

Constantia Capital Merger-Arbitrage Strategy August 2022 Commentary

Our composite returned 1.01% in August, bringing returns to 0.27% for the year-to-date, 3.91% annualized for the past 5 years and 5.10% in almost 11 years annualized since inception.

Equity markets were spooked by the Federal Reserve Chairman's hawkish tone at his Jackson Hole speech late in the month. Both equities and bonds fell during August, with the S&P 500 posting a -4.1% return for the month. Bonds fell 2.8%, but the yield curve remained inverted, an indicator that has forecast "9 of the past 5" recessions. Junk bonds are typically regarded as more accurate in their forecast of a recession, with the Morningstar High Yield category falling 1.8% for the month and 10% year-to-date – lower prices imply that investors are demanding higher yields to compensate for higher risk.

Some of the highlights and lowlights of the month:

- The best contributing deal was Hill International being acquired by Global Infrastructure Solutions. Both companies are in construction management. The acquirer revised their bid from \$2.80 per share to \$3.40 to thwart a potential counter bid, resulting in a contribution of 26 bps.
- Resapp, and Australian health care company, is being acquired by Pfizer. The original deal price was A\$0.146, but based on a fairness opinion, Pfizer increased their bid to A\$0.208 resulting in a positive contribution of 25 bps. (It is not uncommon for Australian stocks to trade in pennies.)
- Avast, a British cyber security company being acquired by Norton Lifelock, was finally granted British antitrust approval. The deal had been approved by a number of jurisdictions including the USA when the British, in March, announced they would exclude Microsoft as a competitor from their review. The spread widened at that time, and in the interest of risk control, we sold half our position at a loss. Eventually, common sense prevailed on the British authorities and they completed their review including Microsoft. The contribution for the month was a positive 20 bps, reducing the loss since inception to 16 bps.
- Two other Pfizer acquisitions cumulatively added 10 bps. Our largest position, Biohaven, has steadily seen its stock price increase over the three months since deal announcement as the market has come to realize the value of a spinoff that is part of the deal. A deal to acquire Global Blood Therapeutics, which has an approved drug for Sickle Cell disease and another in the pipeline, was announced earlier during the month.
- Unity Software is acquiring IronSource. Both are software companies that specialize in monetizing apps (which we understand as helping companies place ads in an app). Applovin, a competitor, fearing the combination's impact on their business, made an all-stock bid for Unity on condition they would drop their deal with IronSource. That potential threat caused a negative

contribution of 31 pbs for the month (-21 bps since announcement). In our opinion it is highly unlikely Applovin’s bid will materialize. Aside from the fact that Unity’s board reiterated their support for the IronSource deal, Applovin cannot afford to buy Unity – their current offer is 20% below Unity’s current share price and they have a lower market capitalization.

- Now that Spirit Air has a definitive deal to be acquired by JetBlue Airways and is no longer involved in a bidding war, the market has continued to be skeptical of the deal being completed. Spirit fell 8% for the month, resulting in a -10 bps contribution.
- The latest twist to Elon Musk’s purchase of Twitter is that a whistleblower ex-employee has emerged (coincidentally) who may bolster Musk’s case to terminate the deal. In fact, Musk revised his case from concern over the number of bots to non-disclosure of a material activity by Twitter. We continue to feel confident that the deal will close, but the new news has decreased the probability, and Twitter stock fell 7% for the month, costing 7 bps.

New deal announcements continued at a strong pace with 29 new deals announced in August, while 24 closed. Diversification in the portfolio continues to be considerably above average, although the number of deals decreased to 108. Leverage is currently 120% (\$120 of long positions for every \$100 of capital), having fallen by 10% over the past 2 months as a few above average size deals closed.

Constantia Capital Merger-Arbitrage: Performance as of August 31, 2022

Benchmark	Reporting Period	Returns (Net) ^{2 3}	Bench-Mark ²	Excess (Net)	Volatility	Sharpe Ratio
LIBOR 3-month USD	Year-to-date	0.27%	1.06%	-0.80%	N/A	N/A
	Latest 3 Years	3.72%	0.83%	2.89%	6.59%	0.44
	Latest 5 Years	3.91%	1.39%	2.51%	5.31%	0.47
	Latest 10 Years	4.79%	0.94%	3.85%	4.65%	0.83
	Since Inception ¹	5.10%	0.91%	4.19%	4.55%	0.92

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