

Constantia Capital Merger-Arbitrage Strategy September 2022 Commentary

Our composite returned -0.50% in September, bringing returns to -0.34% for the year-to-date, 3.76% annualized for the past 5 years and 5.01% annualized in nearly 11 years since inception.

Equity and bond markets continue to be spooked by the Federal Reserve's hawkish tone, raising the scepter of global stagflation. Continuing the trend for 2022, both equities and bonds fell during September, with the S&P 500 posting a -9.2% return for the month. The Bloomberg US Aggregate Bond Index fell 4.3%. Two and three year Treasuries and AAA rated corporate bonds are suddenly yielding in excess of 4% annualized and have been rediscovered as an alternative to equities. Making the point of how tough this year has been for investors, the classic 60/40 Equity/Bond benchmark (All World Index, Bloomberg US Aggregate Bond Index) has fallen 21.1% year-to-date.

Some of the highlights and lowlights of the month:

- The largest detractor for September was F-star Therapeutics, being acquired by Sino Biopharmaceuticals. In an unusual step for a very small (\$100 million market cap) biotechnology company, CFIUS not only reviewed the deal but asked for an extended review. That, coupled with negative sentiment in the market in general, resulted in a negative contribution of 28 bps.
- Airlines fell in-line with the S&P 500. Spirit Air, being acquired by JetBlue Airways, fell despite news that JetBlue may be prepared to terminate their code sharing arrangement with American Airlines. That arrangement is seen as an anti-trust sticking point. We believe the latest fear in the market is that a recession may cause JetBlue to be unable to afford the deal. Spirit fell 17% for the month (6% in the last hour based on news of the timing of the \$2.50 special dividend, which almost certainly will reverse on the dividend ex-date later in October), resulting in a negative 19 bps contribution.
- Our largest position, Biohaven Pharmaceuticals, being acquired by Pfizer, continued to increase steadily over the four months since deal announcement as the market has come to realize the value of a spinoff that is part of the deal. The deal is scheduled to close next month, well ahead of the original projection, contributing 5 bps for the month and 16 bps since inception.
- Unity Software is acquiring IronSource. Both are software companies that specialize in monetizing apps by helping companies place ads in their apps. Applovin, a competitor, dropped their bid for Unity, which had been conditioned on Unity dropping their deal with IronSource. That news resulted in the spread on the deal contracting and a positive contribution of 14 bps reversing a negative contribution the previous month.
- Good news related to the Twitter deal was that two firms hired by Elon Musk concluded that the number of bots on Twitter was in the range of 5% to 11%, in line with Twitter's estimates.

Twitter rose 13% for the month, contributing 11 bps. We continue to feel confident that the deal will close, and the spread has contracted to *only* 23% from well over 40% just a few weeks ago.

Not surprisingly for a bear market, new deal announcements slowed down to 18 for the month, while 22 closed. Diversification in the portfolio continues to be considerably above average, although the number of deals has now decreased to 100. Leverage remained at 120% (\$120 of long positions for every \$100 of capital).

Constantia Capital Merger-Arbitrage: Performance as of September 30, 2022

| Benchmark | Reporting Period | Returns (Net) ^{2 3} | Bench-Mark ² | Excess (Net) | Volatility | Sharpe Ratio |
|----------------------|------------------------------|------------------------------|-------------------------|--------------|------------|--------------|
| LIBOR 3-month USD | Year-to-date | -0.24% | 1.37% | -1.61% | N/A | N/A |
| | Latest 3 Years | 3.29% | 0.87% | 2.41% | 6.62% | 0.36 |
| | Latest 5 Years | 3.76% | 1.43% | 2.33% | 5.33% | 0.44 |
| | Latest 10 Years | 4.74% | 0.97% | 3.77% | 4.66% | 0.81 |
| | Since Inception ¹ | 5.01% | 0.93% | 4.08% | 4.55% | 0.90 |

¹ Returns annualized, since inception date 11/1/2011

² Returns annualized for periods in excess of one year

³ Net returns after performance fee, which three qualified clients have elected as of 7/31/2022