Maxam Arbitrage Fund – Q2 2024 Commentary

Dear fellow investors,

The Maxam Arbitrage Fund[1] gained +1.1% in the second quarter of 2024.

Performance in the second quarter was driven by 16 successful deal closures and our SPAC positions benefitting from liquidations, extensions, and the growth of cash held in-trust.

Attractive yields across our opportunity set and an improving environment for M&A activity supports our positive outlook for arbitrage.

Looking back.

The quantum of announced mergers and acquisitions continued to improve during the second quarter of 2024. We added 74 new definitive deals to our database, a 17% increase over the previous quarter and a 28% increase over Q2 2023.

The fund initiated 24 new merger arbitrage positions during the quarter, had 16 successful deal closures and experienced zero deal breaks.

Notable owned deals that successfully closed during the quarter included: Daseke, MediaValet, Orford Mining, Societal CDMO, IBEX Technologies, Think Research, NEOGAMES, Tricon Residential, Agitili Inc, ZeroFox Holdings, SP Plus, MDF Commerce, The LS Starrett co, Indigo Books & Music, Via Renewables, and Taro Pharmaceutical Industries.

At the end of the second quarter the fund was well diversified across 27 merger arbitrage positions.

Looking forward… to more M&A.

The improvement in deal volumes is encouraging, particularly against a backdrop where higher interest rates, a challenging regulatory environment, and U.S. election year uncertainty have undoubtedly hampered activity – especially for larger and complex transactions.

Continuing a trend that we have been highlighting, M&A activity was robust in the small and mid-capitalization segments of the market during the second quarter. Smaller companies are trading at much cheaper valuations than their larger brethren, making them accretive targets for opportunistic buyers. This continues to be an attractive portion of the arbitrage opportunity set for us to invest in – and we are also benefiting from this dynamic in our equity fund, the Maxam Diversified Strategies Fund.

And there is reason to be optimistic that deal activity will continue to increase and broaden out. Interest rates have likely plateaued and appear poised to start declining, providing would-be acquirors with additional financial flexibility and firepower. The prospect of a Republican administration would also likely create a more predictable regulatory environment for deal-makers – although we suspect many larger transactions may wait for the outcome of the US election before proceeding.

Maxam Capital Management Ltd.
330 – 609 Granville Street Vancouver, BC, Canada V7Y 1A1 T 604 685 0201 F 604 685 9970

Supporting future deal activity even further is the increasing pressure that private equity firms are under to deploy their record US $1.2 trillion of capital – more than 26% of which was raised over four years ago[2].

Northern lights.

Many of our positions tend to be in deals south of the border, where there is consistently a variety of solid deals to choose from. Canada is a much smaller market than the U.S. both from a capitalization perspective and in terms of the number of companies – and thus typically experiences less deal activity as a result.

Of late, we are seeing an increase in takeover activity up North – certainly in part due to the attractive valuations that many quality Canadian companies trade at relative to their US counterparts. From cemetery and funeral services provider Park Lawn and payment technology company Nuvei to decision analytics company Copperleaf Technologies and community solar project developer UGE International – there are some solid deals with attractive arbitrage yields to choose from.

I had a *flashback to 1998* when the news hit the wire on July 11th that National Bank had reached an agreement to acquire Canadian Western Bank.

26 years ago, Canada's finance minister did not allow the proposed mergers of Royal Bank + BMO and TD + CIBC to go through – citing too much power in the hands of too few banks and a significant reduction of competition.

While the National + CWB transaction is likely to be a longer dated deal, perhaps with some political twists and turns, this is a different deal in a different competitive landscape than the 1998 proposed bank mergers.

Deal activity is picking up, and there is lots to do… including up here in Canada.

Dr. Market, is that a pulse?

After only six SPAC IPOs in the first quarter and zero in April, the SPAC market came to life in May and June with the biggest new issuance quarter in two years. 10 new SPACs raised over US $1.8 billion in the quarter, a promising sign given that all of 2023 saw less than US $4 billion raised. While still a far cry from the lofty issuance years of 2020 and 2021 – when nearly US $250 billion was raised in two years – it is encouraging to see fresh (or recycled) capital being deployed into SPACs.

There were 218 listed SPACs at the end of the second quarter, inclusive of the new IPOs, which is 17 fewer than the previous quarter as closed deals and liquidations outnumbered new issuances[3].

Risk adjusted returns across the SPAC universe are healthy – the projected median IRR was above 6% for most of the second quarter, and this has continued into Q3. The SPAC market remains actionable for our nimble and active approach, allowing us to high-grade our holdings and take advantage of liquidations, extensions and trading opportunities.

At the end of the second quarter the fund was diversified across 66 SPACs.

An attractive and improving opportunity set.

While we are not yet back to pre-Covid M&A activity levels, deal volumes have been solid and appear poised to improve with the anticipation of interest rate cuts, a broadening of market breadth and private equity buyout funds sitting on record amounts of undeployed capital.

Existing merger arbitrage yields on solid and uncomplicated deals are as attractive as we have seen in several years. And SPACs, backed by T-bills held in-trust, continue to offer very attractive risk-adjusted yields.

Maxam Arbitrage Fund has demonstrated its unique value over the last few years – during both equity and bond market volatility – providing investors with the ability to diversify risk and create more robust portfolios.

We expect arbitrage to generate positive returns regardless of the market environment – and we think we have a particularly attractive environment in front of us.

Thank you for your trust and confidence. Please don't hesitate to reach out with any questions.

Sincerely,

Travis Dowle, CFA
President & Fund Manager
Maxam Capital Management Ltd.

[1] Maxam Arbitrage Fund, Class F, net of fees and expenses. Inception date October 1, 2020. Please contact us regarding other series of fund units or visit our website www.maxamcm.com

[2] https://commercial.bmo.com/en/us/resource/mergers-acquisitions/specialty-finance/middle-market-ma-update-q2-2024/

[3] SPAC data is from spacresearch.com