Katten

2021 SPAC SURVEY REPORT

SPAC to The Future: Despite Slowdown, SPACs Continue to Be Viewed as Favorable Investment Opportunities

MAY 2021 | katten.com

SPAC to The Future: Despite Slowdown, SPACs Continue to Be Viewed as Favorable Investment Opportunities

In the first quarter of 2021, 296 initial public offerings (IPOs) of special purpose acquisitions companies (SPACs) were completed. That's 48 more than in all of a record-breaking 2020 – when the total number of SPACs grew by more than 300 percent over 2019.

> ***72%*** *of investors who have participated in a SPAC transaction agree that SPAC IPO activity will be strong through at least 2022.*

But then, suddenly, the pace of new issuances slowed dramatically. In late April, research analysts noted that the market had "screeched to a halt" with only six new SPAC IPOs completed at that point in the second quarter. Media, investors, regulators and politicians picked up on the cooldown, which continued well into May. And the burning question remained: What does the future hold for SPACs?

The sentiment, according to law firm Katten Muchin Rosenman LLP's new survey report, is one of optimism – at least through 2022. When we conducted our first poll of 80 investment professionals back in early March, 75 percent of investors who had participated in at least one SPAC transaction – as sponsors, investors, advisors, or underwriters – said they expected SPAC activity to increase through next year.

Despite an underwhelming second quarter, our second poll – held in May, of 100 respondents – revealed continued, undaunted optimism: 72 percent of investors who have participated in a SPAC transaction agree (with 44 percent of those strongly agreeing) that SPAC IPO activity will be strong through at least 2022. Not surprisingly, those who have not participated in a SPAC are more skeptical – just 32 percent feel that activity will be strong through 2022. Even prior to the second quarter breather, (in March) only 45 percent of investors who hadn't participated in a SPAC transaction said they were likely to in the next 12 months. In May, 53 percent of those respondents said they were somewhat (33%) or far less (20%) likely to participate in SPACs, perhaps indicating a fear of the unknown.

And overall, 69 percent of respondents to our second poll believe SPACs will make for favorable investment opportunities moving forward; 19 percent are unsure, and only 12 percent do not believe this to be the case.

"Investors expect that the conditions that have fueled SPACs' growth over the last few years will continue to exist for the foreseeable future," says Brian Hecht, a partner in Katten's New York office. "There will be some ups and downs along the way, including the relative slowdown in SPAC IPOs we're seeing now, for a variety of reasons, including some pullback from the stock market run-ups that SPACs had been experiencing, recent pronouncements from the Securities and Exchange Commission (SEC) and perhaps just a perception that it's an appropriate time for the SPAC market to catch its breath after the frenetic activity in the first quarter. But it appears, more generally, that the momentum fueling the SPAC market is sustainable."

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Plentiful Capital, Efficient Offerings

The two polls – of investment professionals from private equity, venture capital, hedge funds, and investment banks – that constitute this survey report are aimed at assessing the SPAC boom, its drivers, and, of course, its recent slowdown.

Why do survey respondents remain so enthusiastic on the SPAC market? Mainly because of the availability of capital – and with interest rates at historic lows, and private equity funds sitting on nearly $2 trillion in dry powder, investment capital should remain abundant for the foreseeable future.

A portion of that capital will likely be drawn to SPACs, adding to the $81 billion raised through blank-check offerings in the first quarter – a figure that would have been nearly impossible to imagine just a few years ago when SPACs were still widely considered an obscure and even somewhat undesirable vehicle for investor and acquisition targets.

But, as the survey clearly shows, the negative perceptions have all but vanished in the last two years. Investors now view SPACs as a viable and frequently preferable alternative to traditional IPOs. Prior to the slowdown in April and May, media coverage of the SPAC boom focused on the benefits of a reduced regulatory burden, speed to market and ability to lock in pricing as the factors driving SPACs' proliferation. More recently, media coverage has focused on the SEC turning up the heat, as well as other risks such as litigation. However, the swing in media headlines and market activity doesn't appear to be tempering investment professionals interest in SPACs.

Our original survey results largely concurred: in our first poll, 76 percent of respondents said SPAC business-combination transactions compare favorably to traditional IPOs for private companies because they offer a simpler process. And SPAC issuers have had additional flexibility with respect to transactions compared to traditional IPOs, creating free space for SPAC target companies to tell their stories to investors – an advantage that 74 percent of initial survey respondents cited for SPAC deals.

SPAC to The Future: Despite Slowdown, SPACs Continue to Be Viewed as Favorable Investment Opportunities *(continued)*

That said, some of this advantage may be eroded as regulators increase their focus on SPAC disclosures. The heightened pressure perhaps explains why, in our second poll, 56 percent cite increased SEC scrutiny as a contributor to the recent slowdown. Other top contributors noted are increased litigation risk (52 percent), market saturation (38 percent) and trading market performance (30 percent).

Despite these factors, the surge in SPACs appears far from over – especially as more investing professionals have flocked to SPACs, as target companies have increasingly come to embrace them as a preferred access path to equity markets and as capital pours in from cash-rich investment funds. In fact, it may still be in the early stages.

"Our findings make it clear that even with this dip, investors are eager for more SPACs," says Kimberly Smith, Partner and global chair of Katten's Corporate department. "And while regulatory scrutiny or shifting market conditions could curb their appetite, it seems safe to say that SPACs aren't going away."

Among the survey's other key findings:

- Investors' decisions about whether to participate in a SPAC offering are primarily driven by their confidence in the SPAC's prospects for creating value in the eventual merger with a target company (the de-SPAC transaction) and their trust in its team.
- As investors get clarity on SEC guidance and counsel on mitigating litigation risk, SPAC IPO activity will begin to pick up. A return of de-SPAC activity will also help restore momentum to the SPAC IPO market.
- Increased SEC scrutiny and litigation risk are top contributors to the SPAC slowdown, according to both SPAC veterans and those who have not yet taken part in a SPAC.
- Independent sponsors have proliferated in the past year; most independents are professionals who recently left investment firms or are being joined by bigger institutional players. According to our respondents: 70 percent say independent sponsors are on the rise as SPACs become a mainstream investment tool.
- Looking ahead, more 69 percent of respondents to our second poll believe that SPACS represent a favorable investment opportunity over the longer term.

SURVEY FINDINGS AND DATA

Investors Expect Strong SPAC Activity Through 2022

1

May 2021

The SPAC surge that began in 2020 grew into a high-octane investment in early 2021 – new SPACs raised $93.8 billion in the first quarter, 12 percent more than in all of last year (which itself was a record year for SPACs). While the second quarter has seen a drastic slowdown – leading to [cries]() of a speculative bubble – many SPAC IPOs are expected to be completed at some point in the months ahead.

"The market for SPACs has cooled for the moment, but it hasn't gone away – because investors continue to see SPACs as valuable places to deploy capital," says [Mark Wood](), Partner and National Chair of Katten's Securities practice. He added, "We don't know when SPAC IPO activity will pick back up, but we are optimistic that it eventually will, even if not at the rates we saw in 2020 and early 2021."

Respondents to our surveys – in both March and May – clearly agree that the fears of a SPAC bubble are overblown. Even after the market cooled off, 62 percent of respondents (and 72 percent of respondents who have previously participated in a SPAC transaction) agree that we can expect SPAC IPO activity to remain strong at least through 2022. Thirty-eight percent of all respondents and 44 percent of SPAC respondents strongly agreed.

What's more, when asked how they feel about their participating in a SPAC in May versus earlier this year, nearly 70 percent say they feel the same or are more likely (38 percent) to participate, including nearly half of those who haven't done so thus far. Less than a third (31 percent) – mostly comprised of those who haven't participated already – say they are less likely to participate.

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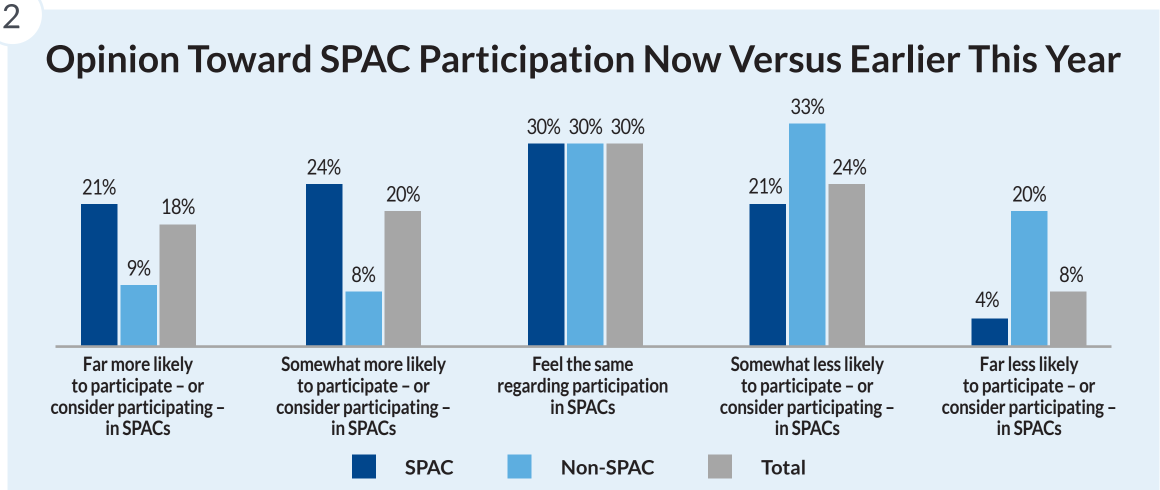

May 2021

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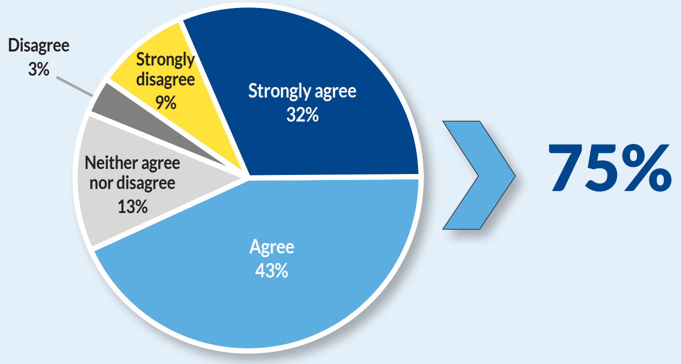
SPAC Activity Will Increase Through at Least 2022



March 2021

These numbers are in keeping with our earlier poll, when 75 percent agreed that SPAC activity will continue to increase through 2022 and nearly half of those who have yet to participate in a SPAC said they are likely to participate in a SPAC in the next 12 months.

"While recent events that have occurred in the second-quarter of this year may have tempered some of the rush to form and launch SPACs, it seems clear from our survey results that the investment community believes that SPACs haven't reached full saturation and that there may still be room for expansion," says Christopher Atkinson, Partner and Co-Chair of Katten's Mergers & Acquisitions and Private Equity practice.

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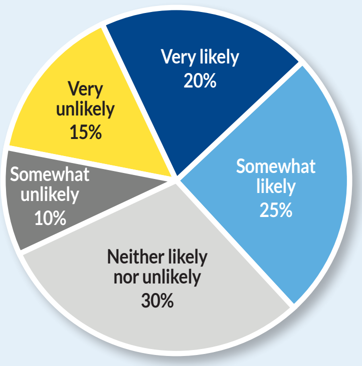
Likelihood to Consider Participating in a SPAC Deal in Next 12 Months



March 2021

SPACS Moving Forward

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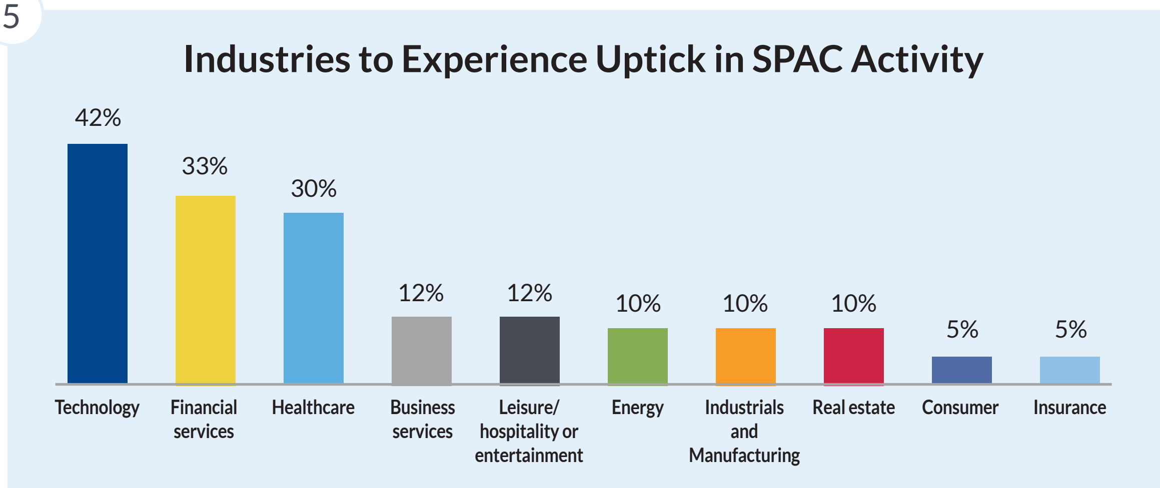

March 2021

The SPAC boom has so far been largely concentrated in industries with the highest concentration of growth companies: technology, financial services and healthcare. Since 2019, 82 SPACs have formed to target companies in technology – far more than in any other sector.

The investors we surveyed believe those three sectors will continue to attract the greatest additional SPAC activity. And perhaps surprisingly, only 10 percent of respondents believe the energy sector will see growing SPAC activity, while just 5 percent predict an uptick in consumer SPACs. Ironically, those sectors – energy and consumer – have been among the most active to-date; 34 SPACs have formed to target consumer companies since 2019. Another 21 have formed to target energy companies.

Overall, survey respondents see a bright future for SPACs moving forward: despite the recent halt, 69 percent of participants in our second poll believe SPACs are favorable investment opportunities moving forward. Nineteen percent are unsure, while only 12 percent do not believe this to be the case.

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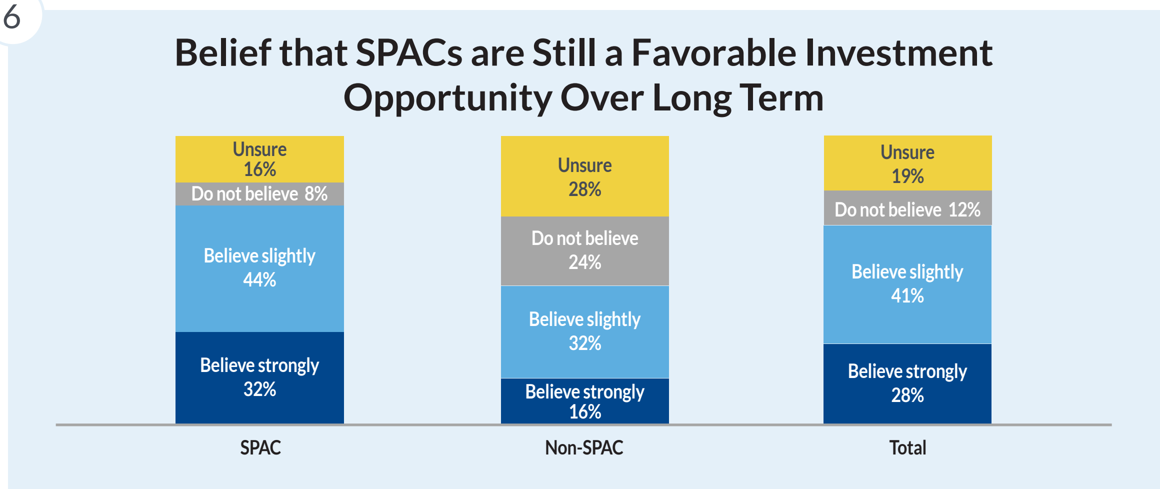

May 2021

SPACS vs. IPOs: Partnerships, Processes and the Market Continue to Fuel SPAC Surge

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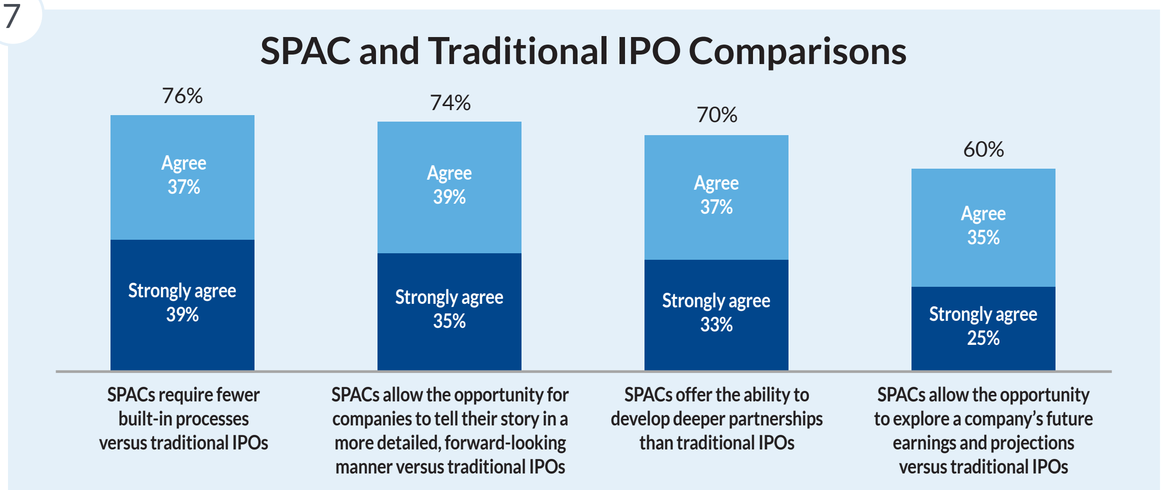

March 2021

For years SPACs were considered an obscure, even undesirable investment vehicle. But as investors have discovered – in droves – over the last 24 months, these "blank-check" companies present an efficient and increasingly well-understood option for taking a private company public.

They also offer advantages over traditional IPOs. The biggest, according to the investors surveyed in our first poll, was a smoother procedural process; when merging a SPAC with target companies, SPAC sponsors don't face the same regulatory and process burdens that come with a traditional IPO. As a result, SPACs can often quickly complete mergers with target companies – sometimes in as little as 60-90 days, according to investors we interviewed – versus 6-12 months between initial filings and public offering for traditional IPOs.

The use of projections in connection with SPAC mergers is clearly an important differentiator between SPAC transactions and traditional IPOs. Legal risks typically prevent companies preparing to go public, and their underwriters, from engaging in forecasting of results. Specifically, in a traditional IPO, the safe harbor for forward-looking statements, which can protect the offering participants against liability, is not available. But that safe harbor does apply outside of the IPO context, which has led to more fulsome storytelling in connection with SPAC business combination transactions; in particular, the SPAC transaction parties typically speak in detail about future projections – in contrast to the traditional IPO process. So it's no surprise that 74 percent of respondents to our first poll said that kind of storytelling differentiates SPACs from IPOs, and another 60 percent said exploring future earnings is a differentiator.

"Our financial model is easy to explain, but you can't just pitch it in an elevator," says a senior executive at an automated lending platform. "The people investing with us had to get into the weeds to understand it more thoroughly, and doing a SPAC gave us that opportunity."

It also important to note, however, that recent statements by SEC staff members indicate that increased regulatory scrutiny may be on the way around disclosures and other SPAC attributes. A public statement issued by Division of Corporation Finance Acting Director John Coates in early April further indicated that much of that scrutiny will focus on forecasts made by SPAC sponsors and targets, and Coates questioned whether the forward-looking safe harbor would in fact apply to the presentation of forecasts in connection with the SPAC business combination. A few weeks later, SEC staff issued a separate statement challenging the appropriateness of the accounting treatment applied to the warrants that SPACs issue to investors, indicating that such warrants should be classified as a liability, not equity as SPACs had traditionally done. This statement set in motion a flurry of activity to address (and in many cases re-state) the financial statements for existing SPACs and adjust the disclosures and accounting treatment related to the warrants in filings for new SPACs. This statement further signaled the SEC's determination to apply regulatory scrutiny in what had been a red-hot SPAC market.

"The regulatory environment around SPACs is evolving quickly," says Wood. "We are regularly advising our clients with respect to appropriate steps to make sure they are not only currently compliant but also prepared to adapt to regulatory shifts."

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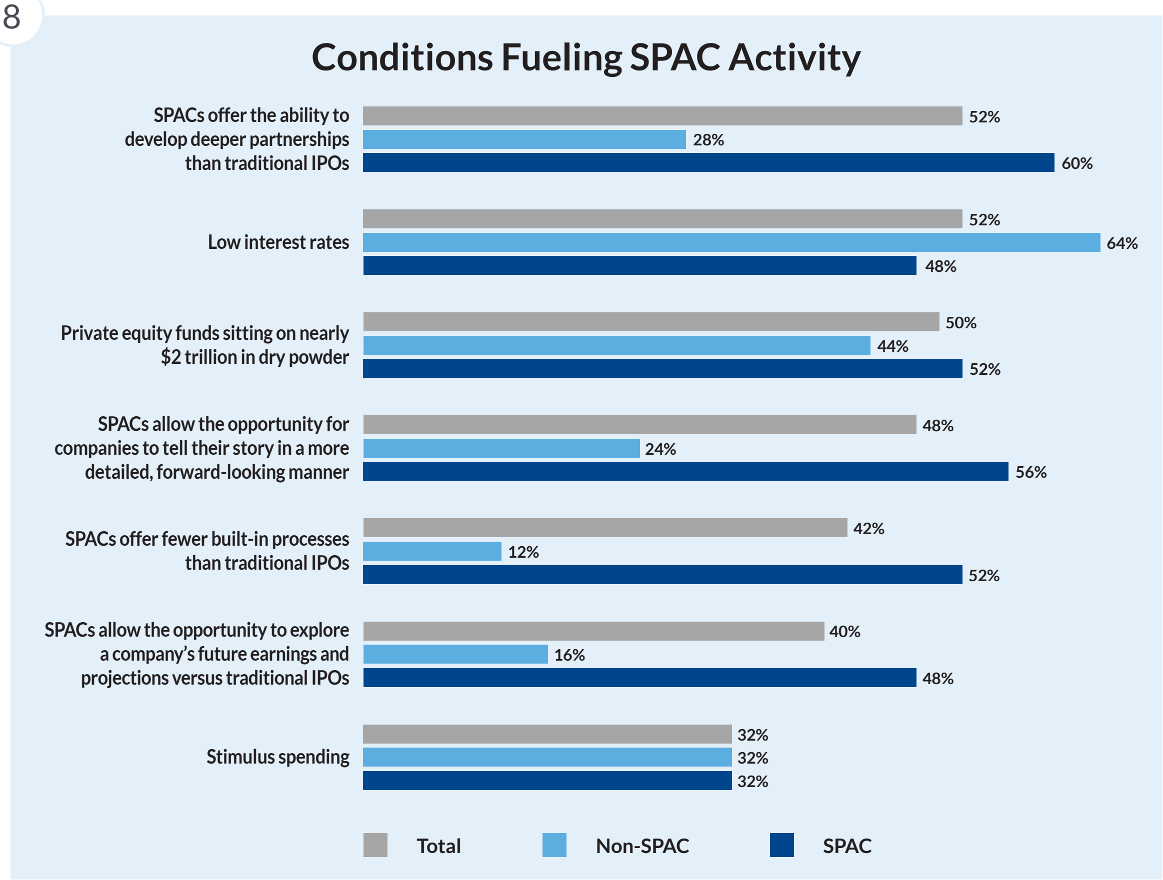

May 2021

Our follow-up poll reveals that while heightened scrutiny has perhaps injected some uncertainty into the benefits of a SPAC process, most participants remain enthusiastic about various elements. When asked what conditions are fueling SPAC IPO activity, more than 40 percent of all respondents note that SPACs (versus traditional IPOs) offer the opportunity to explore a company's future earnings and projections, fewer built-in processes (42 percent), and the ability for companies to tell their story in a more detailed, forward-looking manner (48 percent).

The idea that SPACs represent partnerships between sponsors and target companies increases their appeal as well. In our first poll, 70 percent of respondents said the ability to develop partnerships distinguishes SPACs from traditional IPOs, and in interviews, investors and target-company executives repeatedly emphasized the value of partnerships; in our second, the ability to develop deeper partnerships was selected as the top driver driving SPAC activity (52 percent).

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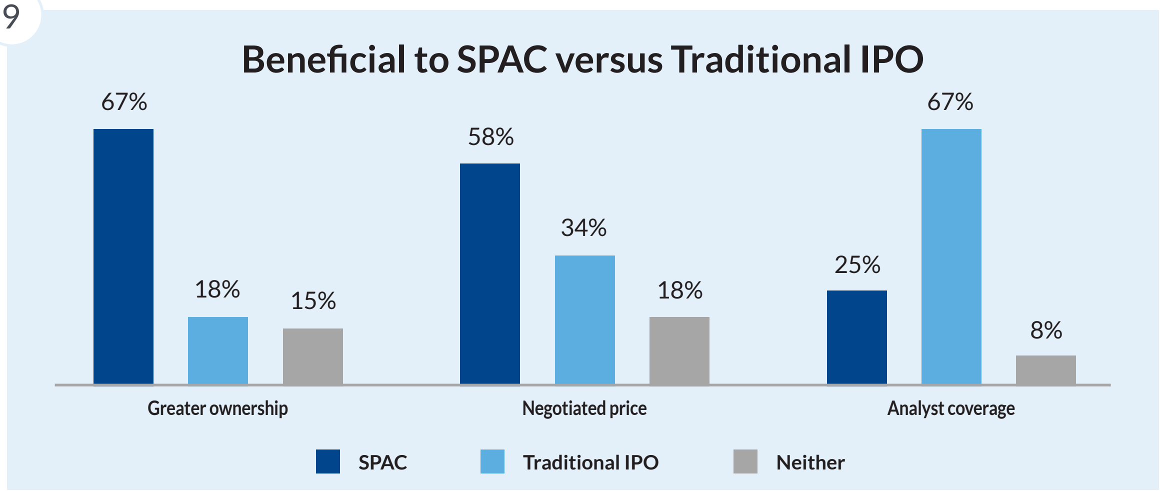

March 2021

Investors consider negotiated price a greater benefit of SPAC transactions. That's likely because SPAC transactions enable a SPAC and its sponsor to agree on a price with the target company, just as they would in a private transaction, while IPO pricing is determined by the public market at the end of the IPO process and therefore subject to far greater volatility and uncertainty.

Analyst coverage is the only characteristic we presented that favors IPOs – but it's an important one. A pre-IPO company engages underwriters and financial advisors at institutions that in turn assign sell-side research analysts to cover both the offering and the business moving forward. The SPAC process doesn't always generate those connections, which may leave the typical post-SPAC company with little or no analyst coverage during its early months as a public company, reducing its exposure to the investment community – including institutional investors.

"You really need coverage on Wall Street for potential growth," says a managing director of a private investment firm. "Not everyone understands the need for analyst coverage – but it's critical."

SPAC sponsors and target-company leadership may generate analyst coverage by engaging multiple investment banks in the merger or merger financing process, or in follow-on offerings that engage multiple institutions. Otherwise they can seek coverage through investor relations campaigns – including post-SPAC road shows and other engagement efforts.

Market Factors Play a Role, Too

As noted in our executive summary, the strong state of the current market overall also contributes to robust SPAC activity. In our more recent poll, 52 percent of respondents say low interest rates are fueling SPAC activity, 50 percent cite private equity funds – which are sitting on nearly $2 trillion in dry powder – and 32 percent cite stimulus spending (see chart on page 9).

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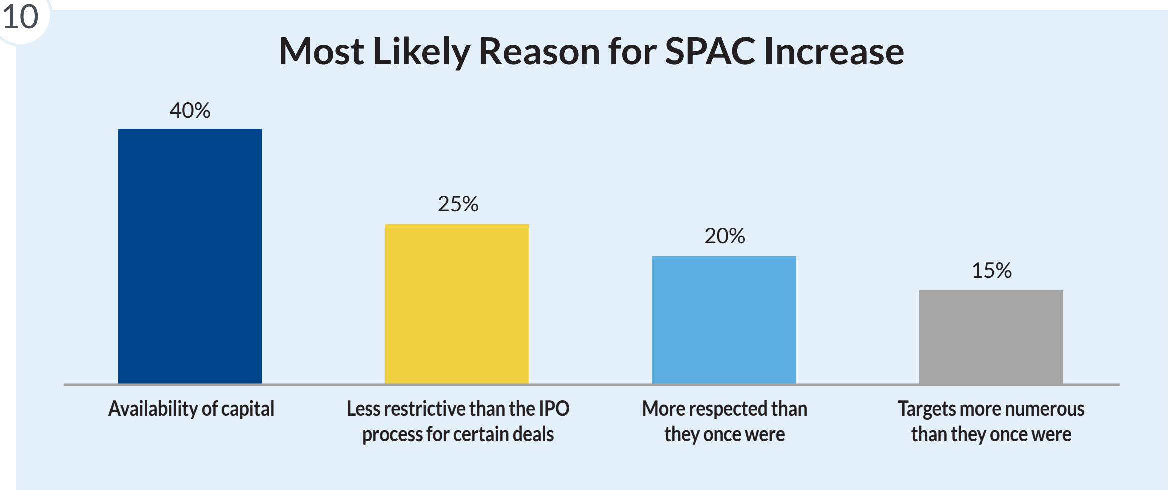

March 2021

In our initial poll, we asked investors who have not yet participated in a SPAC what they believe is fueling the boom in SPACs. Nearly half (40 percent) pointed to the availability of capital. That's far more than any other reason, including more commonly cited factors – the less restrictive process (25 percent) and SPACs' increasing respectability (20 percent).

The investors' belief makes sense in light of the staggering amount of dry powder on hand that will likely take years to deploy – providing yet another reason to believe the SPAC boom could carry on through 2022, and beyond.

The SPAC Slowdown, Explained

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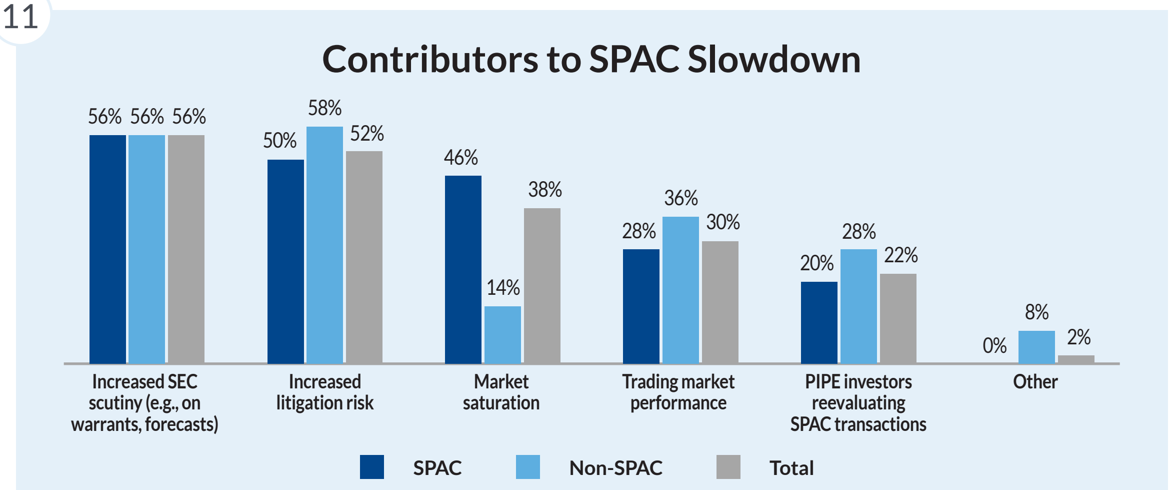

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As previously noted, the SEC is continuing to ramp up its scrutiny of SPAC disclosures, forecasts, warrants and other areas. Meanwhile, the risk of litigation continues to rise – whether plaintiffs are targeting the adequacy of proxy statement disclosures, the quality or selection process for the merger target, and/or allegations that the post-merger operating company misled investors. It tracks that respondents see these two factors as the top contributors to the recent SPAC slowdown, chosen by 56 and 52 percent of participants, respectively.

While these concerns are legitimate, most SPAC participants don't view them as fundamental problems with the model itself. The warrant issue, for instance, is technical in nature and can be addressed through changes to the provisions in the warrant agreements or changes in the accounting treatment applied, while the litigation risks in the long-term should be (broadly speaking) consistent with the risks faced in other capital markets deal activity, including traditional IPOs and public company M&A.

Anecdotally, SPAC participants are entrenched in the evolving market landscape. For instance, it's telling that, while 46 percent of SPAC participants see market saturation as a significant contributor to the slowdown, only 14 percent of respondents who have not participated in a SPAC transaction say the same. This may suggest that those on the outside looking in might be worried more about what are likely short-term issues (e.g., warrants), while those on the inside recognize the importance of market ebbs and flows to SPAC activity.

What Draws Investors To A SPAC? What Turns Them Away?

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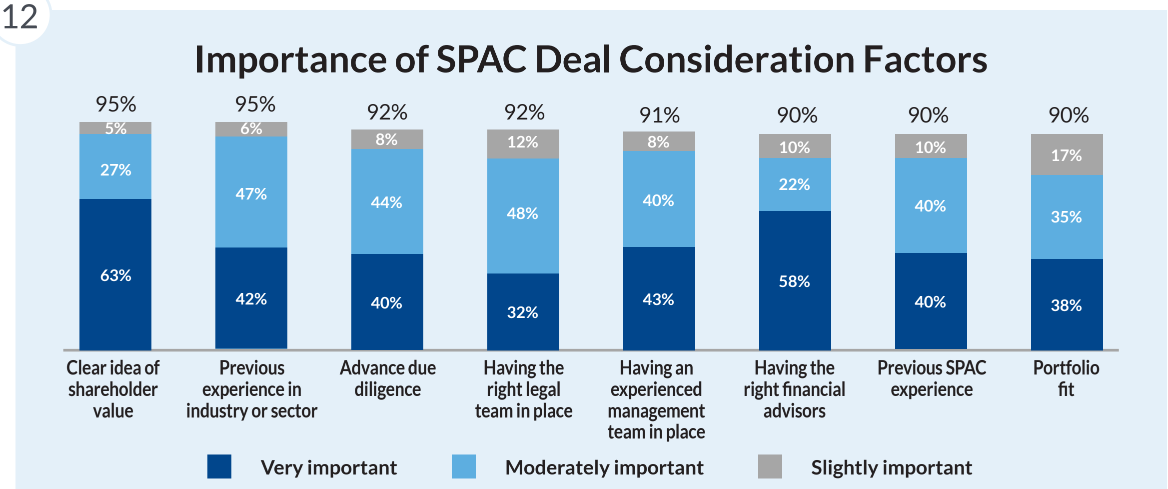

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Investors' decisions about whether to participate in a SPAC's IPO are primarily driven by their confidence in prospects for creating value in an eventual merger with a target company (the de-SPAC transaction) and their trust in its team. An understanding of shareholder value and previous management experience in the industry or sector rank as the top factors for the investors we surveyed. Nearly two-thirds of respondents in our first survey ranked clear shareholder value as "very important" – far more than any other factor.

And more than 90 percent of initial respondents said that the right legal team and financial advisors, and an experienced management team, are important in deciding whether to form a SPAC. In interviews, investors frequently emphasized the value of knowledgeable, experienced leadership for SPACs.

"It's a true partnership," says a senior executive at a global alternative investment manager. "You have to be patient about the right team, right company, right fit so everyone can share in the upside of the public company – it's easier said than done."

What Draws Investors To A SPAC? What Turns Them Away? *(continued)*

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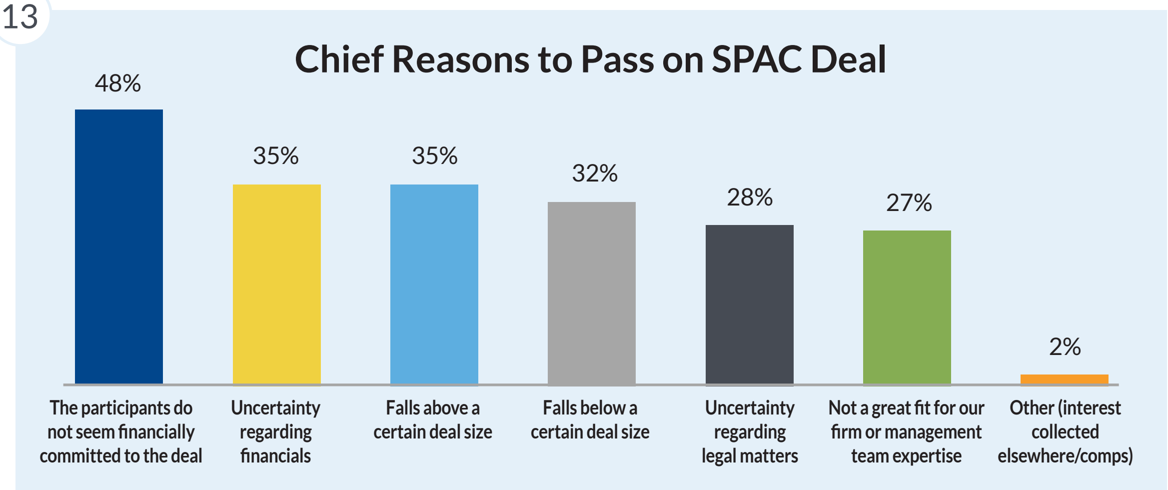

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Nearly half of respondents said they'll pass on joining a SPAC formation when the participants don't seem financially committed – more than any other reason for turning down a SPAC opportunity.

That is likely an outgrowth of the nature of SPACs, which allow investors to exercise redemption rights and pull cash out before the SPAC merges with a target company. That rarely occurs in practice, but when it does, it can leave the SPAC without enough capital to complete a deal, which would likely trigger a flood of investors asking to redeem their shares – an unfortunate outcome for the sponsor.

Independent Sponsors Proliferate – And Bring Deep Experience

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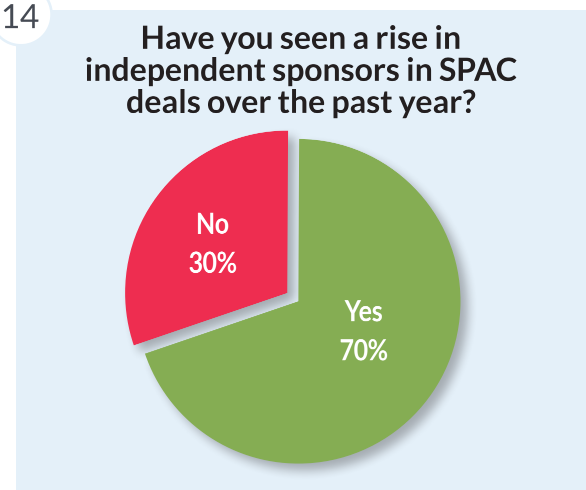

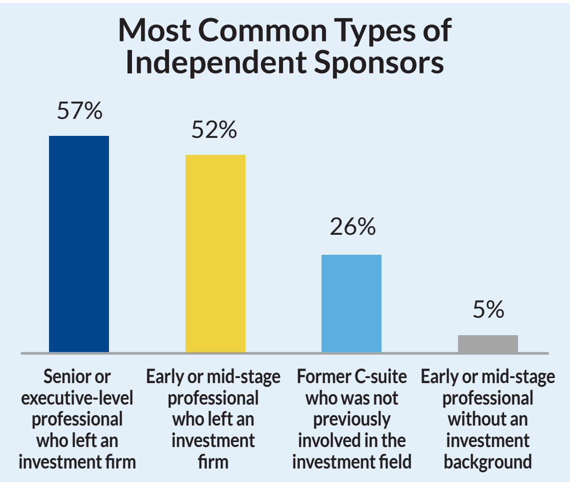

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Historically, SPACs were dominated by independent sponsors – serial entrepreneurs and former private equity executives using a relatively obscure vehicle to take relatively obscure companies public.

Their success led many bigger institutional players to aggressively move into SPACs over the last year – a phenomenon that has been well-documented. Meanwhile, independent sponsors aren't going away. In fact, they're also pouring into the space, according to our respondents: 70 percent say independent sponsors are on the rise as SPACs become a mainstream investment tool.

And these sponsors are predominantly experienced investment professionals; 57 percent of respondents to our first poll said the independent sponsors they've seen are senior-level executives who previously worked at investment firms. Another 52 percent said they're seeing early- or mid-career professionals from investment firms.

"What you find is that there are individuals who want to make money off an individual deal, so they will go create their own SPAC," says John Flynn, Chairman and CEO of Open Lending, a lending-analytics business that went public in a $1.7 billion SPAC business combination transaction in June 2020. "We liked the pedigree of the two gentlemen who started [Open Lending's SPAC] – you see a lot of that going on."

What's Holding Back Those Who've Yet to Do a SPAC?

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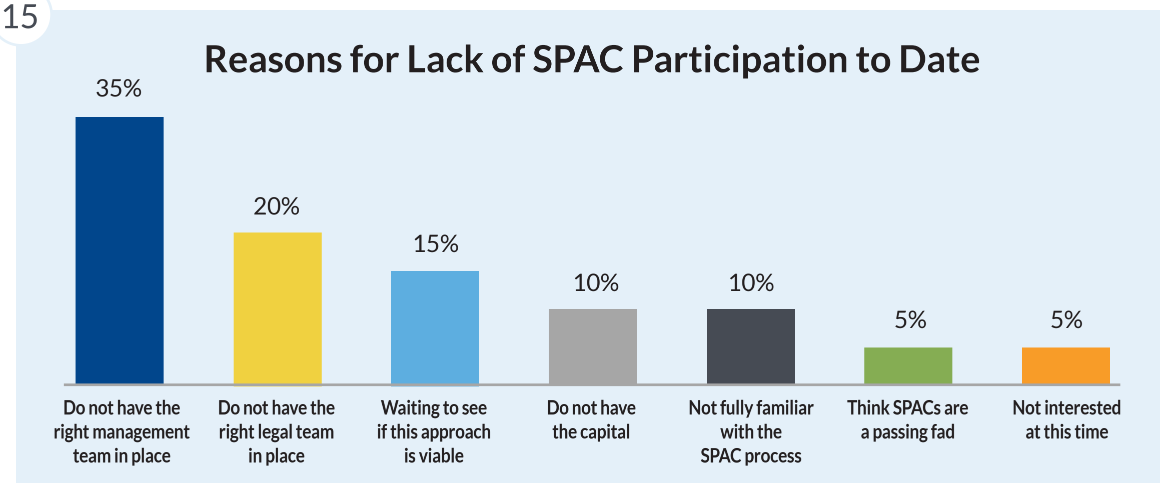

March 2021

Among initial respondents who have yet to participate in a SPAC transaction – 25 percent of total respondents – slightly more than a third said in our March survey that it's because they haven't had the proper management team in place.

That makes sense insofar as it's critical to enter a SPAC process with a dedicated, experienced, knowledgeable management team. But "experienced" may be where some firms are getting hung up. While SPACs seem to be ubiquitous, they remain somewhat unfamiliar relative to traditional IPOs or other fundraising and exit vehicles.

"Some firms may simply not have the capacity to jump into SPACs," says Smith. "But some may be overestimating the complexities involved in forming a SPAC; investment professionals who manage IPO processes should be able to pivot to SPACs if they're given the mandate – and the time."

Methodology

Katten conducted both qualitative and quantitative research as the basis for this report. The firm first conducted interviews of three investors and two operating-company executives with SPAC experience in February 2021. These interviews were followed by an online survey in March 2021, which targeted 80 U.S.-based senior leaders and key decision makers from investment banks (30 percent), private equity firms (29 percent), venture capital firms (25 percent) and hedge funds (16 percent). Twenty-five percent of the group consisted of respondents who had not yet participated in a SPAC as either an investor, advisor, underwriter or sponsor. We issued a follow-up online survey to 100 survey participants fitting the same demographic profile in May 2021. Reponses were anonymous, and data was analyzed in the aggregate. These individuals were recruited through a leading global B2B online panel provider.

Survey Demographics

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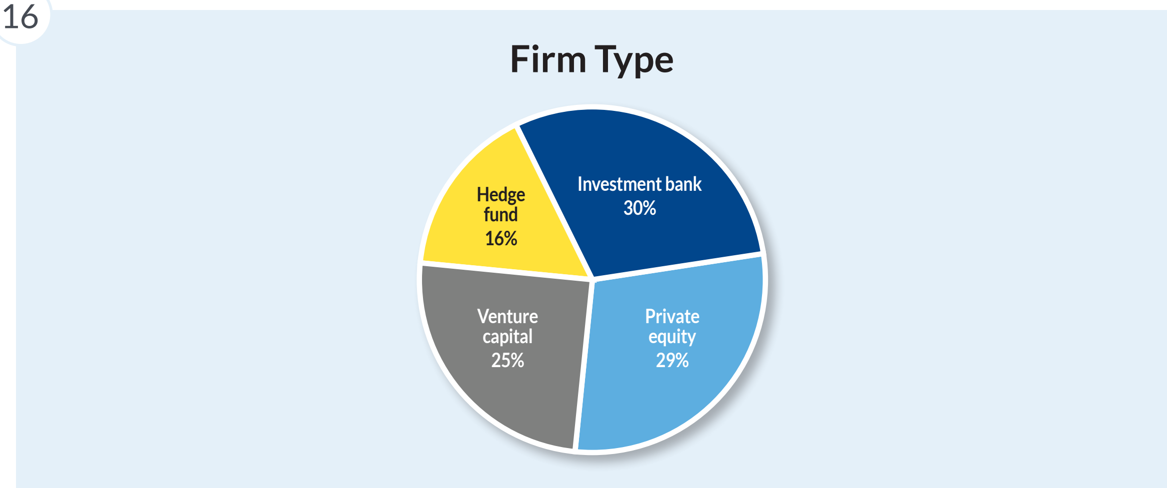

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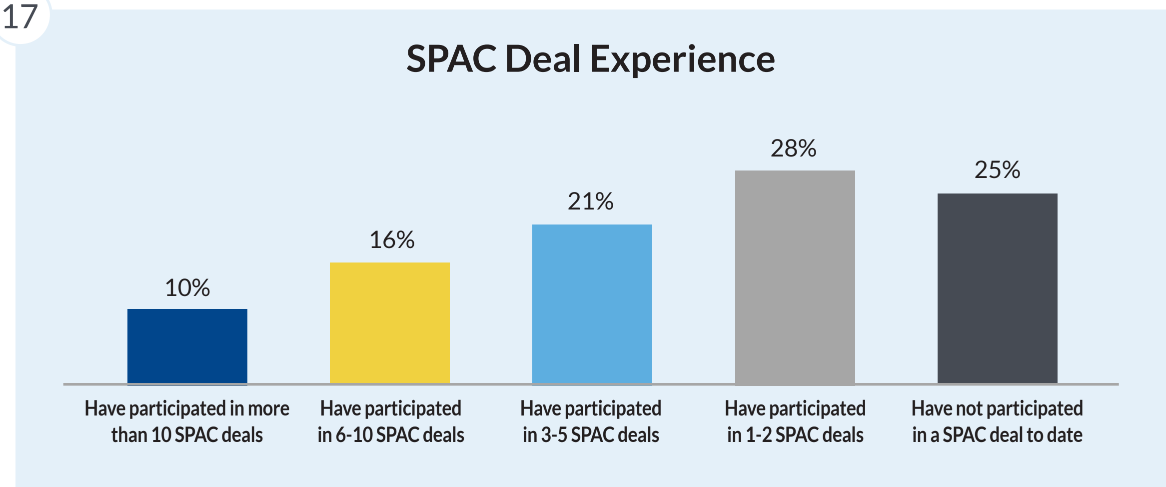

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Survey Demographics

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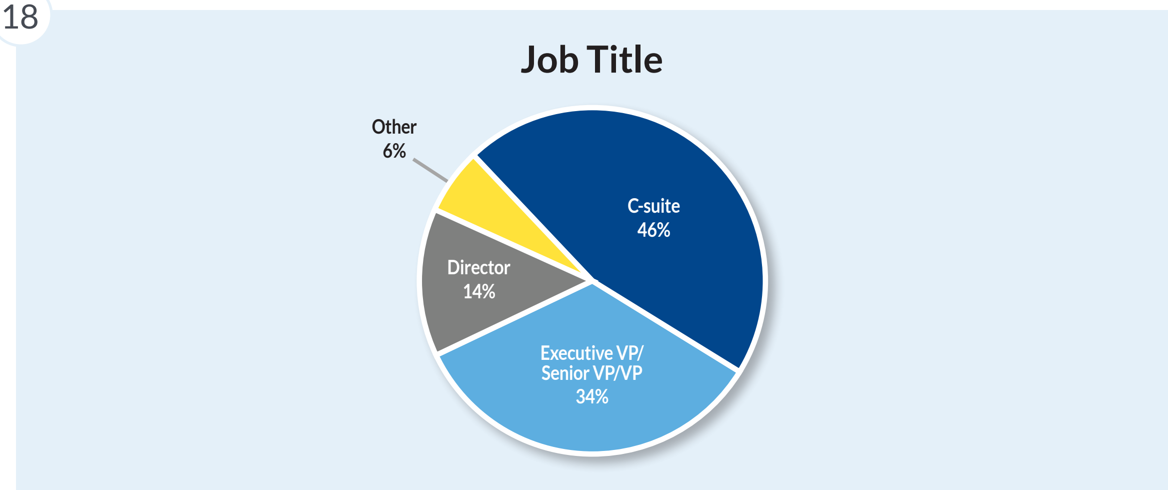

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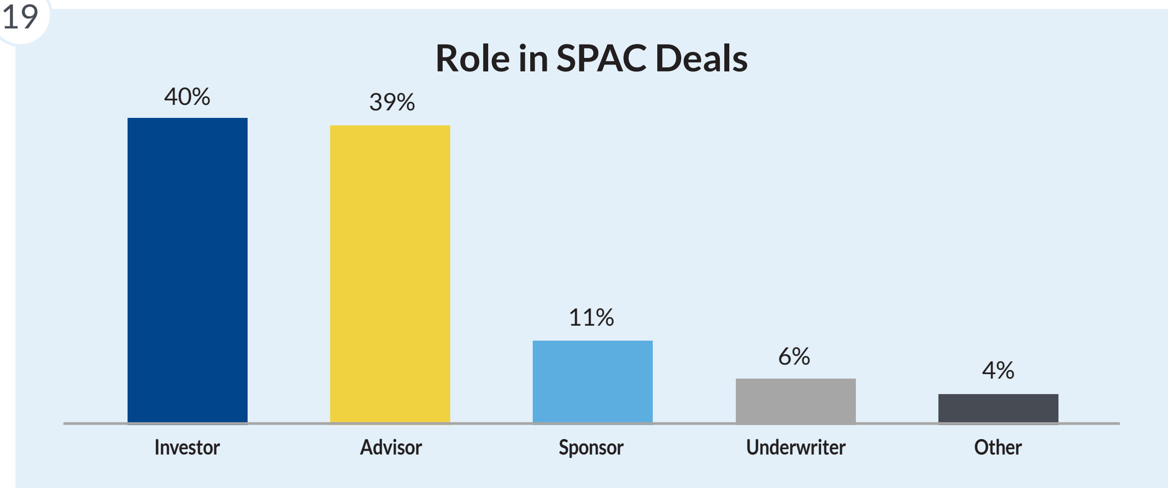

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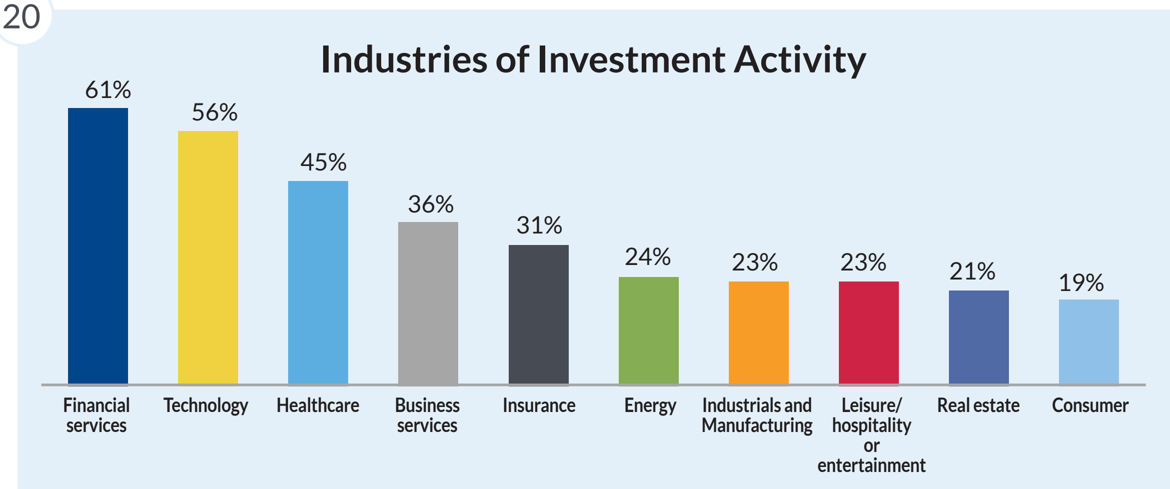

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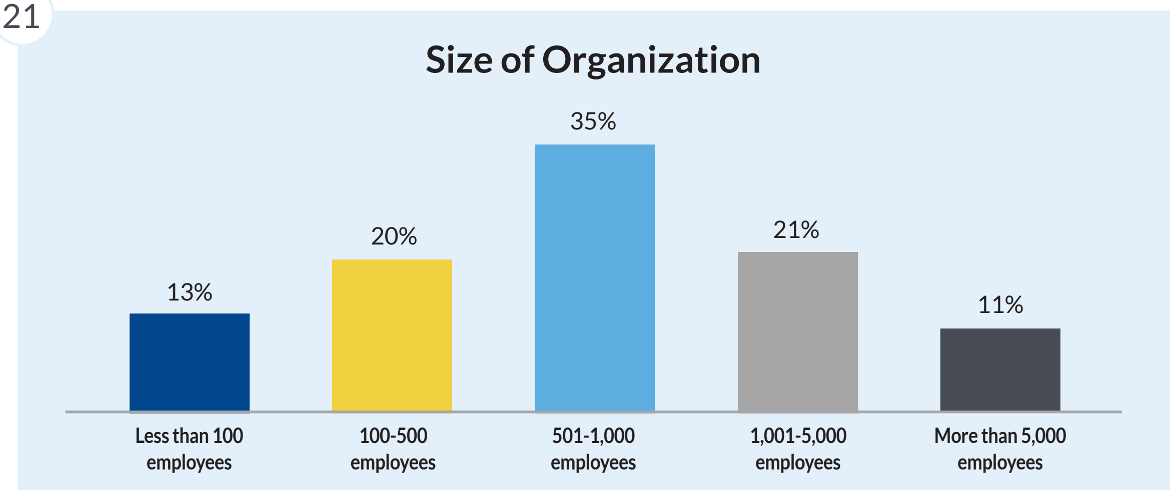

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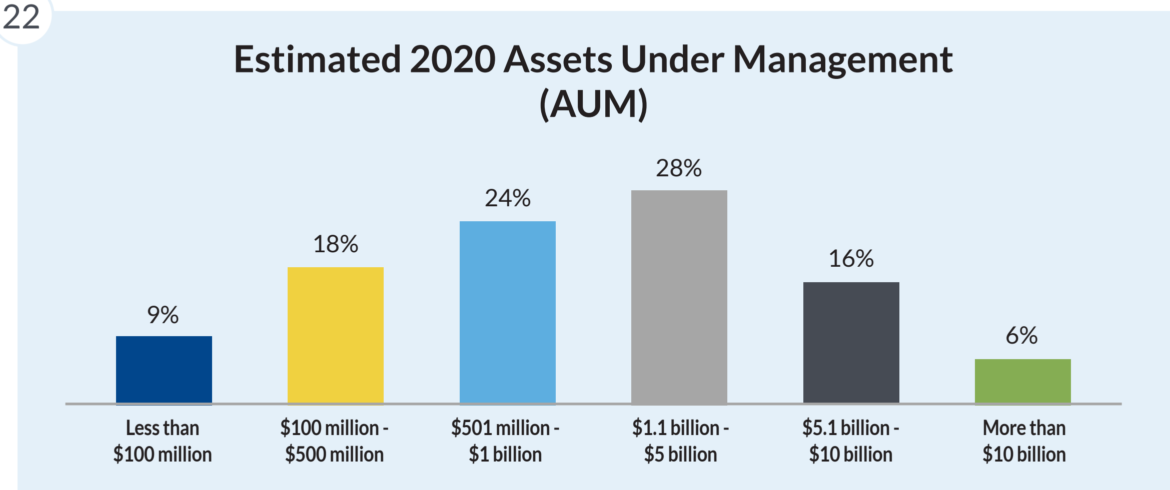

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About Katten

With more than 650 attorneys serving public and private companies, Katten is the firm of choice for clients seeking sophisticated, high-value legal services in the United States and abroad. Our collaborative, entrepreneurial culture leads to true partnerships with our clients. We understand and focus on our clients' business objectives and address their legal needs in a manner consistent with their "big picture." We have a reputation for being trusted advisors, and we demonstrate our value every day in the successful results we deliver.

About Katten's SPAC Practice

As SPACs continue to disrupt the traditional IPO market and more private companies successfully go public through SPAC mergers, Katten's multidisciplinary team of seasoned attorneys provides comprehensive counsel to clients in all aspects of SPAC transactions, including SPAC IPOs, third party investments and SPAC M&A transactions. Our strong securities and M&A experience allows us to take a leading role in the transaction, providing our clients with end-to-end counsel and building long-term relationships that allow us to address the ongoing demands and complexities of a public company transaction.

For more information or assistance with a SPAC transaction, please contact the following attorneys.

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