Yet Another $PSTH deep dive, part 2: scenario analysis and some sample trade

This is the fourth (and hopefully final!) piece I'm writing on PSTH. It should be read in conjunction with yesterday's "framing the opportunity" piece; however, my two prior posts (December's curios case of PSTH options and early Feb's implied vol / SPACsanity) are worth revisiting as well.

Why am I spending so much time and brain power on PSTH? Because I love to provide the disclosure that nothing on this site is investing advice, and options are very risky so please do your own work..... but also because I think the options chain reflects some very strange things and there is a lot of potential opportunity for event investors who structure the trade properly.

Anyway, today I want to do some scenario analysis for PSTH because I think it helps inform both why these trades are so interesting and how the super high implied volatility at PSTH can create really interest risk/rewards and isolate specific event bets.

Let me start be giving an example trade which might be my current favorite trade. As I write this (after market close Tuesday, Feb. 23), PSTH last traded for $29.31. The June $35 calls options last traded for $4.75, so if you buy the stock and sell those calls you're create the stock for ~$24.55. I think that's incredibly attractive. Why?

- Huge upside into deal: I personally think the market is likely to love whatever deal PSTH does. Perhaps this is just a function of the market we are in (where SPAC deal routinely rip 50%+), but PSTH is going to announce a deal and then Ackman is going to go on every business network with a very tight, very coherent pitch on why the deal is a huge winner; I think the pitch will resonate and provide a lot of support for the stock. If PSTH announces a deal and the stock trades to the moon, this buywrite gets >40% gross on your money (given this is a less than 4 month hold, the annualized to getting called on this is.... very attractive), so you get to play a large part of the upside.
    - That's a big reason I like the buywrite now more than selling puts. For example, a trade very closely related to this would be to sell the June $25 puts, which last went for $2.90. That would get you >11% gross on your notional money written and, if you were put the stock, create it for ~$22.10. Absolutely nothing wrong with that trade; in fact, I like it a lot! I just like the buywrite more because for a little more risk you get a lot more upside if the deal "pops" and I like that buywriting the stock lets you own / control the stock (which could be important in some super tail scenarios).
- Limited downside given redemption "put" ($20/share trust value for PSTH): the average SPAC takes ~100 days from deal announcement through deal completion. That would take us to June 8th. June options expire June 18, so this trade basically lines up option expiration with the earliest possible timeframe a merger could conclude (and that assumes PSTH announces a merger basically today). That time frame lining up is huge for this trade: as long as PSTH's deal hasn't closed, the shares can't trade much below $20 (I mean, they can trade anywhere in the short term, but arbs won't let it go below $20 for

long because they could just buy the stock and redeem into the deal for a very low risk arb return). In effect, you are risking $4.55 (your $24.55 net cost of shares down to the $20 put) to make >$10 ($35 call price less your $24.55 net).

- Remember that PSTH currently includes at least 2/9 of a tontine warrant. PSTH full warrants currently trade for $13.70/warrant, so PSTH's embedded tontine warrants are worth ~$3.05/share. If you deduct the warrant value and the call premium, you're effectively creating the stock at ~$21.35/share, or about 7% over trust value. That's a little bit of a stretch, as the warrants value very much depends on the stock value so you get super circular, but I do like the shorthand "buywriting this and striping the warrants away has effectively created the stock at a slight premium to trust".
- That "creating at only a slight premium to trust" is important. This is a controlled speculation; I think the market is going to go bonkers for any deal PSTH announces, but this is still a SPAC subject to winners' curse and dilute from the sponsor's promo (though materially less for PSTH than the average SPAC!). The whole thought here is to use the call premium to get your call basis close to trust so you're only risking a small % in order to make money if the market loves PSTH's deal. Remember, even without knowing the deal, PSTH is trading for a large premium to trust, so the market already thinks it will love PSTH's deal. You're just betting that the market is directionally correct!
- The average SPAC deal took 100 days from deal announcement to completion in 2020. I tend to think that timeframe will lengthen in 2021 because they huge wave of SPAC deals and IPOs means the

SEC is just jammed up reviewing documents. That would be great news for anyone selling options, as it means the redemption put is in place for longer.

- Optionality if PSTH doesn't announce a deal: while I think it's likely PSTH announces a deal between now and June, there's no guarantee that they do. Time is your friend in this trade; if PSTH doesn't announce a deal, the option's time value will decay and you pick that up. You even get exposure to the absolute dream scenario where Pershing announces a deal the day after these options expire and the stock goes to the moon.
- More optionality if the options chain doesn't adjust: I discussed the "reverse DVMT" in yesterday's piece, so I won't dive in here. But in the odd scenario where the options chain does not adjust on deal close, buywriting the stock gives you exposure to that bonanza scenario, while selling a put would not.
    - It's not super applicable to buywriting the Junes versus buying some of the longer dated options, as the June options are short term enough that whoever wrote them would simply exercise before the deal closed if they weren't going to adjust, but again.... free optionality to some strange event.

Anyway, that's my favorite trade for PSTH right now, but there are plenty of others interesting trades that can isolate a variety of variables. Again, all of this is possible because PSTH is such a unique beast: a cash shell searching for a deal that has multiple options embedded into it (from the tontine warrants on the upside and from the redemption put on the downside).

The three main variables to consider when constructing a PSTH trade are

1. Market risk: what happens if the market blows up or continues to rip higher?
2. What type of deal does PSTH announce and how does the market respond?
3. When does PSTH strike a deal?

There are probably other variables, but I think those are the main three. And they are all somewhat intertwined.

For example, consider a market crash. Let's say we have some type of crazy event that causes the market to instantly crash 30%. How does that affect PSTH?

Well, it really depends on the timing. If PSTH announces a deal tmr and this huge crash occurs in three or four months right as the deal is wrapping up, PSTH probably drops like a rock.

But what if the crash happened tomorrow? PSTH would probably trade closer towards trust value.... but they might end up getting a better deal on whatever company they buy. In fact, if we had world in crisis / semi-crisis scenario that likely goes along with a 30% crash, PSTH might be tempted to reach out to a bunch of companies that had already rejected them and see if they were interested in revisiting a merger that would give them access to up to $7B in cash. So, for example, Bloomberg apparently rejected PSTH last year; maybe a real stressed scenario makes them revisit the offer.

Of course, that crash could cause a PSTH deal to take even longer. Let's say Ackman is currently in decently late talks to merge with some company, and they are targeting an early March signing date, and this hypothetical crash happens tomorrow (Feb. 24). Ackman might want to recut the deal to a lower valuation to reflect a stressed market. Or he might look at the stressed market and say "some of those targets that turned me down are available now" (a la the Bloomberg example above). Either of those would extend the timeline for PSTH announcing a merger (and thus a merger closing).

So yeah, a market crash would effect PSTH. But how it would effect PSTH would vary wildly depending on where PSTH is in their deal process. And because the market crash could alter when PSTH announces / concludes a deal, depending on which PSTH options we're talking about a market crash could actually be hugely beneficial for the options. For example, consider selling the September $20 puts (currently trading for ~$1.40/share). If PSTH announced a deal tomorrow, closed in June, and then the market crashed in July, that would be awful for those puts. The $20 redemption put goes away once the deal closes, so that stock would be trading on its own fundamental value. I think it would take a really large market crash for PSTH to go below trust value even post deal, but it could happen and this is about the worst case scenario for those puts. Alternatively, if PSTH hasn't announced a deal and the market crashes in the middle of next month, it's a bonanza for those puts, because, assuming PSTH will be going back to any targets to ask for valuation cuts or maybe circling back with old targets, that crash extends the timeline to closing a deal, which means it's dramatically less likely PSTH could close a deal (and thus lose the redemption puts) before the September puts expire.

Anyway, those are the things to keep in mind when thinking through different options trades. And, assuming you are keeping those in mind, I want to talk through some different possible scenarios and the best ways to play them.

Early, I mentioned I like buywriting the June $35 calls, and I mention some of the reasons for it. Let me give you some of my theories / thoughts on PSTH, and why I think the buywrite sets up well for them.

- Theory #1: Ackman has trouble finding a deal / a deal takes longer than most expect : there's just so much liquidity out there that I think it's going to be difficult to lock down a unicorn target.
    - Why this plays into the buywrite hands: you're writing the calls at a level low enough that you're getting paid a meaningful amount of premium, so if there's no deal the premium you keep will be meaningful and go a long way towards getting your cost basis close to trust
- Theory #2: Despite those troubles, the market loves whatever deal is announced
    - Why this plays into the buywrite hands: the calls are deep enough out of the money that you still get substantial upside exposure
- Theory #3: once announced, deal takes a little longer than normal to close given size and SEC backlog
    - Why this plays into the buywrite hands: a longer time line means more protection from the put at trust value.

Anyway, that's why I like the trade the way I set it up. While I'm here, let me provide a few more hypothetical trades (which are not investing advice!) that might fit a few other theories one could have on PSTH. Note that a core element of all of these trades are safety; if you're an experienced options trader, I do think there are some interesting set ups that could be made with put spreads or call spreads, but intellectually I just prefer playing around with ways to get access to the stock while maintaining the optinality of the redemption put value

1. Theory: SPAC market is overheated; PSTH likely to perform better than most but it's do for a correction
    - Suggested trade: buy-write the January 2022 $30 (last trade: $9.30, for a net cost of the stock of $20).
    - Reasoning: You're creating the stock for trust value. If there's real trouble in the SPAC market, deals might get delayed or maybe PSTH has trouble getting its vote through. This lets you create the stock at trust, and if it's called away from you your net return will be >50%.
2. Theory: Market will love just about any PSTH deal.... except for Subway, and you're worried it'll be Subway
    - Suggested trade: buy-write the January 2023 $45 (last trade: $10.80, for a net cost of the stock of $18.50).
    - Reasoning: You're creating the stock for well under trust value. If Ackman announces a killer deal, you get tons of upside. If Ackman announces for Subway.... well, you've created the stock below trust. Between the tontine warrants and the huge call premium, you'll be fine (probably).
3. Theory: There are more SPACs and competitors out there than Ackman ever thought possible; he's going to really struggle to find a deal
    - Suggested trade: sell September $22.50 puts (last trade: $2.70; net cost of stock if put to you: $19.80)
    - Reasoning: In general, I'd prefer to buywrite the

equity, as I think Ackman will find a deal and the market will really like it. But this trade is a nice bet on Ackman struggling to find a deal. You create the stock for below trust value if it's put to you, and if you think he struggles to find a deal the trust putwon't be going away anytime soon.

Anyway, this has been a very different post/series than I normally do; it felt a little strange to write to be honest. Bottom line: PSTH is a cash shell trading at a 50% premium; that seems pretty crazy, but given the unique tontine structure and the huge implied volatility, I think there are ways to play PSTH that brings your cost basis closer to trust value and exposes you to significant potential upside if/when a deal is announced (and assuming the market likes it, which I think it will).

Three other things before I wrap up:

First, I saw two above market PIPEs yesterday (Lucid was the second); these are the first above markets PIPEs I'm aware of. Ackman is a skilled negotiator; so while I don't think PSTH will need a PIPE attached to its deal (given its size + forward purchase agreement) if they do I wouldn't be surprised if the PIPE was an above market deal. If that happened, it would be generally good for anyone who had sold optionality (an above market PIPE deleverages the company and should reduce volatility).

Second, and related to the above market PIPE, here's a curious thought: PSH has a $3B forward commitment to invest into PSTH at trust value. Could they monetize that commitment? I.e.

could they just sell $1b of their forward commitment to someone for a premium ("give us $250m for the right to buy $1B of PSTH at trust; with PSTH trading at $30 and likely to go up on deal announcement, you're already in the money by $250m!). It'd be really interesting if we started to see sponsors monetize their forward commitment.

Third, CCIV's stock got hammered after announcing their Lucid deal last night. I found the commentary around the stock drop really curious: yes, CCIV fell from ~$60/share to ~$35/share, but people were treating it like the merger was a huge failure. It seems like a pretty classic case of buy the rumor, sell the news combined with some speculative excess. I mean, $35/share is 3.5x trust value and one of the best returns for a SPAC ever. The stock started the year at $10/share; if I had told you that they would be priced at $35/share the day after announcing a deal you probably wouldn't have believed me at the start of the year! Still, speculative manias can pop for strange reasons, and seeing the most hyped SPAC deal drop almost 50% on announcement is as good a reason for a bubble to pop as any.

Ok, that's it for PSTH. Again, the series was a little different than I normally write about, but I just don't think a lot of people have thought through all of the angles of this deal and how there is potential alpha in the unique structure. I'm hugely bullish on the opportunity here, and I'm looking forward to writing an update after they announce a deal (hopefully in late June, after the bulk of my options have expired!).