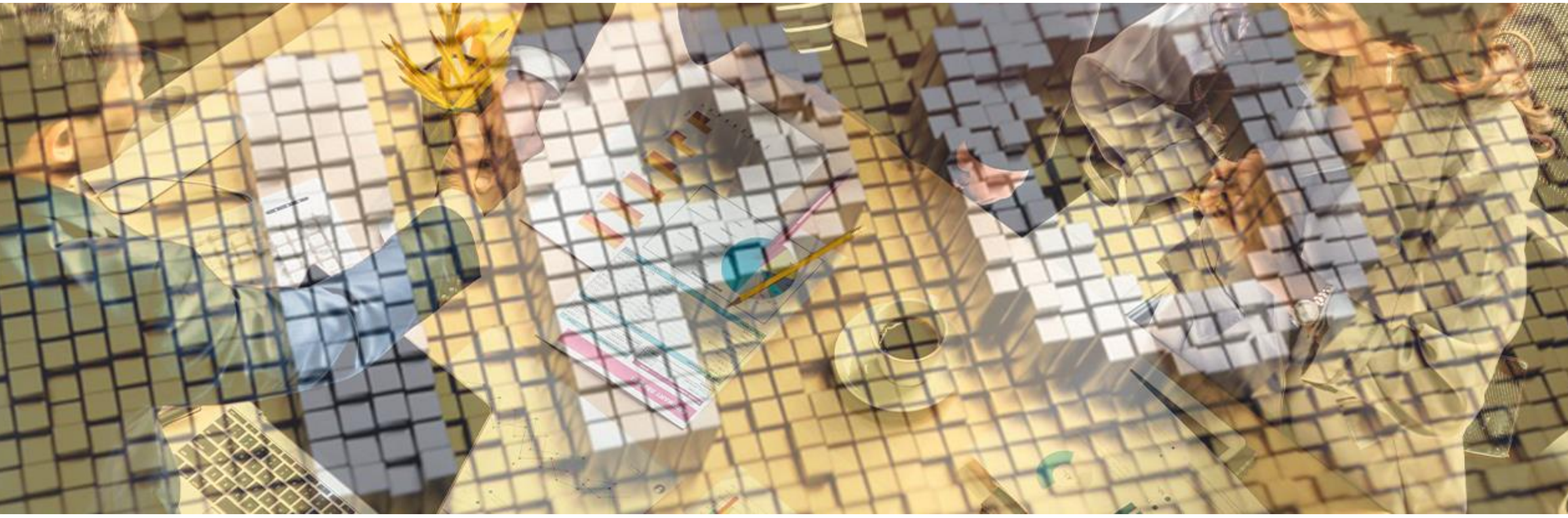


The Special Purpose Acquisition Company

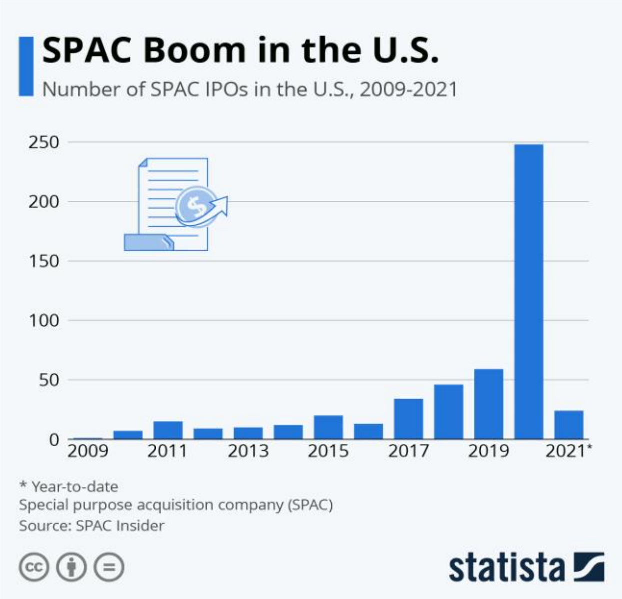
Thoughts for smaller investors to consider when evaluating SPACs

A cynical investor might look at a Special Purpose Acquisition Company with disdain. Here is what a cynic might say: "So, you're telling me a SPAC:

- Makes no products;
- Does not sell anything; and
- Is called a blank-check company?

Why do such entities even exist?"

Well, all of the above is true. SPACs don't make anything, don't sell anything and are called blank-check companies. But they do have a reason to exist and the last few years have brought renewed interest. In fact, just last year alone, there were over 200 SPACs that raised over $73 billion.



How SPACs Work

A special purpose acquisition company is a company that is formed strictly to raise capital through an Initial Public Offering for the single purpose of acquiring an existing, privately held company. SPACs are generally formed by institutional investors (or sponsors) with expertise in a certain industry or sector, with the intention of pursuing a deal of an existing company in their area of focus.

Generally speaking, when a SPAC is created, the "founders" have at least one acquisition target in mind, sometimes multiple, but they don't actually disclose that target during the IPO process. In other words, the IPO investors in a SPAC don't know what company they will ultimately be investing in – hence the name: blank-check companies.

Further, a SPAC usually has two years to complete a transaction or return the money raised to investors. Once an acquisition is complete, a SPAC is usually listed on an exchange.

If the owners of a privately held company are considering going public, then selling to a SPAC might be an attractive option for lots of reasons. For one, proponents of SPACs suggest that selling to a SPAC can add up to 20% to the sale price relative to a sale to a private equity firm. But empirically verifying that is impossible to do.

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SPAC Advantages for Small Investors

Throughout 2020 and into 2021, SPACs have been garnering a lot of media attention and being hailed as attractive investments for smaller, retail investors.

And while SPACs can be attractive from a smaller investor perspective, SPACs also carry a lot of risk too. First, three unique advantages for smaller investors:

1. The fact that SPACs are open to small investors in itself is an advantage;
2. The cost to get in is low as many SPACs are priced at $10/share; and
3. SPACs are investing in hot areas like technology and energy.

SPAC Disadvantages for Small Investors

But SPACs bring just as much worry and a lot of risk too. Three unique disadvantages for smaller investors:

1. SPAC investors usually don't know how their money will be used;
2. There is often a lag between the time you invest in a SPAC and before it actually acquires a company;
3. Track record is mixed. A Goldman Sachs report from the summer of 2020 found the average SPAC underperformed the S&P 500 during the 3, 6, and 12-months after completing its acquisition (but that's a small sample size of only 56 SPACs and the performance comparisons are for a short amount of time). But a report from Renaissance Capital is even more sour.

SPAC Performance

According to Renaissance Capital:

"Of the 313 SPACs IPOs since the start of 2015, 93 have completed mergers and taken a company public. Of these, the common shares have delivered an average loss of -9.6% and a median return of -29.1%, compared to the average aftermarket return of 47.1% for traditional IPOs since 2015."

It should be noted that this data is as of September 30th of 2020, so it is dated, but still…

A Big SPAC Worry?

Yes, SPACs have been around for decades and yes, they are attracting a lot of attention from some famous entrepreneurs and big institutions alike. Richard Branson and Michael Jordan; firms like Fidelity Investments and T. Rowe Price; and investment banks like Goldman Sachs, Credit Suisse, and Morgan Staley have all been linked to SPACs.

But for those around during the 1980s – or for those who appreciate history – SPACs have a checkered history at best. More specifically, during the 1980s, these "blank-check companies" were often just shell companies offering thinly traded penny stocks on the "pink sheets." Sometimes these shell companies either took off with investors' money or engaged in some shady insider- and over-valued-acquisitions that left investors with almost nothing.

Of course since then, the SEC has stepped up its regulations and enforcement. Today, a SPAC has to place investors' money in an escrow account until it announces an acquisition and even small SPACs must register with the SEC.

Should You Invest in a SPAC?

The answer to that question is, of course, a personal one that depends on a lot of variables, including answering questions like:

- Is such an investment consistent with your risk tolerance?
- Does such an investment fit within your overall investment philosophy?
- Does such an investment fit within your overall investment style?
- Does such an investment help you toward your overall financial goal?

Answering these questions, along with the additional questions that will percolate to the top of your analysis, is an exercise that your financial advisor can help you navigate.

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