Merger Arbitrage: Capitalizing Evolving Merger Environment

Executive Summary

The merger arbitrage space offers a compelling opportunity as we look ahead. In June 2023, Versor released a white paper highlighting shifts in the M&A landscape. Since then, the Versor Merger Arbitrage strategy has delivered strong returns and outperformed the HFRX Equity Event Driven Index. This success reflects our differentiated approach, which leverages a proprietary database of 6,000+ deals and advanced artificial intelligence (AI) and machine learning (ML) techniques, to evaluate all aspects of a merger life cycle with a focus on deal termination risk, competing bids and positive amendments. Reduced inflation, fading recession concerns, and the resilient U.S. economy have bolstered corporate confidence. Post-U.S. election indicators further signal a favorable shift in the M&A regulatory environment. Combined with a 20-year high in private equity dry powder and robust cash reserves held by corporations, these conditions suggest a sustained uptick in deal flow in the coming months. As the global M&A landscape is primed for resurgence, the Versor Merger Arbitrage strategy is well positioned to capture attractive, risk-adjusted returns.

To fully capitalize on the favorable M&A environment, an effective merger arbitrage strategy must go beyond basic event-driven approaches. Versor has harnessed a proprietary database of over 6,000 historical deals dating back to 2000, incorporating both fundamental and market data for a holistic view of merger dynamics. This deep dataset, combined with advanced AI and machine learning techniques, enables Versor to forecast deal outcomes with greater precision. Our strategy doesn't stop at simply assessing deal success or failure; it uniquely models the likelihood of competing bids or upward amendments, a critical third outcome that traditional merger arbitrage managers often overlook. With competing bids or amendments occurring in approximately 16% of deals, accurately predicting these events has proven to be a key driver of alpha to the strategy.

Recognized with a nomination for the HFM Performance Awards 2024, Versor's disciplined, systematic approach enables consistent performance even in challenging markets. By continuously refining our strategy with advanced AI/ML models applied to a rich dataset, we capture high-conviction opportunities and deliver resilient, risk-adjusted returns for our investors.

Poised for Growth: Optimism in the Merger Environment

The global M&A landscape is primed for a strong rebound post-U.S. election as the Trump administration is expected to have a pro-business orientation, advocating for reduced regulations and lower corporate taxes. This approach is intended to stimulate economic growth and encourage corporate activities, including M&A.

Since second half of 2023, we have seen expanding opportunities in the merger and acquisition space. This is in stark contrast to a challenging 2022 and 2023, in which actions by the FTC/DOJ caused much uncertainty. As we reflect on the past several months, we believe the Activision (Acquirer: Microsoft) ruling marked a turning point for the environment. More recently, Exxon Mobil completed its acquisition of Pioneer Natural Resources, and in October 2024, the U.S. Federal Trade Commission approved Chevron's acquisition of Hess, injecting new momentum into the M&A landscape. Although these high-profile deals faced scrutiny and heightened perceptions of a restrictive regulatory climate, the actual rate of regulatory intervention has remained low.

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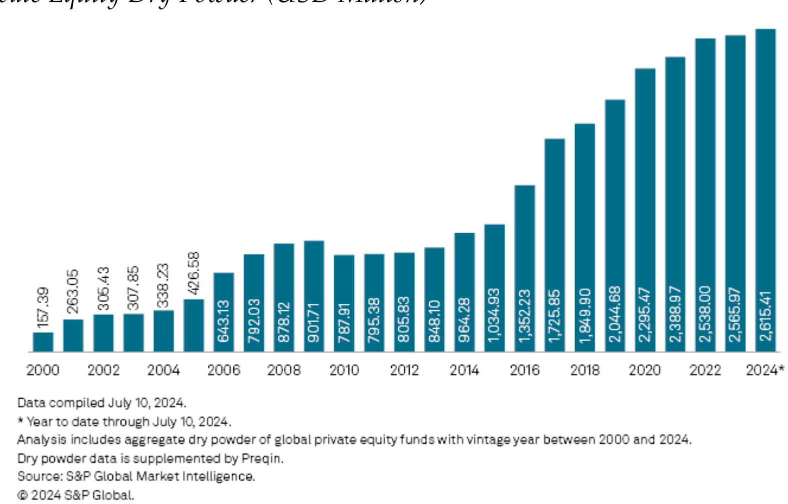
Additionally, a closer look at deal flow shows that smaller deals—making up over 80% of the total deal universe—have faced notably less regulatory interference. This is also visible in the low global deal cancellation rate of 3.55%.

In addition, private equity firms, with dry powder at a 20-year high ($2.6 trillion), are poised for future transactions. Over the six months since December 2023, funds increased their cash reserves by $49.4 billion—over 1.7 times the $27.9 billion accumulated during the prior 12 months.

Figure 1: Global Private Equity Dry Powder (USD Million)



Source:https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/private-equity-dry-powder-growth-accelerated-in-h1-2024-82385822

Lastly, several indicators tracked by Versor signal a healthy merger environment:

- Both global deal value and deal count remain robust and are expected to increase due to pent up demand.
- Global spreads at 9.18% in October 2024, remain attractive relative to historical median of 4.01%.
- Global deal cancellations remain low (3.55%) relative to the historical median of 8.10%, and deal completions are occurring in less than six months.

These developments combined with quantitative environmental indicators below suggest an improving environment with an attractive risk/reward profile in the space.

Versor Merger Arbitrage: A Differentiated Approach

Typically deals are characterized by two distinct outcomes – deal success or failure. However, deal success can be split further into success under the current offer terms and success with a competing bid or upward amendment. Historically, this third outcome, often overlooked by traditional merger arbitrage managers, represents 16% of all merger outcomes. Accurately quantifying the likelihood, a deal will receive a competing bid, or positive amendment can produce materially larger alpha. Leveraging its proprietary database, Versor has successfully used observable deal characteristics to predict the likelihood of a merger receiving an improved offer.

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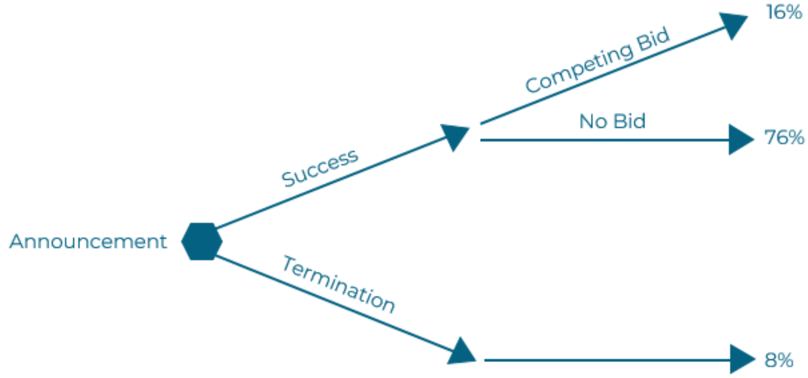
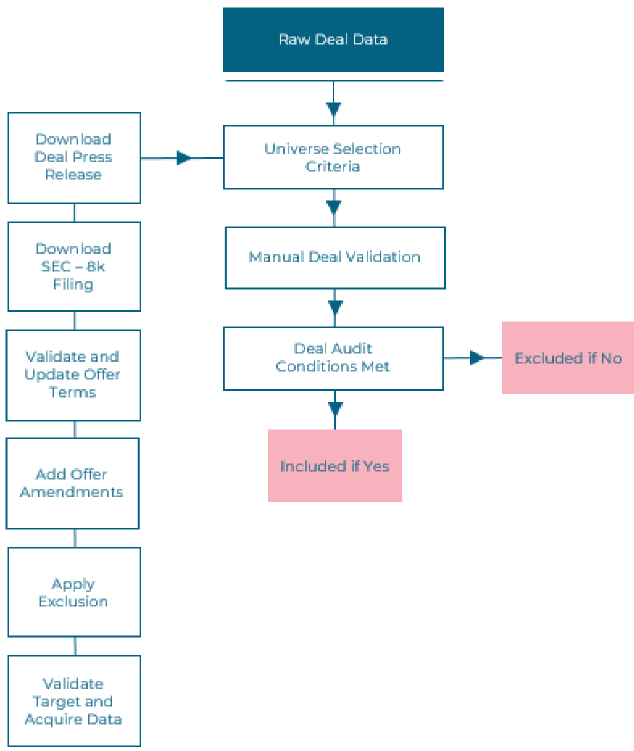
Figure 2: Deal Outcome



Internally prepared by Versor Investments. Simulated price paths for a hypothetical merger target. For illustration only. Data computed for the period January 2003 to December 2023.

The competing bid model described above is just one of the several models (downside risk, duration, liquidity, volatility etc.) that forms part of Versor's extensive model suite.

Figure 3: Proprietary Merger Database



For Illustrative purposes only, actual implementation may differ.

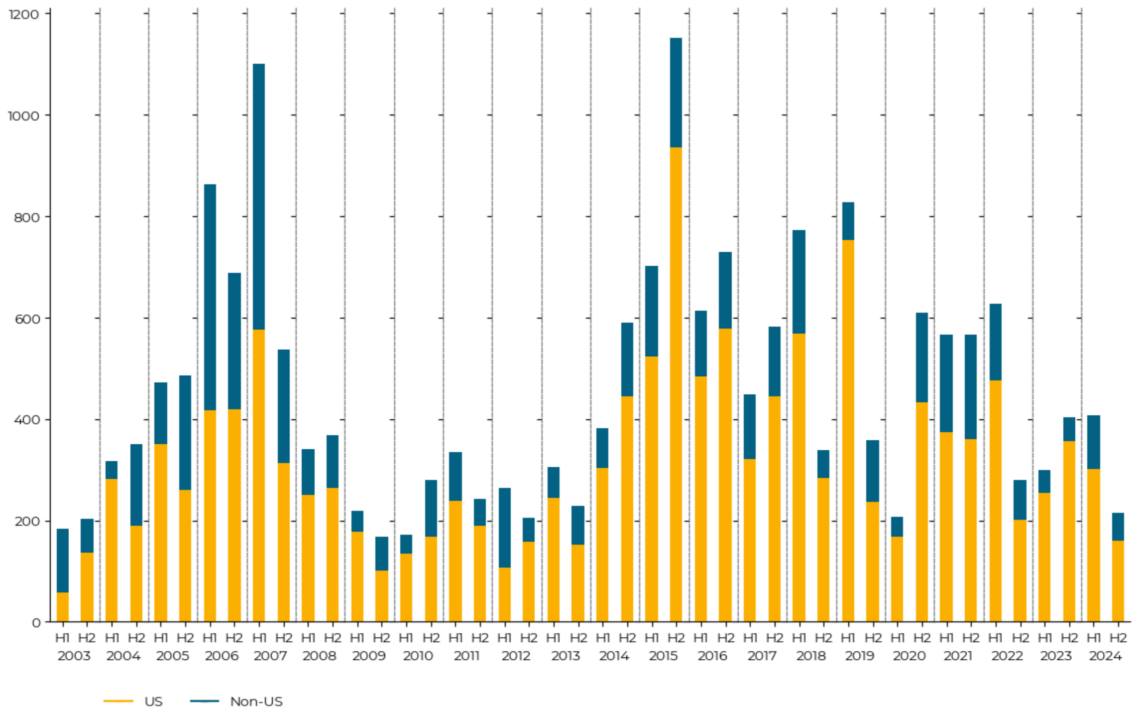
Versor's model suite relies on a vast proprietary database, carefully built to include over 6,000 deals dating back to 2000. Deals are added to the database only after meeting a stringent set of criteria, with press releases serving as the primary data source. Additional data collected on targets and acquirers includes intraday prices, volume, historical financial statements, ESG metrics, and news sentiment.

Over the past 7 years, Versor models, combined with sophisticated use of machine learning and alternative data have culminated in a strategy able to consistently take advantage of favorable environments to a greater degree than those focus on the predictive power of deal spreads.

Environment Indicators:

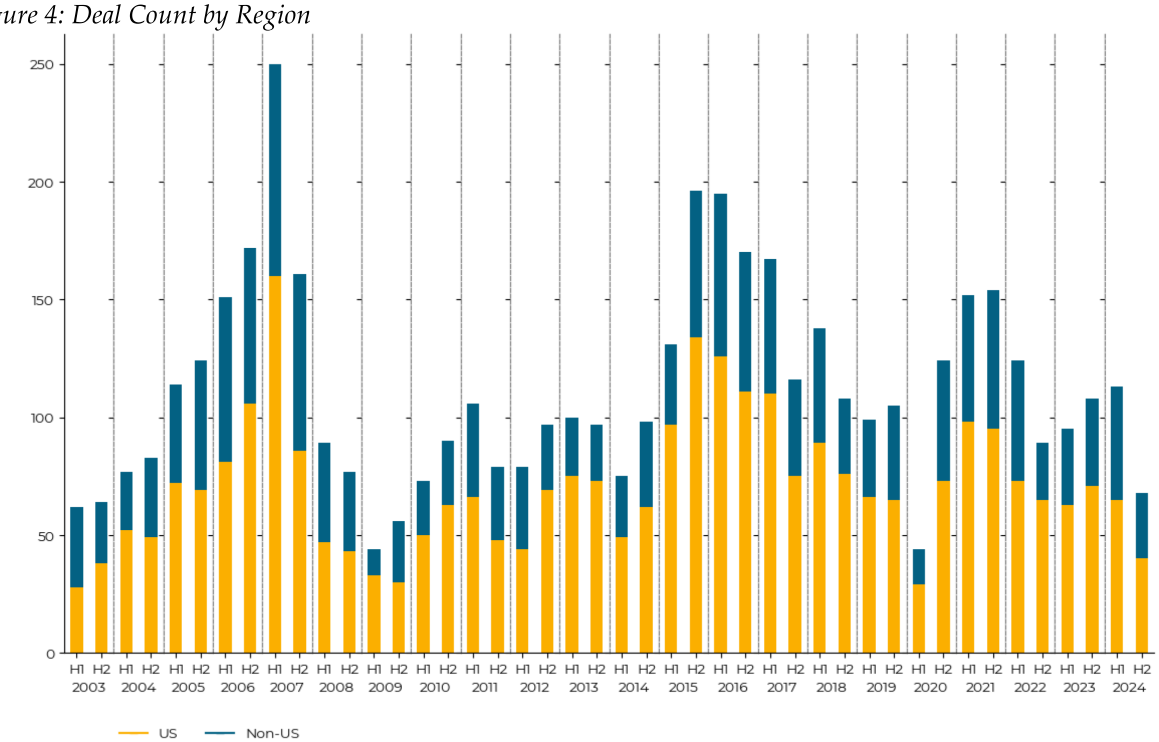
Deal flow: Deal flow has remained robust over the past several months. Due to pent up demand and favorable M&A environment, we expect the deal flow to significantly pick up to levels observed in 2015 to 2018. (see figures 3 and 4)

Figure 3: Deal Value



Past performance is not indicative of future results. Performance results reflect the reinvestment of income. Total announced value represents sum of announced value of all the deals announced in a half year across North America, Europe, Japan, and Australia. H2 2024 includes data through October 31, 2024. The deal value is represented in USD billion. Data received from Bloomberg and internally prepared by Versor Investments. Simulated, back-tested data. For illustrative purposes only.

Figure 4: Deal Count by Region



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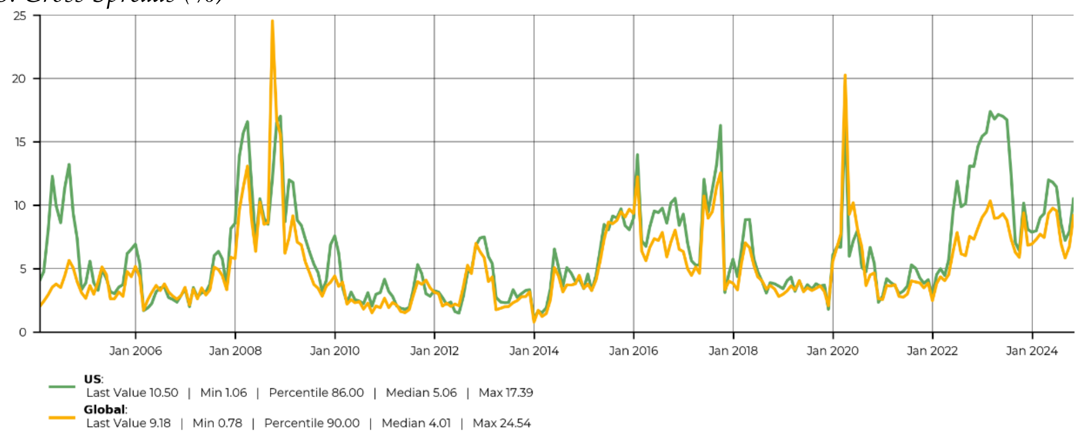
Spreads: The spreads remain attractive compared to historical average. Historically, higher spreads have been an attractive entry point for mergers. (see figure 5)

In March of 2021, we released a whitepaper titled, "The Environment for Merger Arbitrage: 2021."In that paper, we showed that the state of various merger indicators pointed to an exceptionally favorable strategy environment. Merger Arbitrage posted strong returns in the period from April through December of 2021.

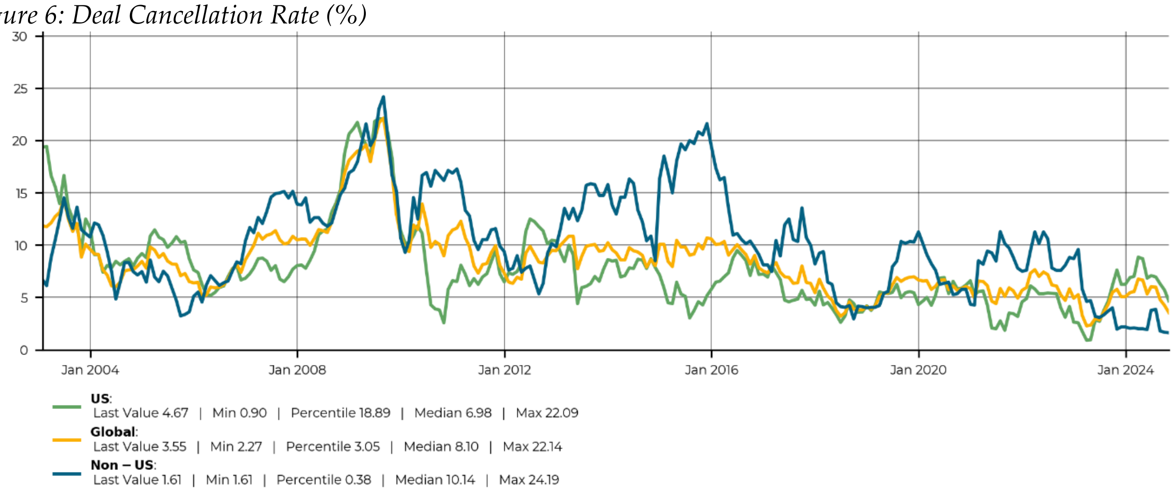
Figure 5: Gross Spreads (%)



Past performance is not indicative of future results. Performance results reflect the reinvestment of income. Spreads represented in the chart are gross spread weighted by the cube root of market capitalization of the targets of all the mergers in the audited universe, on the given date in the respective region. Negative spread values, on any given date, are excluded. US contains mergers where the targets primary listing is in US. Global contains mergers where the target primary listing is in Europe, United Kingdom, Canada and US. The data is through October 31, 2024.

Termination rates: The global deal cancellation rate continues to stand well below historic median. Recently, acquirers litigating blocked deals have been successful. (see figure 6)

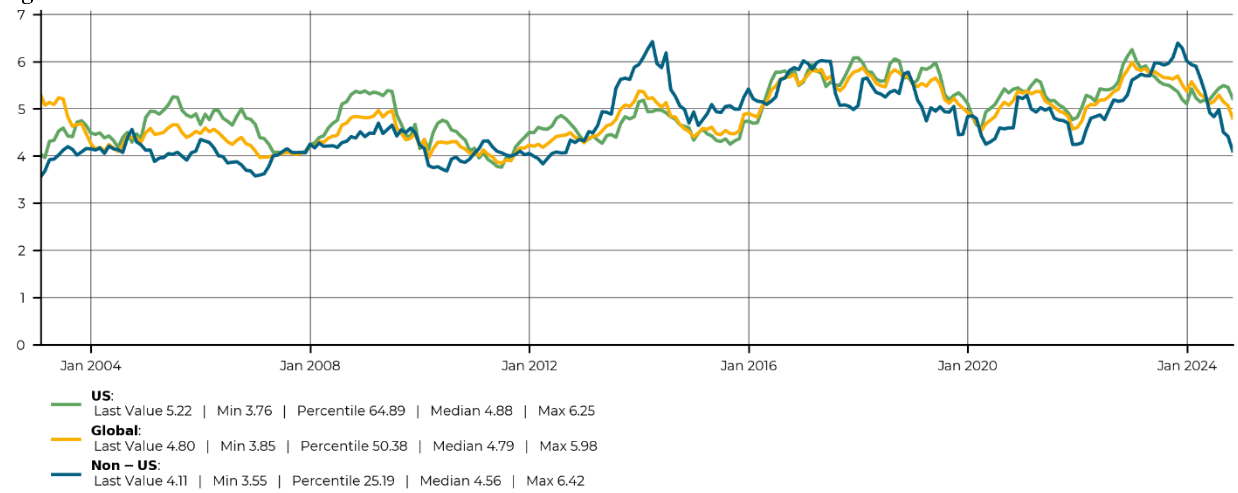
Figure 6: Deal Cancellation Rate (%)



Past performance is not indicative of future results. Performance results reflect the reinvestment of income. The figure shows the failure rate of mergers over time. The failure rate is the number of mergers that terminate divided by the sum of pending and terminating mergers. The data is through October 31, 2024. Simulated back-test data. For illustrative purposes only. Data received from Bloomberg and internally prepared by Versor Investments.

Deal Duration: On average, the merger deals continue to be completed in under 6 months. (see figure 7)

Figure 7: Mean Deal Duration (Months)



Past performance is not indicative of future results. Performance results reflect the reinvestment of income. The figure shows the average deal duration for announced mergers over time. The duration is measured from announcement to successful completion or termination. US mergers have targets with primary equity listings in the US. Non-US mergers constitute mergers with target stocks in Canada, Europe including the UK, Australia and Japan. The data is through October 31, 2024. Simulated back-test data. For illustrative purposes only. Data received from Bloomberg and internally prepared by Versor Investments.

Conclusion:

In summary, Versor's merger arbitrage strategy stands out due to its differentiated process, utilizing a proprietary database and advanced AI/ML techniques to capitalize on unique M&A opportunities. This disciplined systematic approach has delivered strong returns even in a challenging regulatory and economic environment, demonstrating its resilience and adaptability. With an improving M&A landscape supported by favorable economic conditions, easing regulatory environment and renewed corporate confidence, Versor is well-positioned to deliver attractive, risk-adjusted returns. The strategy actively invests in announced mergers across the U.S., Canada, the U.K., and Europe, positioning portfolios for optimized returns.

We look forward to partnering with you to navigate the exciting merger environment. If you have any questions or would like to learn more, reach out to DeWayne Louis at dewayne@versorinvest.com or Nirav Shah at nshah@versorinvest.com.

Sincerely,

Deepak Gurnani

Deepak Gurnani, Founder and Managing partner

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Reported returns are unaudited preliminary estimates, subject to revision and net of management fees and performance fees. Certain investors may have higher management and performance fees depending on applicable share class. Performance results reflect the reinvestment of income. Please note that the returns could be materially different from those stated here in case the strategy was managed in a dedicated standalone fund. In fact, the actual returns could be much lower than those shown here. Please see important disclosures at the end of the presentation.

Live Performance
1. The returns for Versor Merger Arbitrage strategy are estimated by applying a notional capital allocation (and applicable expenses) to the P/L associated with the portion of the ARP Alternative Risk Premia Master Fund allocated to the strategy. Versor Merger Arbitrage strategy is a part of a sub strategy under ARP Alternative Risk Premia Master Fund, which is a multi-strategy fund. From Dec 4, 2018, to Dec 31, 2022, the reported returns are for a Versor Investments advised dedicated fund ["the Fund"] for the Versor Merger Arbitrage strategy. The return estimates presented were for the USD share class and excludes hedge profits/losses pertaining to other non-USD share classes to the extent, if any. Even though the Fund launched from Dec 3, 2018, one day was used to build-up the portfolio of the Fund. Therefore, the return for Dec 3, 2018, is not the correct indication of this strategy performance. The return for the Fund for Dec 3, 2018, was -0.19% while reported performance of Versor Merger Arbitrage strategy for Dec 3, 2018, was 0.45%. Prior to Dec 3, 2018, Versor Investments did not manage capital in the Versor Merger Arbitrage strategy as a dedicated Fund for this strategy. Versor Merger Arbitrage strategy was part of a sub strategy under ARP Alternative Risk Premia 2x Fund, which is a multi-strategy fund. Returns until Dec 3, 2018, for the Versor Merger Arbitrage strategy are estimated by applying a notional capital allocation (and applicable expenses) to the P/L associated with the portion of the ARP Alternative Risk Premia 2x Fund allocated to the strategy.
The returns are net of 1.00% annual management fees and 10.00% performance fees and assume the reinvestment of dividends and other income. Performance fees are a component of management costs. A performance fee of 10.00% of the Trading Profits is calculated and accrued on each Pricing Day and reflected in the reported net returns. The Performance Fee is calculated in respect of each calendar year subject to a high-water mark provision. The Investment Manager cannot guarantee the performance of the Fund or that performance fees will remain at their previous level. Certain investors may have higher management and performance fees, depending on the applicable share class. Versor Investments also manages other accounts using the same investment strategy. Returns for the other accounts may differ from the returns shown here, depending on differences in risk levels and other investment restrictions, timing of cash flows, and fee structures.
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