

### **Event-Driven (~20%, 12 positions)**

Added Intercontinental Exchange {ICE 3.65% 25} at a price of ~98. These bonds will receive 101 if ICE’s take-over of Black Knight is blocked in federal court as the FTC is challenging the merger or simply the bid expires on November 4th. The upside if we are correct is an IRR of 11.40%. The downside is a ~0%-1% IRR consisting of a 1 pt loss on the bond less interest income waiting for the outcome of the event. We think the odds of the deal breaking are far greater than 50/50

Added Cablevision {CSCHLD 5.25% 06/24} at a price of ~93.5 to yield 13.2%. CSCHLD issued new bonds in April to pre-fund the refinancing of our bonds. Our bonds are not callable, and the interest expense associated with the Company’s revolver drawings is higher than the coupon on the bonds so the Company elected to pay down its revolver instead with the intent to redraw it on maturity. The position is not without risk as the Company is distressed and could try to do a coercive exchange to avoid paying cash to retire the bond at maturity.

We are in the midst of monetizing two very large and profitable event trades in July, one involving the sale of a preferred share position we own back to the Company that issued it and the other a closed end credit arbitrage trade.



## Liquidity Provision (~22%)

The Fund had ~22% of its NAV in cash and cash equivalents at month-end but this number can fluctuate throughout the month depending on the short-term event-driven trading opportunities. As an example, at various points during the month we carried 5% cash awhile waiting for events to play out and liquify.

## Special Situations/Stressed Credit (~8%, 8 positions)

We had a long bonds/short stock capital structure arbitrage trade in a Speciality Finance company that we are now unwinding. We intended to hold the position longer, but the bonds rallied 5-6 points from where we bought them, and the stock dropped over 10% and as a result we made our desired return and will look to recycle the capital elsewhere.

## Floating Rate Perpetual Preferreds

One corner of the credit markets that has piqued our curiosity has been floating rate perpetual preferred shares issued by investment grade companies. These securities typically pay a quarterly dividend based on some floating rate index plus a credit spread. Investors go to great lengths to find assets whose cash flows *increase* with rates & inflation by buying bridges, ports, tolls roads to earn 8%-12%. We think this asset class offers similar characteristics as the longer inflation stays elevated the higher the likelihood that short rates stay elevated which means the higher the cash flow from the security. Thinking about portfolio construction, these securities provide a nice offset to the fixed rate assets in the Fund.

We currently have 8% of the Fund invested in floating rate perpetual preferreds across 5 credits. In many cases the yields are so elevated than even a half dozen or so rate cuts still make them cheaper to their comparable fixed rate equivalents.

Credit	Price (in bond terms)	Cash Yield	Pre-Tax Interest Equivalent Yield	Floating Rate Index	S&P Family Credit Rating
Media/Tech	52 cents	9.4%	12.2%	Canada Prime x 70%	BBB
Pipeline	58	11.8%	15.3%	T-Bills plus Spread	BBB+
Financial Services	61	10.7%	13.9%	T-Bills plus Spread	A+
Real Estate	39	12.5%	16.3%	Canada Prime x 70%	BBB-
Aviation	96	15.0%	12.8%	LIBOR x 2.75	BBB
<b>Total</b>	<b>61 cents</b>	<b>11.9%</b>	<b>14.1%</b>		

## Risk Overlay

The Fund is currently net long corporate credit which means we are inherently short volatility as one can think of a corporate bond as a put option on a company's assets. Corporate credit spreads have historically been correlated to equity volatility and the correlation grows stronger as equities decline in value. A sharp decline in the equity markets alongside a spike in volatility often occurs alongside a widening in credit spreads. Therefore, a long position in volatility is a good market hedge for corporate credit. At the beginning of June volatility collapsed so we initiated a modest long position in the VIX Index to hedge some of the *market* not credit risk of the Fund. In addition, we bought a VIX 20/30 "call spread" that would benefit if VIX spiked above 20 but stayed below 30. Both hedges have gone against us in June as volatility was on a steady decline all month, but the offset was capital gains on our core corporate positions.

## Summary

Opportunities in the corporate credit markets continue to be open at depth. We like our positioning in our Corporate Carry bucket and will continue to clip coupons and collect dividends. The task at hand in the months ahead will be refilling our event-driven pipeline with new opportunity as existing trades roll-off and liquefy.



## **Letter IV – May 2023**

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, ended May with a Class C NAV of \$10.854 compared to \$10.862 at the end of the prior month and the inception NAV of \$10.00. Our Net Exposure at month-end was 77% and Gross Exposure was 85% versus 68%/87% at the end of April.

### **Core Corporate (53% of NAV, 20 positions)**

A quick summary of our Core Corporate carry portfolio. A notable metric is our high allocation to senior secured bonds.

Price	Yield-to-Worst	Cash Yield	Credit Spread	Duration	Credit Rating	Secured %
90.38	8.37%	6.94%	452 bps	3.78 years	BB-	44.6%

Positive Performance	Performance Detractors
Titan International TWI 7% 04/28	Carriage Services CSV 4.25% 05/29
TD Bank TD 8.125% 10/82	Vector Group VGR 5.75% 02/29
Winnebago Industries WGO 6.25% 07/28	Canadian Floating Rate Preferreds

### **Exited Positions**

We sold our position in SeaWorld {SEAS 5.25% 2029} bonds at 91.25 to yield 7% simply on bond valuation relative to credit risk. SeaWorld is very well managed and has a good balance sheet but has a yet to be unveiled plan to build hotels on its amusement properties which could see leverage rise. However, at the right price these bonds could re-enter the portfolio.

### **New Positions**

We initiated a position in the \$400mm senior secured 1<sup>st</sup> lien bonds of G-III Apparel {GIII 7.875% 2025}. GIII is a well managed 3<sup>rd</sup>-generation apparel business started in 1956 that has been public since 1989. The Company sources and markets apparel under brand licenses such as Donna Karan, Calvin Klein, Tommy Hilfiger and Karl Lagerfeld. The Company has: a) no material debt other than the subject bonds, b) \$650mm undrawn credit facility, c) \$175mm of cash, d) +\$700mm market cap, e) \$675mm of accounts receivable and \$709mm of inventory, f) generated ~\$200mm of Free Cash Flow in FY2023. At a 10.5% yield for what is likely to be a 1.5-year duration bond given the propensity of high yield companies to refinance one year in advance of a maturity we think the bonds are good value and therefore accumulated a position.

### **Event-Driven (~29%, 12 positions)**

#### ***Ford Motor Credit Canada ("FMCC")***

We initiated a position in one of FMCC's unsecured bonds with the thesis that they will be upgraded to Investment Grade in late-2023/early-2024. The bonds we own by our math are the cheapest of the dozens of FMCC bonds issued globally across multiple currencies. We bought the bonds with a credit spread of 392 bps which compares to ~285 bps for a similar bond in USD and ~315 bps in GBP. GM Financial, the nearest comparable to FMCC, is investment grade and trades with a credit spread of between 165-195 bps for a similar maturity instrument.

If we assume that FMCC is upgraded to investment grade by March 31, 2024, and the bonds tighten to +50 bps above GM Financial then we could see a +2.50% capital gain plus the 7.375% running coupon for a 1-year total return of ~9.9%.



## *First Horizon Bank ("FHN") / TD Bank Risk Arbitrage*

We purchased FHN bonds under the thesis that TD Bank would ultimately acquire FHN but at a "recut" equity price. Part of our conviction was the motivation on both sides to see a deal through to completion was high, albeit at a lower equity price. We bought our FHN bonds at a credit spread of ~340 bps compared to similar TD Bank debt trading at ~170 bps at the time. Should the take-over have been completed, FHN's bonds would have eventually traded at a similar credit spread and generated a 10% capital gain plus a running coupon of ~6%. Unfortunately, we were wrong as the transaction failed, reportedly based on a yet to be disclosed issue the US regulators had with TD bank anti-money laundering compliance. Once our thesis was wrong, we made the decision to exit the position as tactically as possible. We waited for other risk arbitrage sellers to exit over the first week after the deal broke and the bonds rallied 16 pts off the low and we sold the entire position crystalizing a loss for the Fund.

## Liquidity Provision (~23%)

The Fund had 23% of its NAV in cash and cash equivalents at month-end but this number can fluctuate throughout the month.

## Special Situations/Stressed Credit (~6.3%, 6 positions)

We added two new positions during the month, one short and one long.

### *Mining Company*

The Company is currently developing a new mine and surprised the market by obtaining new 2<sup>nd</sup> lien financing with a group of distressed lenders at a high effective cost of ~14%. The new shorter maturity loan is ranked senior to the bonds and has a maintenance covenant. This transaction is what we call "getting primed". We shorted the unsecured bonds at a yield of <11% and given they mature outside of the new financing and are lower ranked in priority in theory they should trade at a higher yield than 14%. The short is a cheap option on the mine failing to start up which could lead to a covenant breach but most importantly, the bonds should not trade at a materially lower yield than were the new debt was raised.

### *Specialty Finance*

We bought the bonds in a Specialty Finance company at a yield of ~16% and a price < 80 cents. We partially hedged the position with a short position in the common stock as we think there is a disconnect in the valuation of the two parts of the capital structure.

## Summary

Corporate defaults are rising, and credit conditions are tightening. Avoidance of defaults will be key to outperformance in the months ahead. Credit selection is the process of *exclusion* not *inclusion* (i.e., it is the bonds you don't buy that matter more than the bonds you buy). Some prognosticators believe high yield credit spreads are too tight given where we are in the cycle, and we have some sympathy for that argument. A reasonably bad scenario is that spreads widen 200 bps but this likely means a decline in government yields as they are often negatively correlated. If government yields decline by 100 bps this would imply a net rise in high yield bond yields from ~9% to 10% and a 3.7% capital loss on the High Yield Index. However, the running yield on high yield is ~6.7% or 58 bps per month with a yield-to-worst of ~9%. So practically, using the simple scenario math above, if you think credit spreads are too tight and want to "time the market" you need spreads to really blow out in the next 6 months or so to be better off simply holding onto the asset class and accepting the net return of "carry less capital loss" while avoiding the friction costs of buying and selling. *We are being cautious and prudent but the opportunity cost of being too negative on corporate credit is quite high at these elevated yields.*



### **Letter III – April 2023**

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, ended April with a Class C NAV of \$10.86 compared to \$10.79 at the end of the prior month and the inception NAV of \$10.00. Our Net Exposure at month-end was 80.0% and Gross Exposure was 91.5% versus 67.5%/87.4% at the end of March.

### **Core Corporate Carry (44% of NAV, 19 positions)**

A quick summary of our Core Corporate carry portfolio:

Price	Yield	Credit Spread	Duration	US/Canadian
91.1	8.04%	435 bps	3.8 years	61%/39%

Positive Performance	Performance Detractors
Carriage Services CSV 4.25% 2029	Arko Corporation ARKO 5.125% 2029
Baytex Energy BTECN 8.75% 2027	Floating Rate Preferreds
Canadian AT1 Securities	N/A

### **Arko Corporation**

Arko, a US convenience store operator, launched a competing bid to acquire Travel Centers of America ("TA"), after TA agreed to sell itself to BP plc. The complex competing bid would see Arko lever-up and use most of its debt capacity to finance the transaction. The bonds traded down from 84 down to 81 cents to yield 9%. After reviewing the bid, we felt it was unlikely Arko could finance the proposed acquisition which was opposed by TA itself. We took the opportunity to add to our existing position as we like the management team of Arko and while they are no doubt acquisitive, they are good operators. We think the M&A risk is already priced into the credit at 9%.

### **Event-Driven (~29%, 12 positions)**

We closed four event-driven positions during the month:

#### ***Brookfield Select Opportunities Fund ("BSO-U") – Credit-Focused Closed End Fund Liquidation***

On December 19, Brookfield, BSO's Fund Manager, issued a press release stating the following: *"the investment manager, is considering various strategic alternatives for the Fund given its small size. This includes, reducing the Fund's quarterly distribution in 2023, a potential reorganization into another fund or liquidation of the Fund. PSG will provide an update once it determines to advance one of these strategic options and expects to be in a position to do so by the end of the first quarter 2023."*

BSO was trading at \$5.55 at the time even though its NAV was only \$1.76 as the Fund never adjusted its distribution downward as the income from the underlying portfolio declined. Investors flocked to its ~30% yield even though much of the distribution was return of capital. The Fund's own disclosure stated that it paid out way more than they earned. We shorted BSO in Q1 awaiting the event and on March 14 Brookfield announced they were liquidating the Fund and holders would receive the NAV by the end of April. We took a second bite at the apple when the Units traded down to as low as

\$1.25 even through the NAV was \$1.58. We covered our short position and went long the Units on the same day and continued to buy aggressively right up until the Liquidation Date. The Fund received \$1.605 in cash on April 25.

#### *Rogers Communications - RCICN 5.25% 2082 Junior Subordinated Bonds – Index Event*

RCI issued investment grade “hybrid” bonds in February 2022 to finance part of the Shaw acquisition. It was widely known that the credit rating of these bonds would be downgraded to high yield following the closing of the transaction. As expected, on April 6, the bonds were formally downgraded by Moody’s and S&P. The downgrade caused *forced selling* by investment grade index funds and as a result we bought some bonds at an attractive level from an indexer. Then at the end of the month, the bond formally entered a high yield index which then caused aggressive *forced buying*. We then sold the bonds to another indexer at a higher level than where we bought them.

#### *Maxar Technologies – MAXR 7.75% 06/27 Senior Secured 1st Lien Bonds – Make-Whole Redemption*

We accumulated the bonds at an average price of ~105.125 after a thorough read of the bond indenture indicated that as part of the take-private transaction the private equity sponsor would have to redeem the bonds using its “make-whole” privileges. The bonds were redeemed at ~106.5 and we collected a 7.75% coupon while waiting for the redemption.

#### *Seaspan - SSW 6.50% 2026 Senior Unsecured Euro-dollar Bonds – Change of Control Offer*

Our position was redeemed at a price of 101 following a Change of Control Offer. Atlas Corporation, the Parent of Seaspan, was taken private on March 28<sup>th</sup> and as a result the Company was required to offer us a redemption price of 101.

### **Liquidity Provision (~25%)**

The Fund had 25% of its NAV in cash and cash equivalents at month-end but this number can fluctuate throughout the month based on our active trading. We purchased a “hard-called” IG bond during the month at a 6% 30-day yield.

### **Special Situations/Stressed Credit (~7%, 4 positions)**

We finally found a few opportunities to deploy capital within this sleeve. We acquired a position in a security tied to the commercial real estate market at an interest equivalent running yield of ~17%. Having had a bearish position in commercial real estate credit for most of the year we now think opportunities are beginning to emerge on the long side. The constant negative sentiment on commercial real estate, particularly office, has caused a wash out in securities prices across a wide range of credits even though the balance sheet structures, and asset quality vary widely. In addition, we purchased a 1<sup>st</sup> lien secured bond from a performing credit that yields 15%. This was done via the primary market, a first for the Fund.

### **Risk Management Overlay**

- We have maintained our short position in USD investment grade credit spreads because of an expected busy month of primary issuance that could see credit spreads widen from April levels.
- We did not roll our bearish HYG option structure on expiry but instead replaced it with a short position in HYG. HYG is trading at ~50 bps premium to NAV.

We are currently focused on scaling two attractive event-driven trades and harvesting a handful of what we think are profitable existing event-driven trades scheduled to roll-off in the next 3 months.



## **Letter II – March 2023**

The NewGen Credit Strategies Fund, a corporate credit-focused liquid alternative strategy, finished the quarter-ending March 31<sup>st</sup> with a Class C NAV of \$10.79 compared to \$10.56 at the end of prior month and the inception NAV of \$10.00. Our Net Exposure at month-end was 67.5% and Gross Exposure was 87.4%

### **Core Corporate Carry (47% of NAV, 21 positions)**

Our *Core Corporate Carry* sub-strategy positioning remains unchanged from the prior month. We are tilted towards B+ rated senior secured and unsecured paper from US mid-market publicly traded companies. We continue to prefer this part of the credit universe as we think the flight to quality (“BB”) has investors trading off *lower* credit risk for *higher* interest rate risk. Contrarily, we are shunning the lower end of the high yield market (“CCC”) which while much less correlated to interest rates is very exposed to default risk. We are aligning the portfolio to have a reasonable balance between *interest rate risk* and *credit risk* until we have a clearer picture of where we are in the rate/credit cycle. We favour simple businesses that are FCF positive with no near-term debt maturities. A quick summary of our Core Corporate carry portfolio:

Price	Yield	Credit Spread	Duration	US/Canadian
90.3	8.09%	434 bps	3.75 years	49.9%/50.1%

Positive Performance	Performance Detractors
Canadian Bank AT1 securities	Titan International
Arko Corporation	Bluelinx
Cars.com	Floating Rate Preferreds

All our positions except for one bond were purchased on the secondary market and many of the positions we own are “well seasoned” meaning they have been outstanding for a reasonable period. We have been adding to existing positions when Credit ETFs are selling for liquidity.

### **Banking Crisis and Canadian Bank AT1s**

The Fund entered the recent Banking Crisis with ~20% cash, no leverage, de minimis exposure to Banks and *zero* positions (long or short) in very volatile “risk-free” governments bonds. When the Banking Crisis started to unfold mid-month, we dropped what we were working on to focus on the headline grabbing Bank AT1 market. We first sold the very small exposure we had in CAD AT1 securities and rotated into a large weighting in two USD Canadian Bank AT1 from TD and BNS that we view as being the cheapest two bonds out of the dozens of AT1 securities issued by Canadian Banks. We actively traded our AT1 positions throughout the month and as a result the largest contributor to Fund’s Core Corporate Carry sub-strategy was our position in TD’s 8.125% 82 USD AT1 security.

	BNS 8.625% USD	BNS 7.023% CAD	TD 8.125% USD	TD 7.283% CAD
Price (March 16 <sup>th</sup> )	100.625	99.23	99.5	101.14
Yield-to-Next Call (2027)	8.55%	7.11%	8.34%	6.98%
Spread-to-Next Call (2027)	487 bps	423 bps	466 bps	392 bps
Yield-to-Maturity	8.22%	7.30%	7.93%	7.10%
Spread-to-Maturity	453 bps	405 bps	430 bps	405 bps

<sup>1</sup>As a reminder, the Fund does not sell short government bonds on a levered basis to buy bonds issued by Banks.

### **Event-Driven (~20%, 12 positions)**

Our Event-Driven sleeve continues to be the largest driver of returns for the Fund year-to-date. We closed three positions during the month:

- Long IAA 5.50% 2027 bonds against a short position in new issue Ritchie Brothers unsecured bonds. The take-over of IAA by RBA closed successfully, and our bonds bought at ~98.25 were redeemed at 102.75 and we covered the RBA short before settlement.
- Long Intercontinental Exchange ICE 3.65% 2025 with Special Mandatory Redemption. Exited the position after ICE agreed to continue to fight the FTC to close the merger with Black Knight. Our thesis was that the deal was going to break, and we would receive 101 on our bonds.
- Long First Quantum Unsecured Bonds. Company had a positive resolution with the Panama Government around the economic terms and conditions associated with its flagship Cobre Panama Mine and we exited the position bought during the early stages of the dispute.

### **Liquidity Provision (~30%)**

The Fund had 30% of its NAV in cash and cash equivalents at month-end but this number can fluctuate throughout the month based on our active trading.

### **Special Situations/Stressed Credit (~2%, 2 positions)**

Our positioning remaining unchanged as we wait patiently for companies with stressed balance sheets that need capital to come to the primary market. We are currently working on a credit file where we think we can deploy some of the Fund's capital into a senior secured performing credit at a 15% yield. The bogey for us to deploy the Fund's capital into more stressed or special situation credits remains very high.

### **Risk Management Overlay**

- We entered the month with a short position in a *Commercial Real Estate* security as a general risk hedge because of our general worries about the CRE market. However, we ended up monetizing the hedge as the price of the security deteriorated rapidly as the banking Crisis unfolded.
- We initiated a macro short position in US investment grade cash credit spreads during the beginning of the Banking Crisis that helped protect the Fund against a market decline.
- Our bearish option structure on Blackrock's HYG ETF remains intact.

The opportunity set in credit is robust and we hope the ongoing volatility associated with the Banking Sector continues as it opens up more active trading opportunities and gives us a chance to add to our core positions at lower prices.



**Letter I – Feb 2023**

Today marks the second month for the NewGen Credit Strategies Fund, a **credit-focused liquid alternatives strategy** launched on January 1<sup>st</sup>. The current Net Asset Value ("NAV") for the Class C units is \$10.5463 versus our Inception NAV of \$10.00.

A quick summary of the portfolio:

### **Core Corporate Carry (~49% of NAV)**

Our *Core Corporate Carry* sub-strategy is now yielding 7.9%, has a credit spread of 369 bps and a duration of 3.7 years across 22 positions. The portfolio is tilted towards B+ rated senior secured paper from US mid-market publicly traded companies. Examples below:

1. Dave & Busters
2. Bluelinx
3. Winnebago Industries
4. Titan International
5. Vector Group
6. Cars.com

We also have a modest allocation to floating rate preferred shares as well as investment grade junior capital securities from Canadian Banks.

### **Event-Driven (~27%)**

Our *Event-Driven* sleeve has been the largest driver of returns for the Fund year-to-date. One example is a short position in a Closed End Credit Fund that is trading above NAV. While a small focus of the overall portfolio, we see some opportunities in Closed End Credit Funds that primarily hold corporate credit assets trading at material discounts or premiums to their NAV. Another contributor was our trade in the bonds of Resolute Forest Products. We purchased the bonds in January at 99-99.25, clipped some coupon and sold them between 102-102.40 following the announcement that the Company was going to call the bonds as we expected. We anticipate that many of our Event-Driven trades will roll off between 30 and 180 days with several positions tied to situations where a Company or successor entity is required to retire their bonds prior to maturity at a pre-determined price on a defined timeline. We will then look to reload on what we anticipate will be a busy year for corporate events.

### **Liquidity Provision (~17%)**

We are maintaining plenty of liquidity in the Fund at present for two reasons;

1. Ample cash and cash equivalents allow us quickly to fund *Event-Driven* trades that typically occur at random on a daily basis (i.e. an announced merger or asset sale). Often for *Event-Driven*



trades, we need to react within 30 minutes of a press release and having liquidity to build a position without selling something else quickly is important and we don't anticipate using leverage in the Fund.

2. We are being paid reasonably well at present to hold near cash securities relative to longer duration credit assets. Our *Liquidity Provision* portfolio currently yields close to 5% and is composed of cash sitting at our Prime Brokerage account, High Interest Saving Account ETFs and near-term fixed rate corporate bonds.

### Special Situations/Stressed Credit (~4%)

We only have ~4% of the portfolio in *Special Situations/Stressed Credit*. We don't anticipate allocating materially more capital to this sub-strategy at present because we anticipate further credit stress on lower rated credit moving forward. Outside of one isolated position, we hold no debt in private companies, no LBO debt and no CCC high yield paper. Despite seemingly attractive yields on 'CCC' paper, we think there is more pain ahead as lower rated companies struggle to cover their interest payments especially ones with a large component of floating rate debt in their debt structure.

### Risk Management Overlay

We were active in trading listed options tied to liquid credit indices such as the Blackrock's HYG high yield ETF. We have on a bearish options structure that helped cushion some of the market risk for the month of February from our *Core Corporate Carry* portfolio. We took the opportunity to roll forward our option structure an additional month at almost no cost during the largest negative down day in credit so far this year.

### Summary

We are excited about the first few months of the Fund and the opportunity set ahead. The Fund is fully operational with a fully ramped up portfolio ready to be scaled. While we are cautious on the current corporate credit valuations, we continue to find opportunities daily to generate reasonable returns either through corporate events or mispriced bonds under-appreciated by larger credit managers or index funds. The high yield market in North America has +\$1.4 trillion of bonds outstanding across +2,500 issuers and there are tens if not hundreds of press releases and earnings reports on a daily basis to sift through. The Fund is small and nimble enough to deploy capital and take advantage of mispriced corporate credit securities.