Constantia Capital Merger-Arbitrage Strategy
December 2023 Commentary

Our composite returned 1.21% in December, bringing full year returns to 6.42%, 4.25% annualized for the past 5 years and 5.12% annualized in slightly over 12 years since inception.

A year ago, we made the bold prediction that returns for our Merger-Arb composite would be in the range of 7% to 8%, representing short-term cash returns of approximately 4% at the time and a risk premium of 3% to 4%. We were slightly short of that goal, but importantly finished the year comfortably ahead of our benchmark and all the major money market funds, which returned in the range of 5.2% for the year. Further, our composite was ahead of the average of eight Merger-Arb mutual funds and ETF's that we track by **234 bps**. Hedge fund returns for December are not available as of this writing, but through the end of November our composite was **293 bps** ahead of the Merger-Arbitrage category average as tracked by Hedge Fund Research, the "Morningstar of Hedge Funds".

For the year, our strategy invested in 438 different deals. Some of those were leftover deals from 2022 and some will continue into 2024. We made money in approximately 76% of deals. The worst detracting deal for the year was TD Bank's acquisition of First Horizon Corp. The two companies had mutually agreed to terminate the merger at the height of the mini banking crisis during the second quarter, costing 71 bps. The best contributing deal was Rithm Capital's acquisition of Sculptor Capital Management – Rithm prevailed after a bidding war, contributing 31 bps. About 3% of deals cost 10 bps or more, while slightly more than 4% contributed in excess of 10 bs.

From a Merger-Arbitrage perspective, 2023 might be best remembered for fights that US anti-trust authorities fought and *lost*. The stage was set in February when United Healthcare had the FTC's decision to block their acquisition of LHC Group overturned in court. Microsoft ultimately prevailed in court and consummated their acquisition of gaming software company Activision Blizzard. In the third high profile case, the FTC had attempted to block Amgen's acquisition of Horizon Therapeutics based on a drug for which Horizon already had a monopoly position. Following the FTC's loss in that case, merger activity in the biotech sector has increased dramatically.

In world markets, more good inflation news precipitated bond yields to continue to fall, driving both stocks and bonds to the second extremely strong month in a row. World equities gained 4.8% (The US makes up approximately 60% of the index, and the S&P 500 returned 4.5%.) The Bloomberg Aggregate Bond Index posted returns of 3.8% for the month and finished the year up 5.5%. The classic 60/40 Equity/Bond benchmark (All World Index, Bloomberg US Aggregate Bond Index) returned 4.4% for the month and 15.7% for the year.

Some of the highlights and lowlights of the month for our Merger-Arb portfolios were:

- The biggest contributor was Wentworth Resources, a small British natural gas E&P company with operations in Tanzania. The company had joint ownership of a gas field with M&P, a French company that was the acquirer in the deal. More than a year after announcing their definitive merger, the companies came to an agreement with the Tanzanian Petroleum Development Corporation leading to regulatory approval. That resulted in a contribution of 17 bps for the month but a slight loss since inception as we had reduced our position based on the deal's uncertainty.
- Ellington Financial acquired Arlington Asset Investment Corp in a stock swap merger among two mortgage REIT's. The market had been skeptical of this merger at least in part because Ellington terminated a second deal (to acquire Great Ajax Corp, a deal in which we had no position). The deal closed in December, contributing 17 bps.
- Kin and Carta, a British IT services company is the target of a bidding war between the original acquirer, Apax Partners, and a second private equity firm, BC Partners, contributing 13 bps.
- We've had a small position in Hollysys Automation, a Chinese automation and control system manufacturer for more than a year based on multiple proposals. The company now seems to have accepted a $26.50 bid from Ascendant Capital, a private equity firm with a 13% ownership stake despite a competing proposal at $29 that claims to have secured financing. All of that has resulted in an 11 bps contribution for the month and 21 bps since inception.
- Seagen, a biotech company with clinical stage cancer drugs, saw its acquisition by Pfizer close during the month, contributing 7 bps for December and 11 bps overall. The deal was announced before the FTC was defanged by the Amgen/Horizon Therapeutics case, and as a result traded at a higher-than-average spread over most of the life of the deal.
- The biggest detractor was Powerfleet's acquisition of Mix Telematics in a stock swap merger, with a negative contribution of 12 bps as the spread widened over the month. Both companies are small-cap providers of software for vehicle fleets. Mix Telematics has ADR's that trade in the US, but its primary listing is Johannesburg with some operations in Israel. The company has been affected by having some key personnel called up to serve in the war against Hamas in the Gaza Strip. Possibly related, the companies have been granted an extension to file certain merger documents. Another explanation for the poor price action is that Powerfleet's stock is becoming expensive to borrow due to the company's low market cap and limited share issuance.
- Eli Lilly completed their acquisition of Point Biopharma, a biotech company with expertise in the growing field of radiopharmaceuticals in the fight against cancer. As noted in prior months' commentaries, the stock had been trading at a premium to the deal price on the expectation that Lilly would be forced to increase their bid. We had sold approximately half our initial position in Point over the prior months as its stock price rose. During December, Point announced disappointing results for a prostate cancer drug at which time the stock dropped and subsequently closed at the original deal price. For the month, the negative impact was 8 bps, but positive 6 bps since inception.

New deal announcements were a healthy 30 for the month. However, 37 deals closed. Diversification is well above average although the number of deals has fallen to 91 from 96 a month ago and 110 two months ago. Leverage has also fallen as many new deals are in non-US companies where position sizes are typically below average (typically we have less access to information concerning non-US deals making them slightly riskier leading to a lower weight in the portfolio). The portfolio now has approximately $85 of long positions for every $100 of capital. As noted in previous commentaries, excess US Dollar balances are invested in money-market equivalent ETF's yielding above the rate Interactive Brokers pays on overnight balances.

Constantia Capital Merger-Arbitrage: Performance as of December 31, 2023

Benchmark	Reporting Period	Returns (Net)[2] [3]	Bench-Mark[2]	Excess (Net)	Volatility	Sharpe Ratio
LIBOR/SOFR	Year-to-date	**6.42%**	5.20%	1.22%	N/A	N/A
3-month USD	Latest 3 Years	**5.47%**	2.59%	2.88%	3.10%	0.93
	Latest 5 Years	**4.25%**	2.13%	2.12%	5.31%	0.40
	Latest 10 Years	**4.10%**	1.56%	2.54%	4.54%	0.56
	Since Inception[1]	**5.12%**	1.34%	3.78%	4.39%	0.86

[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 a small number of qualified clients have elected as of the date above