

## **Constantia Capital Merger-Arbitrage Strategy January 2022 Commentary**

Our composite returned -0.49% in January, bringing returns to 4.79% annualized for the past 5 years and 5.32% in just over 10 years annualized since inception.

Most asset classes started the year in negative territory. The ACWI World Stock Index fell 4.89% in-line with the S&P 500, which was down 5.17% for the month. Bonds fell on continued inflation fears as well as Fed signaling that it will raise interest rates, with the Bloomberg Aggregate Index posting returns of -2.15%.

Analysis of our historical returns shows a small positive correlation with equities – hence we should not be surprised by our results in January. Falling stocks reduce the possibility of bidding wars as well as impacting deals that are “proposals” as opposed to definitively signed deals. The reality is more complex. The Biden administration has been blaming mergers for some inflationary pressure, primarily in the meat industry. There is also a movement to rework merger metrics that has affected certain large technology mergers.

Some of the highlights and lowlights of the month:

- The worst detracting deal for the month was Microsoft’s acquisition of game maker Activision Blizzard. The deal was announced early in January, and under current anti-trust rules should win approval reasonably easily. Nevertheless, the spread widened on fears that expanded anti-trust rules are aimed at blocking mergers such as this that involve one of the tech giants. The negative impact was 18 bps.
- Two other game makers, Take-Two Interactive and Zinga are merging. As with the Activision deal, there appears to be little overlap in their businesses. Nevertheless, the spread has widened, resulting in a negative 9 bps contribution. This deal has a collar, making it difficult to hedge, which may explain part of the loss.
- Two separate deals were terminated during the month. US anti-trust authorities have sued to block Lockheed Martin’s acquisition of Aerojet Rocketdyne. German authorities appear to be blocking Taiwan’s Global Wafers acquisition of Siltronic AG, despite that deal also being granted Chinese approval earlier in the month. Both were below average size positions, and the impact of each was approximately -5 bps.
- British software company Playtech had been involved in a three-way bidding war, and as a result had been trading above the prevailing highest bid. With the sell-off in technology stocks, two of those bids evaporated and we gave up our unrealized gains from last year as the stock is now

trading below the level of the original deal price. That resulted in a negative contribution for the month of 16 bps.

- The best contributing deal for the month was US Communications Equipment manufacturer Adtran’s acquisition of small-cap German company ADVA Optical. The spread had widened inexplicably during 2021, but various approvals have seen the spread narrow, contributing 25 bps.
- Also noteworthy was AMD’s acquisition of Xilinx. The companies were granted Chinese approval for their deal as they had predicted. However, US approval was granted more than a year ago, and the companies need to reapply – that should be a formality, but it does delay the closing. We added to our position both ahead of (based on favorable market chatter and price action) and after the China approval announcement. The resulting contribution for the month was 20 bps.

New deal announcements slowed down compared to the breakneck pace of 2021, with 17 new deals announced in January, while 27 closed. Diversification in the portfolio continues to be considerably above average. The number of deals is 126, while leverage has remained constant at 135% (\$135 of long positions for every \$100 of capital).

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

Benchmark	Reporting Period	Returns (Net) <sup>2 3</sup>	Bench-Mark <sup>2</sup>	Excess (Net)	Volatility	Sharpe Ratio
LIBOR 3-month USD	Year-to-date	-0.49%	0.03%	-0.52%	N/A	N/A
	Latest 3 Years	4.36%	0.95%	3.41%	6.55%	0.52
	Latest 5 Years	4.79%	1.33%	3.46%	5.27%	0.66
	Latest 10 Years	5.16%	0.87%	4.30%	4.64%	0.93
	Since Inception <sup>1</sup>	5.32%	0.86%	4.46%	4.63%	0.96

<sup>1</sup> Returns annualized, since inception date 11/1/2011

<sup>2</sup> Returns annualized for periods in excess of one year

<sup>3</sup> Net returns after performance fee, which three qualified clients have elected as of 1/31/2021