MERGER ARBITRAGE

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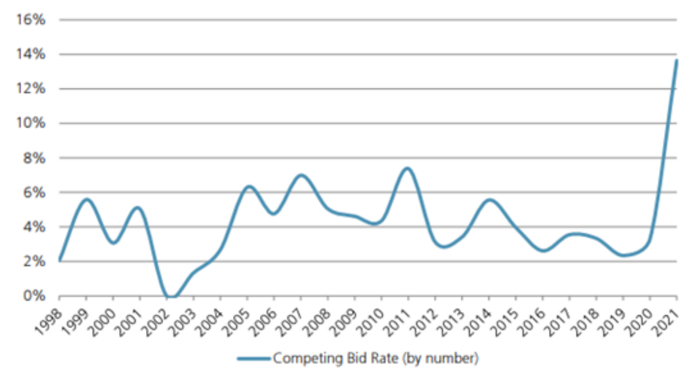
Second quarter deal activity remained robust as in recent quarters. The conditions for M&A continue to be favorable with attractive financing rates, tremendous dry powder from private equity and corporates, and the desire for scale. While there is an increased opportunity set, our favored "rate of return" type spreads are often a bit tighter than we prefer in this environment because investors are pricing in the potential for a topping bid. Such a scenario is not a "free option." If a topping bid fails to materialize, an arb will face a loss if the deal is trading through terms or an unattractive annualized rate of return if too close to terms. While we have witnessed more topping bids than usual (Exhibit 1), we believe investors have been pricing in too frequently, reflecting a "recency" bias. We are reluctant to "chase" such deals, and prefer to monitor in case it trades down to a more suitable level.

EXHIBIT 1: COMPETING BIDS



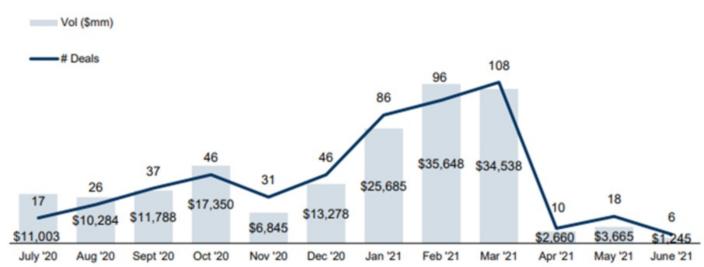
Source: UBS

We also remain wary of arb deals that involve heightened regulatory scrutiny. At the time of this writing, the DOJ has sued to block the Willis Towers Watson/Aon deal, which is a situation of the insurance brokerage industry consolidating from three to two major players, and several pending global tech deals require Chinese approval. While the only aborted deal involving Chinese approval was NXP Semiconductor/Qualcomm in 2018, we continue to see heightened risks around such deals. It is quite possible that they ultimately receive approval, but the process is often long (which can reduce annualized return) and opaque (which could cause substantial volatility if there are fears of a rejection). The relationship between China and the West has become tense in recent months and there has been significantly less outbound Chinese M&A in Western economies compared to a few years ago. While not our base case, it is still a possibility that China utilizes the regulatory process as a means of defending its domestic companies.

Another development on the regulatory front has been the appointment of Lina Khan as FTC Chair, Ms. Khan has been vocal about the need for heightened scrutiny of M&A, particularly in the tech industry. In 2017, she wrote Amazon's Antitrust Paradox (https://www.yalelawjournal.org/note/amazons-antitrust-paradox), which argued that current antitrust policies are not suitable for analyzing market concentration of dominant companies like Amazon. Her appointment could either dampen deal activity in tech and other consolidated industries for fear of regulatory rejection, or lead to more government lawsuits against merger parties. We believe both scenarios raise deal risk, which would need to be reflected in future arbitrage spreads.

Since 2019, we have invested in SPACs (special purpose acquisition corporations) in our merger arbitrage portfolio. We had monitored the space for several years, and decided to start investing when we observed higher quality sponsors and targets (well before the heady times in late 2020 and early 2021). We continue to find the space attractive due to the lack of antitrust risk and their inherent downside protection (as discussed last quarter). We also like that if the SPAC does an attractive acquisition, there is the potential for upside from both the stock and warrants. Given the downside floor and equity like upside potential, the payoff structure of a SPAC is similar to a default free convertible bond.

EXHIBIT 2: SPAC ISSUANCE BY MONTH



Source: RBC Capital Markets

We believe the current SPAC environment is healthier than during the fervor of Q4 2020 and Q1 2021. In recent months, issuance has slowed and is more akin to the pace prior to late 2020 (Exhibit 2). Consequently, most underwriters are only bringing higher quality sponsors to market, such as those that have previously closed deals with success. Also, many sponsors have a forward purchase agreement in hand, lessening financing risks and signaling alignment with investors. Some recent acquisitions have included lengthy sponsor lockups or a vesting schedule at higher price points than the initial $10.00 investment. This means that if the target does not trade above $10.00 post the announced combination, the sponsor's 20% stock stake will have no value, just as the investors will not make money with a sub $10.00 price. Recent examples of such deals include the GS Acquisition Holdings Corp II (GSAH) deal announced in June 2021 and the SmartRent/Fifth Wall Acquisition Corporation deal announced in April 2021.

As the SPAC market has corrected, we believe we are in trough like conditions with limited downside. The fact that most SPACs are trading near or below cash trust value provides significant downside protection. As the froth has subsided, we have witnessed investor terms start to improve. For example, some deals that were initially offering 1/3 warrant coverage in their registration statement have increased terms to 1/2 warrant coverage in order to get the IPO over the finish line. Other deals have increased the cash in trust to 10.10 or higher in order to entice investors. When doing an acquisition, SPACs often need additional capital in the form of a PIPE (private investment in public equity). PIPE financing has become more selective in recent months, and as a result, the agreed upon valuation for targets now is often at a haircut from the lofty multiples of six months ago. This benefits investors since the target is entering the public markets at a more reasonable valuation and realistic expectations. Also, the investor appetite to fund loss making, blue sky 2025 revenue and earnings projections for potential acquisitions has become quite limited to nonexistent, so the caliber of announced deals coming to market has started to improve. Lastly, in recent weeks, some of the recently announced acquisitions have closed and rallied in their initial days as public companies. In instances where we have elected to redeem our investment because the stock was below cash trust, we often continue to hold the warrants. When the target starts to rally post-deal closure, the warrants provide a positive contribution to portfolio performance while the initial investment has been entirely recouped during redemption.

While some speculative capital playing IPOs and announced deals has presumably left the space during the correction over the past few months, we believe the SPAC ecosystem is now stronger and more sustainable and we feel comfortable increasing our exposure to the space. The risk has been lessened given pre-deal SPACs are trading at or near the downside floor while the reward has improved due to better warrant coverage and higher caliber targets at more realistic valuations. In this environment, we will take advantage of the more favorable terms for investment opportunities.

About our firm:

DuPont Capital Management is an SEC registered investment advisor based in Wilmington, Delaware. Since the firm's establishment in 1993, we've had a long history of developing global investment opportunities in both traditional and alternative strategies across equity, fixed income and alternative investments. Our investment team structure gives us the ability to be flexible and adapt to changing market conditions. DuPont Capital's focus is delivering consistent investment management results for our clients. Our history of institutional asset management is rooted back to 1942 when our former parent company, DuPont, established a pension plan for its employees. Corteva Inc. succeeded DuPont as sponsor of the DuPont Pension Plan in 2019. DuPont Capital is a wholly owned subsidiary of Corteva and continues to manage the legacy DuPont Pension Plan.

DuPont Capital's President and CEO, Valerie Sill believes in education and diversity of experience as represented in our investment teams which are comprised of PhDs, engineers, medical doctors, and scientists. We believe their global expertise creates a portfolio implementation edge that benefits our clients.

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Important Disclosures: