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SPAC Popularity Soaring in Healthcare

The popularity of *special purpose acquisition companies* (SPACs) has been soaring in recent years. There are 35 times as many SPACs operating in 2020 as in 2010, and these companies seem poised for greater exponential growth in the future.[1] While many experts are predicting a continued, rapid increase in SPACs, this article will also examine the factors that could possibly slow SPAC growth and diminish their future prospects.

SPACs are companies set up by investors that do not produce or sell their own products.[2] Instead, these companies, also termed "*blank check companies*," are set up solely to raise money through their *initial public offering* (IPO) and the future acquisition of other companies.[3] SPACs typically have a deadline of two years after the IPO to find an acquisition deal, and shareholders vote to approve these deals.[4] SPACs span several market areas, including biotechnology and healthcare; this article will review SPAC trends generally as well as healthcare SPACs in particular.

As noted above, overall SPAC activity has soared over the last decade. In 2010, there were seven SPAC IPOs with a little over $500 million in proceeds in the U.S., while in 2020, there were 248 SPAC IPOs with over $83 billion in proceeds.[5] While the number of total IPOs also increased during this period, the share of SPACs grew at a much faster rate, from 4% of total IPOs in 2010 to 55% in 2020.[6] Similarly, SPAC IPO proceeds made up only 1% of all IPO proceeds in 2010, but comprised 46% of all IPO proceeds a decade later.[7] Interestingly, unlike during the Great Recession, where the growth of SPAC IPOs plummeted from 66 in 2007 to 1 in 2009,[8] the number and share of SPAC IPOs have increased exponentially amid the current *public health emergency* (PHE) and resulting economic market volatility, from 59 SPACs in 2019 (28% of the total IPO market) to 248 in 2020 (55%), the first year of the PHE.[9]

SPACs in the healthcare sector saw similar booms in 2020, as well as in the first three months of 2021. Overall healthcare merger and acquisition activity is projected to increase in 2021,[10] and healthcare SPAC activity is expected to follow that trend. The number of healthcare-focused SPAC IPOs increased on a monthly basis throughout 2020, and peaked in October 2020 and again in January 2021.[11] Overall, there were 36 healthcare SPAC IPOs in 2020, with a total of $8.8 billion dollars raised, compared with only two healthcare SPAC IPOs in 2019.[12] As of March 2021, there were 53 SPACs actively searching for target companies in healthcare and life sciences.[13] In fact, the funds raised in the first quarter of 2021 alone is almost double the amount raised in all of 2020.[14] Healthcare, which comprises 20% of the U.S. *gross domestic product* (GDP), has been subject to significant disruption through the COVID-19 PHE.[15] Consequently, investors have looked to SPACs as a way to combat this market volatility and uncertainty, while pursuing promising new companies that can fill in the gaps in healthcare highlighted by COVID-19.[16]

Despite SPACs' status as arguably the most popular asset class in American equity markets, a study from the *Financial Times* found that the majority of SPACs organized between 2015 and 2019 were below the standard starting share sale price to the public of $10 per share.[17] This evidence consequently indicates that SPACs may be a risky investment as "*only half of them are shown to be value creating*."[18] SPACs also struggle with a reputation for fraud and other suspicious business dealings where financiers used the model to unload dubious companies onto unsuspecting investors.[19] Another emerging and growing concern is the strong incentives given to SPAC founders, also called sponsors.[20] SPAC founders are usually given a 20% share in the acquired company for free, as a way to compensate these individuals for their efforts in locating the target company. However, these terms can also lower the incentive to find quality businesses.[21]

Nevertheless, SPACs hold certain advantages over traditional IPOs, and some have seen wild success, with valuations for two of these companies (DraftKings and Nikola) currently over $10 billion.[22] The process for a business to create a traditional IPO is long and tedious.[23] SPACs have filled in the gap left by the worsening underpricing of IPOs to create an easier and faster process for start-ups to bring their business to market.[24] SPACs may present less risk for companies by allowing them to coordinate with the SPAC founder for a fixed amount of money and negotiated price.[25] This concept is essentially the difference between traditional IPOs and SPACs: IPOs involve companies looking for funders to invest in them, while SPACs are funders looking for a company in which to invest. Further, the one-on-one deals involved with SPACs may also be more conducive to the remote work environment brought about by the

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COVID-19 PHE than the typical meetings and "*roadshows*" that are part of traditional IPOs.[26] For pre-revenue companies, SPACs also hold the appeal of lower liability risk for mistakes or omissions to investors and more flexibility on future earnings projections.[27]

Accordingly, some experts have voiced concerns about the long-term viability and trends related to SPACs. Some speculate that the huge growth seen over the past year cannot continue at the same rate.[28] In the end, each SPAC that is formed is looking for a company to acquire. Too many SPACs in the market could mean that SPACs will begin to compete with each other on a greater scale for a limited number of start-ups available for acquisition.[29]

SPACs are often formed by experienced investors, high-profile CEOs, Wall Street professionals with private equity or hedge fund experience, or other major players, in order to grant them some legitimacy and attract investors.[30] Healthcare SPACs, for which biotechnology and health information technology (HIT) are two main areas of focus, are no exception to this general practice.[31] In fact, a study of HIT SPACs showed that few of these organizations' leaders had industry knowledge – rather than having healthcare experience, leaders were largely experts in investments and deal-making.[32] This may be a cause for concern in the long-term and calls into question the sustainability of healthcare (and other) SPACs. Evidence has shown that many SPACs have not performed well post-merger, and not having leadership that is familiar with the industry may continue this trend for healthcare SPACs.[33]

Despite the various potential drawbacks, the continued popularity of SPACs both in and outside of healthcare cannot be denied. One recent notable healthcare SPAC is Jackson Acquisition, whose board includes former Florida governor Jeb Bush and former *Centers for Medicare & Medicaid Services* (CMS) administrator Marilyn Tavenner.[34] This SPAC aims to raise $300 million through its coming IPO and is following the precedent of similar SPACs who are taking this opportunity to get in on a growing market, albeit with a board laden with healthcare industry experience. The willingness of high-profile individuals to join the boards of SPACs may lend further credibility to these organizations and present an additional transactional opportunity for healthcare start-ups and investors alike.

The future prospects and sustainability of SPACs are currently based solely on speculation, but evidence has also shown that as more high-profile figures and well-regarded companies get involved with SPACs, new entrants are more likely to choose to pursue this method over traditional IPOs.[35]

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