SIFMA Insights

Spotlight: 2020, the Year of the SPAC

Explaining SPACs and Analyzing Issuance Trends

August 2020

Key Takeaways

- With the number of IPOs down over the last few years as companies stay private longer (averaging 12 years), SPACs grew in popularity as another tool to access capital
- SPACs have already had their biggest year in 2020, with $22.2B deal value through July (+65% Y/Y)
- The COVID-19 issuance recovery path: secondaries ($50.8B in May, +283% vs. start of year); IPOs ($14.7B in June, +414% vs. start of year); and then SPACs ($10.3B in July, +599% vs. start of year)

Spotlight: 2020, The Year of the SPAC

What is a SPAC?

A special purpose acquisition company (SPAC) is a company with no commercial operations, a shell company. It is established solely to raise capital through an initial public offering (IPO) for the purpose of acquiring unspecified existing companies. They are commonly referred to as blank check companies. SPACs are formed by a founder(s), experienced business executives with strong reputations and operational track records who provide the initial capital. The founders are the selling point to investors, often referred to as betting on the jockey (founder) rather than the horse (company). In fact, the IPO prospectus focuses on the founder and not the company, which does not have financial statements or performance history.

As with a traditional IPO, the founders contract an investment bank to handle the IPO process (due diligence, drafting/filing, roadshow, pricing, trading/market making)[1]. At the IPO, investors get units, each comprising of one share of common stock and a warrant to purchase more shares (or portion of a share) at a future date. A unit typically costs $10.00. The founders receive a promote fee, around 20% of the common stock.

After the IPO, management has 18 to 24 months to identify a target and complete the acquisition. The fair market value of the target company must be 80%+ of the SPAC's trust assets, and time to completion varies by industry and company. During this time, 100% of the money raised in the IPO is held in a trust account generating interest.

Once the acquisition is complete, founders and investors receive equity interest in the acquired company relative to their capital contribution. If no acquisition is completed within a predetermined time period, the SPAC is dissolved, and investor money is returned. Additionally, if an investor does not want to participate in the deal, he can exercise redemption rights and get his money back.

In December 2010, Nasdaq amended its listing rules to allow SPACs to utilize a new structure, referred to as the tender offer structure. NYSE Amex adopted a rule change for the same purpose in January 2011. Prior to this, SPACs had to solicit shareholder approval prior to completing an acquisition. With this new structure, SPACs can instead make a tender offer for the shares held by certain shareholders prior to acquisition completion. This is designed to facilitate subsequent acquisitions. Exchanges made the rule changes to improve SPAC liquidity and therefore make SPACs more attractive to investors.

Many list an advantage of a SPAC as less time to IPO, as deal points are only negotiated with the founder(s), versus holding roadshows with many investors. Additionally, in the COVID-19 world, market participants indicate SPAC processes work well virtually. It is often considered an efficient way to put capital to use. However, SPACs are deemed expensive, as you have all the standard IPO expenses plus the founder's promote fee. Of concern for investors, there are less disclosure requirements and no lockup period as with a traditional IPO. Additionally, SPAC stock performance can be questionable. According to Renaissance Capital's IPO data, from 2015 to 2020, the average return for SPACs was -18.8%, versus 37.2% for traditional IPOs. Only 29% of SPACs during this time had positive returns. That said, all is not equal: 2019-2020 SPACs outperformed earlier ones; larger SPACs outperformed smaller ones; and healthcare and tech industry SPACs outperformed other sectors (ex: energy).

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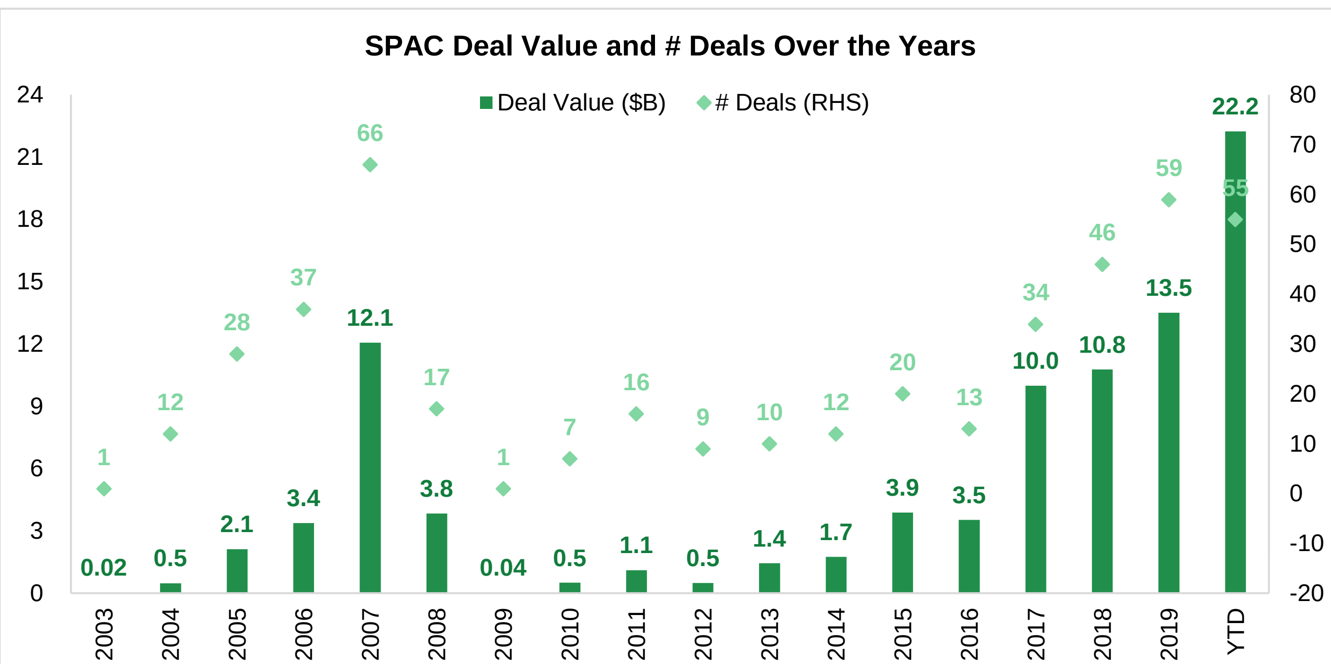
[1] Please see SIFMA Insights US Equity Capital Formation Primer

Analyzing SPAC Statistics

While SPACs have been around for many years, their recent uptake continues to increase. For the most part, the number of IPOs has been down over the last few years. Companies are staying private longer, with some estimating the average length before going public is now 12 years. SPACs grew in popularity as another tool to access capital. This trend accelerated in 2020, with the turbulent economic times forcing companies to search for liquidity. SPACs provide this source of liquidity at a time when companies need it most.

- **1990s**: SPACs have existed since the 1990s, disappearing with the growth of traditional IPOs for companies of all market caps in the later part of the decade
- **Early 2000s, pre-GFC**: SPACs returned in 2003, with 1 deal worth $24 million. For the next five years prior to the global financial crisis (GFC), SPACs grew at a 246% CAGR, peaking in 2007 at $12 billion deal value
- **GFC**: After starting off with $3.8 billion in deals, the market eventually closed in 2008; it remained essentially closed throughout 2009 (1 deal, $36 million deal value)
- **2010-2016**: SPACs returned in 2010, growing at a more modest pace for the next seven years (+29% CAGR), peaking in 2015 at $3.9 billion deal value
- **2017+**: SPAC deals have increased over the last four years, with average deal value $14.1 billion from 2017-2020 or $11.4 billion excluding 2020, (versus $2.5 billion from 2003-2016)
- **2020**: SPACs have already had their biggest year, with $22.2 billion in deal value through July (+65% Y/Y)

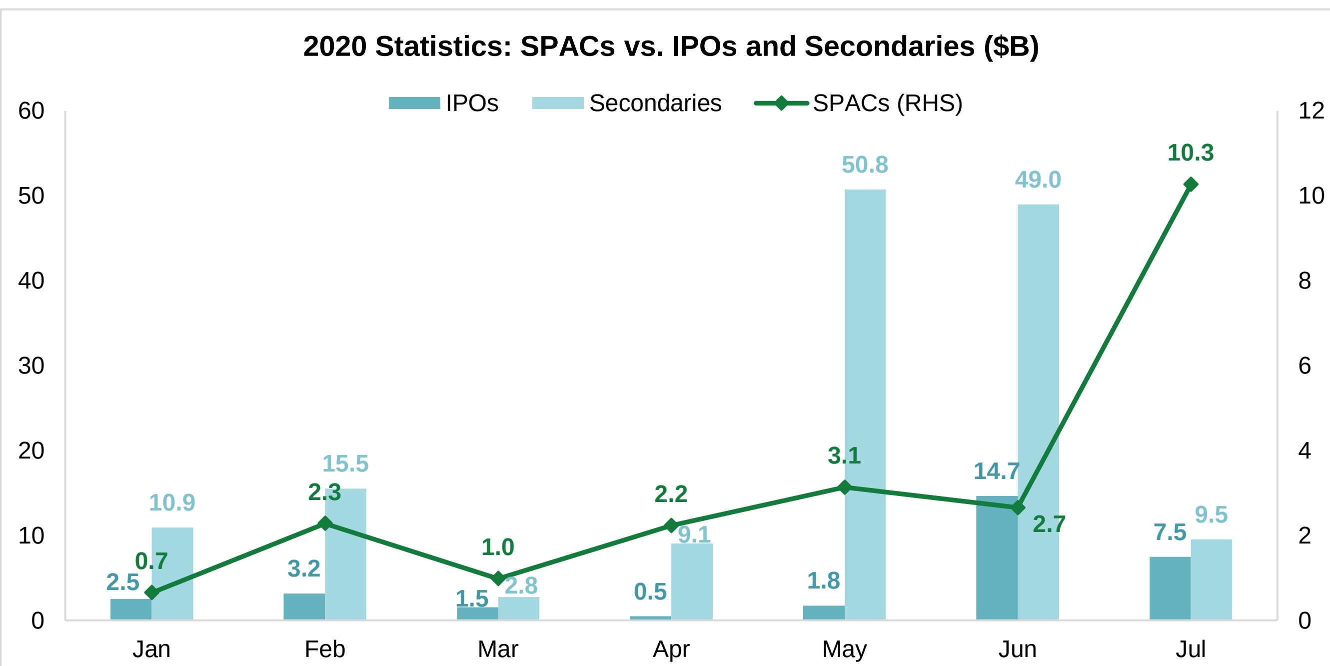


Source: Dealogic (YTD = July 2020)

SPACs vs. IPOs and Secondaries

At the height of the COVID-19 related market turmoil, total issuance of all types slowed substantially in March and remained muted in April. The first type of issuance to recover was secondary offerings (secondaries or follow-ons), as companies looked to strengthen balance sheets with cash infusions. IPOs recovered in June, followed by a SPAC explosion in July. SPAC founders continue to see unique opportunities in this economic environment to acquire stressed companies. And market participants expect SPAC growth to continue.

- **Secondaries**: After averaging $13.2 billion deal value at the start of the year, secondaries troughed in March at $2.8 billion deal value; this vaulted to $50.8 billion in May (+283% since the start of the year)
- **IPOs**: After averaging $2.9 billion deal value at the start of the year, IPOs troughed in April at $0.5 billion deal value; this recovered to $14.7 billion deal value in June (+414% since the start of the year)
- **SPACs**: After averaging $1.5 billion deal value at the start of the year, SPACs troughed in March at $1.0 billion deal value; this jumped to $10.3 billion in July (+599% since the start of the year)



Source: Dealogic

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