

Constantia Capital Merger-Arbitrage Strategy February 2021 Commentary

Our composite returned 0.94% in February, bringing returns to 4.00% annualized for the past 5 years and 5.04% annualized since inception.

February saw the return of volatility in equity markets driven by an increase in interest rates. One thing we like to stress about Merger-Arb is that it is a fixed income alternative with low correlation to interest rates. That was hurt last year as the Fed cut short term rates to near zero and the pandemic-induced recession caused long term rates to follow, causing returns on bond portfolios to soar. This year bond portfolios are experiencing negative returns and merger-arb is helping offset that in a diversified fixed income portfolio.

Some of the highlights and lowlights of the month:

- We benefited from three counter-bid situations during the month. Coherent, a laser-systems company, agreed to be acquired by Lumentum in January, then saw a counter bid by II-VI (pronounced 'Two-Six') followed by a second counter bid by MKS Instruments for a total contribution of 25 bps.
- Corelogic, a real-estate data services company, agreed to be acquired by Stone Point Capital early in February after a highly public bidding process. Costar Group counter bid, leading to a contribution of 20 bps.
- The third situation involved Tribune Publishing. Alden Global had made a proposal to purchase the company a few months ago at \$14.50/share, and then formalized the deal at \$17.25/share, leading to a contribution of 8 bps.
- January's biggest negative contributor was Huya's acquisition of Doyu (both partially owned by Tencent), but fears of Chinese government threats to the deal subsided and contributing 6 bps.
- The biggest negative contributor was the Tilray's acquisition of Aphria, both cannabis stocks. Suddenly the Gamestop/Reddit crowd starting buzzing about Tilray, a stock with an historically high level of short interest. Tilray briefly tripled giving rise to "buy-ins" and we covered a portion of our short position at the worst possible time, costing 35 bps.
- Partly offsetting that was two other cannabis deals. Two true penny stocks, Stem Holdings and Driven Deliveries, concluded their merger, contributing 10 bps. Canadian medical cannabis company, Liberty Health Sciences, is being acquired by a larger competitor, contributed 9 bps.
- Salesforce's acquisition of Slack, which had been our largest position, has seen a Department of Justice "request for more information", causing the spread to widen slightly and costing 5 bps. Such requests, while never a positive, are not unusual.

Looking forward, the environment continues to be very positive for Merger-Arbitrage. The number of deals remains over 100, and leverage is close to 120% (\$120 of long positions for every \$100 of capital). February saw 26 new deal announcements, while 24 closed and 1 was terminated.

Constantia Capital Merger-Arbitrage: Performance as of February 28, 2021

Benchmark	Reporting Period	Returns (Net) ^{2 3}	Bench-Mark ²	Excess (Net)	Volatility	Sharpe Ratio
LIBOR 3-month USD	Year-to-date	1.07%	0.03%	1.04%	N/A	N/A
	Latest 3 Years	3.30%	1.66%	1.65%	6.37%	0.26
	Latest 5 Years	4.00%	1.45%	2.55%	5.03%	0.51
	Since Inception ¹	5.04%	0.93%	4.11%	4.71%	0.87

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 1/31/2021