GigCapital™

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Comparing a Private-to-Public Equity *(PPE)*™ (Special Purpose Acquisition Company - SPAC) Transaction to a Private Equity (PE) Transaction

Why a *PPE* ™ Transaction Can Be a Superior Alternative to a PE Transaction

Late stage private companies that are in need of a cash infusion to support the ongoing growth of the business, either organically and/or through strategic acquisitions, typically rely on the traditional sources of debt, private equity (PE) or, in some cases, venture capital (VC) funding. While each of these sources can be useful financial tools, they all have their limitations and various pros and cons. This whitepaper focuses only on the PE financing alternative and compares it to the attributes of a *PPE*™ (SPAC) transaction. In many ways, a *PPE*™ transaction can offer significant benefits to the company, its current investors and its employees that are not present in a PE transaction.

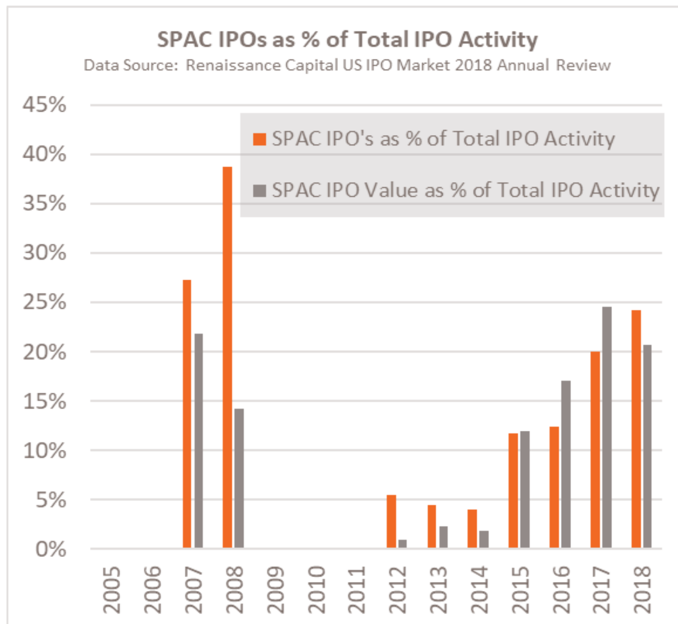
For those who are not familiar with the SPAC concept, it can basically be described as follows:

- The SPAC entity, sometimes referred to as a “blank check” company, is first formed by an investor group of experienced and qualified investors and business professionals.
- The SPAC then undergoes the typical initial public offering (IPO) process, whereby the company is listed on a major US exchange, receives a “ticker” on that exchange, raises capital and starts market trading. The entire process, exactly as in the standard IPO process, is tightly controlled and regulated by the SEC rules.
- Immediately after successful completion of the IPO process, the SPAC entity, which has a limited time duration before expiration and dissolving itself (typically 18-24 months), launches a search process to identify an appropriate target company, engages in negotiating a definitive agreement to merge with that company using the “reverse merger” mechanism and implements the merger, typically within 6-9 months after the execution of the definitive agreement.
- The result is that the target company becomes listed on a major US stock exchange under a new “ticker” symbol and has full access to the public capital market.
- Additionally, the company typically enjoys an infusion of cash at the closing of the combination.

Overall, this process provides the target company a faster and lower risk path to become a publicly listed entity with less disturbance to the on-going operations of the company and its strategic growth plans. Further, as compared to a traditional IPO process, the PPE/SPAC process significantly reduces the management time and attention required to achieve public company status. In many ways, the PPE process can be characterized as "an IPO in box".

Because of its effectiveness in bringing companies public, especially for fast growing, late-stage private companies that are resource limited by the nature and growth stage of the company, the SPAC process has gained significant interest from both the financial and enterprise communities as evidenced by the significant growth in the number of SPAC IPO offerings in recent years and their increasing portion of IPO activity. There has been an upward trend in SPAC IPOs since 2011. In 2018, SPACs accounted for 24% of all U.S. IPO transactions and 21% of IPO dollar value. As of October 2019, there are 90 active SPACs, which have raised total of about $18 billion. Of this group, 20 have already announced a combination target that they have been engaged with or have executed shared purchase agreements (SPA) with and expect to close the merger transaction shortly.

The listing of Virgin Galactic on the NYSE on October 28, 2019 via a combination with the Social-Capital SPAC is a prime example of a late stage private technology company leveraging a SPAC instead of continuing to finance the company through additional PE funding.



Why consider a SPAC transaction?

SPAC transactions typically address companies that are in late stage growth and have achieved financial parameters that support an Enterprise Values (EV) of $500 million or higher. As listed below, as compared to private equity funding, utilizing the SPAC process offers significant advantages to the target company.

- **Straightforward access to public capital markets.** The most obvious advantage of a SPAC is that it affords the target company a clear and more secure path to the public capital markets. A business combination with a SPAC guarantees a public listing (i.e. a "ticker") and avoids the limitations of the "IPO window", the risky pricing discovery process and the uncertainty in actually completing the offering that is associated with the traditional IPO process. One need only consider the number of IPOs that are "pulled" before completion to understand the value of this certainty. Since the SPAC has completed an IPO and is already traded as a public company, the combination, since it is a "reverse merger" controlled by the SPAC entity, has a minimum and clearly understood risk of failing. Hence, the public listing of the target company is secured with a very high level of confidence.

- **Ready access to public capital markets.** Post the combination, the company has access to two valuable forms of currency. Namely, cash on the balance sheet and the ability to issue equity instruments to obtain additional financing of various sorts. This flexibility is a tremendous advantage for the company as it can provide either cash or equity to be used in strategic transactions (i.e. M&A) and use equity sales to strengthen its balance sheet. In comparison to PE funding, using the public currency for raising funds for the company can usually be less dilutive and avoids the strictures typically put on management in PE funding transactions. These points become even more important and critical in market segments that are undergoing fast consolidation, where timely acquisitions are necessary to secure rapid growth of the company. The company's public currency can be deployed quickly and such transactions avoid the delays inherent in PE transactions.

- **Preferable exit vis-à-vis a PE transaction**. PE funds, on average, have a holding period of five to seven years in an active deal market and they will exit their investments before the fund liquidates. More typically, the fund will liquidate its investment in the company at the point of highest return on its investment, as is their legal remit, regardless of the impact on the company and its potential for future growth and development. This financially driven, "ROI first" approach largely disregards management's plans for the future of the business and what is best for the long term health of the business. In contrast, a SPAC transaction provides the company an opportunity to evaluate options and opportunities from both a short-term and long-term perspective, all under the control of the company's management team.

- **Retention of management control.** In a PE transaction, where the PE firm owns a controlling interest in the company, it is typical that the PE firm exerts significant control in the company's day-to-day operational management and strategic direction. Existing management loses much of its control and often times is simply replaced with new management hand-picked by the PE firm. In a SPAC transaction, the current management continues to lead the company and typically is supported by members of the SPAC sponsorship team who join the company as members of the Board of Directors or in other types of advisory positions. This type of involvement is more of an advisory and supportive partnership approach that is focused on the long-term stable and successful growth of the company to the benefit of all stakeholders, rather than highly focused on short-term ROI financial gains. This partnership theme is further motivated by the fact that the SPAC team, as significant shareholders in the business, see their financial upside based purely on the future enhanced equity value of the enterprise.

- **Moderate use of debt.** It is often the case that PE-owned companies assume higher, and oftentimes riskier, levels of debt. These high levels of debt are used not only to finance the business, but also to provide dividends to the PE firm. It is in the interest of PE firms to realize their investment return sooner rather than waiting for the target's potential, longer-term exit. Often PE-owned firms are over-leveraged which distresses the company's balance sheet, hurts its financial resilience and limits the company's future exit alternatives, all leading to a diminished value of the company.

- **Focus on long-term value creation.** The key fiduciary duty of management in the now publicly traded company that has been created through the combination with the SPAC, is to achieve stable financial performance and generate long-term value. This is in stark contrast to a short-term, ROI driven perspective that can lead to reduced opportunities for the business and sub-optimal long term value creation performance. A SPAC transaction provides a vehicle for the founders, investors and management of the company to continue to build the business and implement their long term vision for the enterprise and thus provide enhanced value creation for all stakeholders.

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The unique advantages of working with GigCapital

In addition to the general advantages of a SPAC transaction as noted above, the GigCapital team, which pioneered enhancing the traditional SPAC process with its *Private-to-Public Equity (PPE)*™ and *Mentor-Investor*™ approaches, provides a unique set of advantages and benefits to the target company. The GigCapital team is a very experienced group of entrepreneurs and executives comprised of former CEOs, senior-level corporate finance and SEC accounting executives, technical experts and industry renowned and respected thought-leaders that bring expertise and insights across all aspects of company management. It includes the complete spectrum of company leadership skills from product development and new product introduction (NPI), operations, sales and marketing, strategic planning and execution, private and public market financing, mergers and acquisitions, fund raising and wall-street connectivity, and global senior leadership level experience. As successful entrepreneurs and industry leading multinational corporation executives, the GigCapital partners provide a complete set of advisory expertise that may be needed by the target company as it enters the new stage of its growth as publicly traded companies.

Our unique approach to the SPAC transitional methodology is characterized by the following attributes:

- Ongoing support of the company through our *Mentor-Investor™* involvement that typically includes providing expert Board of Director membership and Advisory Board participation.

- Providing an “IPO in a box” solution, which fundamentally brings all the required practices, connections, methodology, processes and knowhow to the IPO process, based on years of experience and numerous successful IPO transactions.

- Guidance and mentoring to management as they enter the public capital markets and start their journey in this unique environment.

- Leveraging our extensive investment banking relationships to assist the company in subsequent financing activities and using the variety of available public company funding mechanisms, such as Private Investments in a Public Entity (PIPE), secondary offerings, preferred debt financing, secondary public offerings, etc.

- Extensive experience in M&A transactions as a method to enhance and accelerate the growth of the business.

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- Mentorship to senior management as they grow and develop the business and face the inevitable challenges associated with that growth. This mentorship focuses on enhancing the operation of the business and further unlocking the inherent value of the enterprise.

- Through our personal networks, provide introductions to industry leaders and executives on a worldwide basis, as well as investment banks, research analysts, institutional investors and debt lenders.

Our *PPE™ / M-I*™ approach not only provides the key benefit of quickly becoming a publicly traded company through the SPAC methodology, but additionally, it is based on forming a true partnership with the company leadership and owners by providing assistance and guidance to assist in the development of the long term potential of the business.