Q&A-"Shelled out" SPAC market makes for great pickings; U.S. SEC needs to examine forward projections closely: Andrew Walker, Rangeley Capital LLC

A deflation in the euphoric levels among blank check companies seen earlier this year has led to a “shelled out” market for special purpose acquisition companies (SPACs) that makes for ripe pickings for event-driven investors, **Andrew Walker, portfolio manager at Rangeley Capital LLC,** told the Reuters Global Markets Forum on Wednesday, April 21.

Walker, who has been active in derivatives linked to Bill Ackman-led Pershing Square Tontine Holdings, says there are opportunities for discerning investors in SPACs, but that the U.S. securities regulator needs to closely look at SPACs with unrealistic forward projections.

Following are edited excerpts from the conversation:

Q: What is the current state of play in the world of SPACs? What's looking attractive and what's looking frothy?

A: I think "bombed out" is the word; the SPAC market ran a full euphoric to depressive market cycle in roughly three months. In February, basically every SPAC traded well above trusts, IPOs (initial public offering) were popping 10% on day one, and deals were being met with huge pops. Today, none of that is true. The IPO market is closed, almost every SPAC is trading around trust regardless of sponsor, and deals being met with pops are few and far between.

For event investors, I think that's pretty attractive. You can get "free options" on good teams announcing great deals, or you can get some interesting yield by buying SPACs below trust value. One example: LMACA (Liberty Media Acquisition Corporation) is trading around 2% above trust value. That's Liberty's SPAC; if you looked at Liberty's track record and had the option to buy into a private equity vehicle run by them for roughly cash, I think everyone would jump at that chance. LMACA basically gives you that chance.

Q: Given what's happened, how much of this could be a possible 'Gary Gensler effect'?

A: I do think the SEC (Securities and Exchange Commission) has something to do with it. They recently announced they are looking at the accounting for SPAC warrants; that announcement has basically stopped the SPAC industry but I think the real issue is the market just got overwhelmed with supply; in Q1, we were seeing three to five SPACs IPO a day. There simply aren't enough investors to meet all that demand or companies to eventually merge with. You've also seen waves of post-SPAC companies that are announcing huge issues right off the back; I think that's scared a lot of the retail bid.

CLOV (Clover Health Investments Corp) had an unannounced DOJ (Department of Justice) investigation when they went public, tons of EV (electric vehicle) SPACs have gone public and immediately pulled guidance or announced huge issues. SPACs have been taking advantage of a loophole that lets them issue forward guidance -- normal IPOs cannot do this.

Q: Beyond this treatment of warrants, what regulations could be put in place to align interests more closely?

A: I think the SEC needs to give a real look at those forward projections; companies are going public on forward projections that border on impossible, and then once they go public they've been saying "oh yeah, never mind those projections; we can never hit those!" I think something that more closely ties the SPAC sponsors promote/payout with long term performance of the stock would be a good start.

Q: What are your favorite SPACs currently, those trading under trust value i.e. $10 and otherwise?

A: I mentioned LMACA earlier; I love the Liberty team and I think buying them at a slight premium to trust is a unique opportunity. RTP (Reinvent Technology Partners) is interesting as an event driven trade; this is Reid Hoffman's SPAC that is merging with Joby. The founder's agreed to restructure their promote so they are very aligned with shareholders, and they've got a really interesting group of strategic sponsors in the PIPE (private investment in public equity). RTP shares are trading below trust right now, and it's in

ARK's space ETF (exchange-traded fund). So, you get a little bit of a free look: if the market gets excited for the company again, the stock will go up. If not, you can just hold the shares and redeem for trust value in a few months.

Q: What is your thought process/approach when you assess SPACs?

A: I think the devil is generally in the details; SPACs can have wildly different terms and that can create some opportunities. For eg., PSTH (Pershing Square Tontine Holdings Ltd) has a rather unique tontine structure. Some SPACs have more than $10/share in trust. Others have different liquidation timelines. With the market currently so shelled out, I think there's opportunity to find SPACs with somewhat unique structures that can create extra opportunity. I also like SPAC sponsors that have access to unique deal flow, as those are generally the ones who can announce deals that the market really likes / announce deals that are actually good.

Q: What's the discrepancy in option or underlying pricing of PSTH that you've been active in and by when do you see this aberration close?

A: PSTH's trust value is around $20/share. They're trading for around $23.50/share, so a headline number would say they're trading just under 20% premium to trust. However, PSTH has a tontine structure, where every share that doesn't redeem when they announce a deal will be given 2/9th of a warrant plus some extra warrants from any shares who redeemed and forfeited their tontine structure. What's interesting is PSTH has options trading on it, so you could buy-write the stock and create it for roughly trust value, which would get you those potential tontine warrants for free if and when they announce the deal. In addition, I believe that the options market would not adjust for those tontine warrants -- there is an open debate on this, so if you buy-write the stock and hold through the deal you would be given the tontine warrants for "free" because the options deliverable would remain one share of stock.

PSH (Pershing Square Holdings Ltd) trades for a discount to NAV (net asset value), generally around 20%. PSTH trades for a premium to NAV. With PSTH, investors are saying "we love Bill Ackman, cash in his hands is worth a premium because he'll deploy it so well." With PSH, investors are saying "we hate Ackman, assets he manages should trade for below NAV because he will destroy value." That's a weird combo, in particular because PSH has a big exposure to PSTH, so they will benefit from any value creation there.

Q: Is this also the case with Softbank-backed SPACs, since Softbank in Tokyo has had issues with conglomerate discount?

A: I think the answer is technically yes, though Softbank is a little different. PSH's assets are almost exclusively highly liquid publicly traded companies, so you can feel pretty comfortable about their NAV. With Softbank, you need to adjust for the tax drag of some of their assets -- PSH doesn't pay taxes -- and you also need to worry about the marks of their illiquid stakes. Also, Softbank's SPACs trade much closer to NAV than PSTH -- I think they're interesting as well!

Q: What do you feel about the effect SPACs have had on late stage venture capitals/private equity? If the SPAC model persists if/how do you see late stage VC adapting?

A: Tough to say. On the one hand, the boom earlier this year meant VC/PE were getting showered with money. It's got to be nice having hundreds of forced buyers -- as SPACs are; if they don't announce and complete a deal before their time runs out, their founders lose millions. And I think VC/PE were unloading assets at incredible prices. On the other- a lot of companies that would generally be VC/PE targets are getting removed, so the pool of companies is smaller.

Q: Any parting thoughts for us?

A: The SPAC market is certainly interesting; I think it's an event driven investor's dream playground.